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Husson University
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Husson University, Bangor, ME.
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PUBLICATION LOCATIONS


The Journal is listed in Cabell’s (Management) Directory.

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DATA TRANSFERS FROM THE EU TO THE U.S.
AFTER SCHREMS

by Carter Manny∗

I. INTRODUCTION

Transfers of personal information from the European Union to the all other countries must comply with the provisions of the EU’s Data Protection Directive which provides a framework for national implementing legislation in each of the 28 Member States.1 Transfers are permitted only when the information is going to a country with an “adequate” level of privacy protection2 or when one of a very limited number of exceptions is available.3 Adequate privacy protection can exist by virtue of a destination country’s law or as a result of commitments to protect the privacy of the data made by the government of that country through negotiations with the European Commission.4 Only a few countries have qualified as meeting the adequacy standard.5 Europe and the U.S. have very different systems for protecting privacy. The European approach relies on

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2 See id. at Art. 25(1).
3 See id. at Art. 26.
4 See id. at Art. 26(6).
5 As of March 2016, only six countries (Switzerland, Canada, Argentina, Israel, Uruguay and New Zealand), the Principality of Andorra, and four dependencies (Guernsey, Jersey, the Isle of Man and the Faroe Islands) have been found by the Commission to provide adequate protection for personal data. See http://www.ec.europa.eu/justice/data-protection/document/international-transfers/adequacy/index_en.htm (last visited Mar. 24, 2016).
comprehensive privacy legislation administered by dedicated data protection agencies in the Member States. The U.S. system, however, is a patchwork of sector-specific state and federal laws enforced by a large number of governmental agencies, many of which have privacy law enforcement as only one of many areas of responsibility.\textsuperscript{6}

Because the systems in the EU and U.S. are so different, the U.S. could not expect to qualify for a general adequacy determination based upon its law. Consequently, the U.S. sought to obtain a more narrowly-focused adequacy determination through negotiating with the European Commission to assemble a set of privacy commitments that could be adopted by U.S. businesses. The negotiations were successfully concluded in the summer of 2000, resulting in a system known as Safe Harbor.\textsuperscript{7} The Commission determined that a combination of privacy commitments made by U.S. businesses joining Safe Harbor, combined with system of enforcement of those commitments, would provide adequate privacy protection, thus enabling those businesses to receive personal information from Europe, consistent with EU law.\textsuperscript{8} During the next fifteen years, over 4000 U.S. businesses of all sizes joined Safe Harbor, using it as a lawful basis to receive data transfers.\textsuperscript{9} During that time, however, Safe Harbor was criticized as affording insufficient protection.\textsuperscript{10} Following


\textsuperscript{9} See U.S. – EU Safe Harbor List, available at http://safeharbor.export.gov/list.aspx (last visited Mar. 24, 2016). The list well over 4000 entries, but some organizations are noted as being “not current.” Many large businesses are Safe Harbor participants, including Google, Facebook, Yahoo, Microsoft, Apple, Proctor & Gamble, Exxon-Mobil, Ford Motor Company, Chrysler, General Motors, General Mills, Genzyme, Georgia Pacific and Hewlett Packard.

the revelations by U.S. government contractor Edward Snowden that massive quantities of personal information of Europeans transferred to the U.S. had been subjected to surveillance by U.S. government intelligence, criticism of Safe Harbor intensified.\footnote{11} In March 2014, the European Parliament recommended that Safe Harbor be terminated.\footnote{12}

It was the judicial branch of the EU, however, which ended the data transfer arrangement. In October, 2015, the European Court of Justice (ECJ) found Safe Harbor to be invalid under the Data Protection Directive and the EU Charter of Fundamental Rights and Freedoms.\footnote{13} The Court noted two errors in the European Commission’s approval of Safe Harbor: (1) failure to conclude that the country of the United States, as opposed to the provisions of the Safe Harbor documents themselves, provided privacy protection that was “essentially equivalent” to protection in Europe, and (2) improper limitation of the ability of data protection authorities in the EU Member States to investigate complaints relating to data transferred to Safe Harbor participants in the U.S. Although the ECJ did not examine the content of the Safe Harbor’s provisions,\footnote{14} it made a number of observations about deficiencies in the Safe Harbor system and therefore provided guidance for formulating a new EU – US data transfer agreement. Those observations largely involve the need for limitations on U.S. governmental access to, and use and storage of, data transferred to U.S. businesses under an exception for national security, public interest and law enforcement.\footnote{15} The Court also observed that EU data subjects must have sufficient rights of administrative and judicial


\footnote{14} See id. at ¶ 98.

\footnote{15} See id. at ¶¶ 90 – 94.
redress allowing them access to, and rectification and deletion of, their data in the U.S.\textsuperscript{16}

Following the Court’s decision, former Safe Harbor participants were faced with the difficult task of finding lawful ways to continue receiving personal information from Europe.\textsuperscript{17} In the meantime, the European Commission and officials of the U.S. government worked on a new data transfer agreement to replace Safe Harbor.\textsuperscript{18} The negotiations produced a set of documents from the U.S. government agencies published in February, 2016, known as the proposed EU – U.S. Privacy Shield. The documents contain a strengthened version of privacy commitments and enforcement provisions, together with assurances relating to U.S. government intelligence gathering activities.\textsuperscript{19} During that same month, the Judicial Redress Act was signed into law, affording non-U.S. persons, including EU residents, limited rights to use U.S. courts to assert privacy rights against U.S. governmental institutions.\textsuperscript{20}

This article examines deficiencies in Safe Harbor as identified by the European Court of Justice and the European Commission, and U.S. efforts to correct those deficiencies in the proposed Privacy Shield and the Judicial Redress Act, as of March, 2016. European officials, including the organization of national data protection commissioners in the 28 Member States known as the Article 29 Working Party, as well as the European Parliament, have been reviewing the Privacy Shield.\textsuperscript{21} Depending upon their reactions, the Commission may be able to implement a decision that the Privacy Shield enables the U.S. to provide adequate privacy protection for data transfers consistent with

\textsuperscript{16} See id. at ¶ 95.

\textsuperscript{17} See, e.g., Joe Mont, \textit{Safe Harbor Squashed, What’s Next?}, 12 \textit{Compliance Week}, Nov. 2015, at 8 (considering alternatives available to businesses following invalidation of Safe Harbor.)


\textsuperscript{19} See EU – U.S. Privacy Shield, available at https://www.commerce.gov/sites/commerce.gov/files/media/files/2016/16eu_us_privacy_shield_full_text.pdf.pdf (last visited Mar. 1, 2016). The Privacy Shield consists of documents from the U.S. Department of Commerce, the Federal Trade Commission, the State Department, the Department of Transportation, the Justice Department and the Office of the Director of National Intelligence.


Data Transfers from the EU to the U.S.

the Data Protection Directive and the EU Charter of Fundamental Rights. Following the analysis of the Privacy Shield, the article briefly discusses other lawful data transfer possibilities for U.S. businesses, independent of the Privacy Shield.

II. INVALIDATION OF SAFE HARBOR BY THE EUROPEAN COURT OF JUSTICE

A. Background of the Case

In June, 2013, shortly after Edward Snowden’s revelations about mass surveillance of online information by U.S. government intelligence authorities became the subject of news reports around the world, Austrian resident Maximillian Schrems contacted the Irish Data Protection Commissioner to request action against Facebook’s Irish subsidiary, Facebook Ireland. Any registered user of Facebook in Europe enters an agreement with Facebook Ireland, which transfers some or all of the user’s personal data to computer servers in the U.S. owned by Facebook, which was a member of Safe Harbor. Mr. Schrems alleged that because U.S. intelligence authorities were reportedly using personal data of Facebook users, the Safe Harbor system failed to ensure adequate privacy protection. Accordingly, he asked the Commissioner to exercise his statutory powers and prohibit Facebook Ireland from transferring Mr. Schrems’s data to the U.S. The Commissioner refused, because his power was limited by the European Commission’s determination in 2000 that Safe Harbor provided adequate privacy protection. Mr. Schrems then brought an action against the Irish Data Protection Commissioner in the Irish High Court which referred questions of EU law to the European Court of Justice (the “ECJ.”)

22 See id.
24 See id.
25 See id. at ¶ 28.
26 See id.
27 See id. at ¶ 29.
28 See id. at ¶ 30. Art. 3(1) of Commission Decision 2000/520, supra note 8, permits DPAs to suspend data transfers when a U.S. government agency or “independent recourse mechanism” has determined that a Safe Harbor organization is violating the Safe Harbor Principles. A DPA may also suspend data transfers when four factors are present: (1) substantial likelihood of a violation of the Principles, (2) reasonable belief that an enforcement mechanism will not settle the case in a timely manner, (3) a continuing transfer would create an imminent risk of grave harm, and (4) one or more DPAs have made reasonable efforts to provide the Safe Harbor organization with notice
B. Flaws in the European Commission’s Decision to Approve Safe Harbor

1. Limits on Investigative Powers of Data Protection Authorities

In rejecting Mr. Schrems’s complaint, the Irish Data Protection Commissioner took the position that the European Commission’s decision approving the Safe Harbor in 2000 precluded any data protection authority in a Member State from considering whether privacy protection in the U.S. might not be adequate. The ECJ, however, concluded that neither the EU Charter of Fundamental Rights, nor the Data Protection Directive, permit the Commission in an adequacy determination to limit the ability of a data protection authority to review an international data transfer.

2. Failure to Determine That the U.S. Ensures Adequate Privacy Protection

The Court carefully analyzed the requirements for an adequacy decision by interpreting provisions in the Data Protection Directive. It noted that the concept of adequate level of protection is not defined anywhere in the Directive, and that the Directive specifies that the Commission’s decision must find “that a third country ensures an adequate level of protection . . . for the protection of the private lives . . . of individuals.” The Court interpreted that language, together with the right of data protection in Article 8 of the Charter, as requiring the third country to ensure a level of protection that is “essentially equivalent” to what is provided in the EU by the Directive and the Charter. Without making its own determination of whether the content of the Safe Harbor Principles ensured an adequate level of protection, the court focused on the precise language used by the Commission in 2000 when approving Safe Harbor and noted that the

and an opportunity to respond.


31 See Directive, supra note 1, at Art. 28.


33 See id. at ¶ 70.

34 See Directive, supra note 1, at Art. 25(6).

Commission had not determined whether the United States as a country ensures an adequate level of protection, by reason of its domestic law or international commitments, as required by the Directive.\textsuperscript{36} Although the Court never precisely states what the Commission actually determined, the language in the Commission’s decision states that “the ‘Safe Harbor Privacy Principles’ . . . are considered to ensure an adequate level of protection for personal data transferred from the Community to organisations (sic) established in the United States . . . .”\textsuperscript{37} In other words, the Commission appears to have erred by finding that the provisions of an agreement, rather than a country, ensured an adequate level of privacy protection. Despite the emphasis on the precise language of the Directive and the Commission’s decision, the Court elaborated on how Safe Harbor enabled violations of rights protected by EU law, especially with respect to surveillance by U.S. intelligence authorities. The analysis provided by the ECJ is especially important as guidance for what a replacement for Safe Harbor must include.

\textbf{C. Observations On How EU Rights Must be Protected}

1. Surveillance by U.S. Government

The Court began its analysis by considering the Safe Harbor’s language stating that its principles may be limited to the extent necessary to meet national security, public interest or law enforcement requirements, and that non-compliance with the principles is limited to the extent necessary to meet overriding legitimate interests established by statute, regulation or case law.\textsuperscript{38} The Court also noted that U.S. government agencies were not required to comply with Safe Harbor Principles.\textsuperscript{39} Accordingly, the ECJ concluded that national security, public interest and law enforcement requirements take priority over Safe Harbor privacy protections.\textsuperscript{40} Thus, the Commission’s decision to approve Safe Harbor and facilitate lawful transfers of personal data from Europe to the U.S. enables interference with EU privacy rights, to the extent that U.S. governmental authorities can gain access for national security, public interest and law enforcement purposes.\textsuperscript{41} The EJC noted that the Commission

\textsuperscript{36} See id. at ¶¶ 83, 96, 97; Directive, supra note 1, at Art. 25(6).
\textsuperscript{37} See Commission Decision 2000/520, supra note 8, at Art. 1(1).
\textsuperscript{39} See id. at ¶ 82.
\textsuperscript{40} See id. at ¶ 86.
\textsuperscript{41} See id. at ¶ 87.
agreed with the Court’s assessment in a report published in November, 2013, which stated that U.S. intelligence authorities were able to access personal data transferred pursuant to Safe Harbor and to process the information in ways incompatible with the purposes for which the data were transferred, beyond what was “strictly necessary and proportionate” for the protection of national security.\footnote{See id. at ¶ 90.} The Court emphasized that under its case law, EU legislation involving interference with privacy rights guaranteed by the EU Charter must contain “clear and precise rules” governing the scope and application of the legislation and “minimum safeguards” protecting against risk of abuse, and unlawful access and use of the data.\footnote{See id. at ¶ 91.} Case law also requires that any exceptions and limitations to privacy rights apply only in so far as is “strictly necessary.”\footnote{See id. at ¶ 92.} The court then explained that under these standards, legislation that authorizes on a general basis the storage of all personal data transferred from the EU to the U.S. without certain limitations would fail the “strictly necessary” test. Those limitations must include: (1) differentiation, limitation or exception made in light of the objective pursued, and (2) an objective criterion by which to determine the limits of access to the data and its subsequent use, “for purposes which are specific, strictly restricted and capable of justifying interference which both access to that data and its use entail.”\footnote{See id. at ¶ 93.} The implication of the Court’s observations is that the Commission would need to determine that U.S. law and international commitments meet these standards before it could properly approve any future data transfer arrangement.

2. Rights of Redress

The EJC also provided guidance on EU rights of redress. It cited Article 47 of the EU Charter as guaranteeing a right to an effective remedy before a tribunal.\footnote{See id. at ¶ 95.} Art. 47 of the Charter provides: “Everyone whose rights and freedoms guaranteed by the law of the Union are violated has the right to an effective remedy before a tribunal in compliance with the conditions laid down in this Article.” See Charter of Fundamental Rights, supra note 30, Art. 47, 2000 O.J. C 364 at 20.

Accordingly, the Commission would need to determine that U.S. law and international commitments provide these rights before it could properly approve any future data transfer arrangement.

3. Compliance Monitoring and Enforcement

Although the Court did not examine the content of the Safe Harbor monitoring and enforcement mechanisms, it did include general analysis of these issues. It acknowledged that a system of self-certification is not in itself contrary to the Directive, but that the reliability of such a system is founded on effective detection and supervision mechanisms.\footnote{See id. at ¶ 81.} Those measures should enable any infringement of privacy rights to be identified and punished in practice.\footnote{See id.} Presumably, the Commission should explicitly address these issues when approving any future data transfer arrangement.

III. THE PRIVACY SHIELD AND STANDARDS STATED IN SCHREMS

A. Overview of the Privacy Shield

In February, 2016, the U.S. Commerce Department released a set of documents from the State Department, Federal Trade Commission, Department of Transportation, the Office of the Director of National Intelligence, and the Justice Department, as well as the Commerce Department, which together constitute the Privacy Shield.\footnote{See EU – U.S. Privacy Shield, available at https://www.commerce.gov/sites/commerce.gov/files/media/files/2016/eu_us_privacy_shield_full_text.pdf.pdf (last visited Mar. 1, 2016).} The Commerce Department documents set forth privacy principles, a self-certification mechanism for organizations to join and maintain participation in the Privacy Shield system and an alternative dispute resolution enforcement system, all of which are strengthened versions of similar provisions in Safe Harbor.\footnote{See EU – U.S. Privacy Shield Framework Principles Issued by the U.S. Department of Commerce contained within the EU – U.S. Privacy Shield, available at https://www.commerce.gov/sites/commerce.gov/files/media/files/2016/eu_us_privacy_shield_full_text.pdf.pdf (last visited Mar. 1, 2016).} In addition, there is a voluntary system for arbitration of disputes before a new Privacy Shield Panel in the U.S. in the event that other dispute resolution mechanisms are not successful.\footnote{See Arbitral Model contained within the EU – U.S. Privacy Shield, available at https://www.commerce.gov/sites/commerce.gov/files/media/files/2016/eu_us_privacy_shield_full_text.pdf.pdf (last visited Mar. 1, 2016).} Officials from the Federal Trade Commission\footnote{See letter dated Feb. 23, 2016, from U.S. Secretary of Commerce Penny Pritzker to
Department of Transportation\textsuperscript{54} describe each agency’s enforcement system as it relates to the Privacy Shield. Several documents relate to limitations on U.S. Government access to data transferred from Europe. These include letters from the officials with the Office of the Director of National Intelligence\textsuperscript{55} and Justice Department\textsuperscript{56} which set forth limits on collection and use of information for national security and law enforcement. In addition, the State Department provided a document describing a new ombudsperson mechanism to review complaints from the EU regarding access by U.S. intelligence services to personal information transferred from the EU to the U.S. under the Privacy Shield and other transfer mechanisms.\textsuperscript{57} That same month, the European Commission released a draft adequacy determination evaluating the representations in the Privacy Shield and concluding that the United States ensures an adequate level of protection to U.S. organizations which join the Privacy Shield.\textsuperscript{58} The following analysis will consider the contents of those documents in light of standards articulated by the European Court of Justice in \textit{Schrems}.


B. Surveillance by U.S. Government

The central feature of the ECJ’s decision in Schrems was that EU privacy rights were being violated by U.S. intelligence services obtaining access to personal data transferred to U.S. organizations, including Facebook and Google, pursuant to Safe Harbor. The ability of the Privacy Shield to protect against these violations depends largely on the effectiveness of limits on U.S. intelligence activities as outlined in the letter from the Office of the Director of National Intelligence (“ODNI.”) Some of those limits were imposed after 2013 when the information provided by Edward Snowden became public and after the Commission issued its report criticizing Safe Harbor. There are three major sources of limitations: (1) Presidential Privacy Directive 28, adopted in January, 2014, (2) limits in the 2008 Amendments of the Foreign Intelligence Surveillance Act, and (3) the USA Freedom Act signed into law in June, 2015.

Presidential Privacy Directive 28 (“PPD-28”) sets forth limits on collection, use, dissemination and retention of signals intelligence. Many of the limitations are expressed in general language. For example, PPD-28 states that privacy and civil liberties shall be considerations in planning intelligence activities, that collection is limited to foreign intelligence or counterintelligence purposes, that foreign private commercial information shall be collected only to protect national security, and that intelligence activities shall be “tailored as necessary.” Language limiting bulk collection is also relatively general. Bulk collection is limited only for the purposes of detecting and countering: (1) espionage and other activities directed by foreign powers, (2) threats from terrorism, (3) threats involving weapons of mass destruction, (4) cybersecurity threats, (5) threats to U.S. or allied personnel including the military and (6) a very broad category of “transnational criminal threats.” PPD-28 has a general provision stating that all persons should be treated with dignity and respect, regardless of their nationality or where they reside. There are provisions calling for minimization of dissemination and retention of information, with some extension of the same protections to data of

62 See PPD-28, supra note 59.
63 See id. at § 1.
64 See id. at § 2.
65 See id. at § 4.
foreigners as are extended to U.S. persons.\textsuperscript{66} The letter from the representative of ODNI also lists numerous types of review and oversight of intelligence activity. His analysis of PPD-28 and other provisions of law and policy governing signals intelligence, including classified information, support the conclusion that privacy protections for all persons are provided, regardless of nationality.\textsuperscript{67}

The representative from ODNI asserted in the letter that collection of data under Section 702 of the Foreign Intelligence Surveillance Act (“FISA”) is narrowly focused on individually identified legitimate targets.\textsuperscript{68} Surveillance is subject to both judicial supervision\textsuperscript{69} and substantial review and oversight within both the Executive Branch and Congress.\textsuperscript{70}

The USA FREEDOM Act prohibits bulk collection of data pursuant to various provisions of the Foreign Intelligence Surveillance Act of though a type of administrative subpoena issued by the FBI, known as a National Security Letter.\textsuperscript{71} The letter from the representative of ODNI emphasized that the Act provides for public disclosures on information regarding FISA data collection and National Security Letter requests.\textsuperscript{72} The letter concludes that the USA FREEDOM Act provides clear evidence of the effort of the U.S. to put privacy, civil liberties and transparency at the forefront of its intelligence practices.\textsuperscript{73}

The European Commission’s Draft Adequacy Decision includes a detailed analysis of U.S. law governing access and use of data for national security purposes.\textsuperscript{74} The analysis includes a thorough review of the laws cited in the letter of the representative of ODNI. Although the Commission appears to have conducted its own analysis of U.S. law, it does occasionally rely on representations contained in the ODNI representative’s letter. For example, the Commission mentions the representative’s explicit assurance that the U.S. intelligence community does not engage in indiscriminate surveillance of anyone, including ordinary European citizens.\textsuperscript{75} The Commission concludes that the U.S. legal framework has been significantly strengthened

\textsuperscript{66} See id.
\textsuperscript{67} See ODNI Letter, supra note 55, at I (e).
\textsuperscript{68} See id. at II.
\textsuperscript{69} See 50 U.S.C. § 1881a.
\textsuperscript{70} See ODNI Letter, supra note 55, at II. (Page 12 of the letter lists reports to Congress, including reports by the Attorney General and Director of National Intelligence.)
\textsuperscript{71} See id. at II.
\textsuperscript{72} See id. at III.
\textsuperscript{73} See id.
\textsuperscript{74} See Draft Adequacy Decision, supra note 58, at ¶¶55 – 105.
\textsuperscript{75} See id. at ¶ 69.
since November, 2013, when it issued the report cited by the ECJ in Schrems as evidence that U.S. intelligence activities were violating privacy rights of people whose data had been transferred to the U.S. using Safe Harbor. The Commission states that its analysis shows that U.S. law contains clear limitations on the access and use of data for national security purposes as well as sufficient safeguards protecting against unlawful interference and risk of abuse. The Draft Adequacy Decision thoroughly examines provisions under U.S. law providing for oversight of U.S. intelligence activities by civil liberties officers and inspectors general within intelligence agencies, independent oversight boards, the Foreign Intelligence Surveillance Court and committees of the U.S. Congress. It also lists rights of redress available to EU data subjects under U.S. law, including use of the newly created Privacy Shield Ombudsman. Based on the analysis, the Commission concluded that there are rules designed to limit interference for national security purposes with EU privacy rights to what is “strictly necessary to achieve the legitimate objective in question,” thus satisfying the strict necessity standard in Schrems.

C. Right of Redress

In Schrems, the European Court of Justice stated that under Article 47 of the Charter, the right to an effective remedy before a tribunal means that there must be effective judicial review designed to ensure compliance with EU law. Thus, there must be effective legal remedies enabling a data subject to have access to the data, and to obtain rectification or deletion of that data. Such rights of access, rectification and deletion of data held be a Privacy Shield organization are provided in the Privacy Shield Principles and can be enforced through various mechanisms including use of an independent dispute resolution body, a process conducted by the FTC, and binding arbitration before a Privacy Shield Panel. The Commission’s Draft Adequacy Decision concludes that these recourse mechanisms enable violations to be

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77 See Draft Adequacy Decision, supra note 58, at ¶ 55.
78 See id. at ¶¶ 76 – 94.
79 See id. at ¶¶ 95 – 104.
80 See id. at ¶ 75.
82 See id. at ¶ 95.
“identified and punished in practice and offer legal remedies to the data subject to gain access to personal data relating to him and, eventually, to obtain the rectification or erasure of such data.” While the recourse mechanisms arguably comply with the term “tribunal” used in Article 47 of the Charter, it is not clear that they satisfy the ECJ’s standard of “judicial” review, which implies use of a court.

With respect to alleged violations of EU privacy rights related to U.S. intelligence gathering for national security purposes, the Commission’s Draft Adequacy Decision provides a detailed analysis of mechanisms for people in the EU to seek redress. These include civil actions against the U.S. government in U.S. courts under a number of statutes. In addition, the Commission outlines how the Privacy Shield Ombudsperson Mechanism contributes to ensuring individual redress. Implicit in the Commission’s determination that the U.S. ensures effective legal protection against privacy violations by its intelligence authorities is the conclusion that rights of redress in the U.S. available to EU residents are sufficient to meet the requirements of the ECJ in Schrems.

It is less clear that EU residents have sufficient rights of redress when U.S. government agencies are using their data outside the national security context. Although the Commission’s Draft Adequacy Decision discusses access and use for law enforcement and public interest purposes, the analysis emphasizes limitations under the Fourth Amendment which do not extend to non-U.S. persons, but might be asserted by a U.S. organization holding data relating to that person. Despite the weakness of the Commission’s analysis, it concludes that there are U.S. rules designed to limit interference for law enforcement or other public interest purposes with EU privacy rights to what is “strictly necessary” to ensure effective legal protection against such interference. The Draft Adequacy Decision omits reference to recently enacted U.S. legislation, the Judicial Redress Act, which extends to non-U.S. persons the right to bring lawsuits against U.S. government agencies under the U.S. Privacy Act. The Privacy Act sets forth privacy standards for the U.S. government and establishes individual rights of access to, and rectification of, data

83 See Draft Adequacy Decision, supra note 58, at ¶ 51.
84 See id. at ¶¶ 95 – 105.
85 See id. at ¶¶ 96 – 99.
86 See id. at ¶¶ 100 – 104.
87 See id. at ¶¶ 107 – 110.
88 See id. at ¶111.
relating to that individual.\(^{91}\) The Judicial Redress Act, however, is not a complete extension of the Privacy Act to non-U.S. persons.\(^{92}\) It contains significant limitations, including the ability of the U.S. Attorney General to limit its benefits to citizens of certain countries, the ability of some federal agencies to “opt out” of its provisions and the fact that it only covers information transferred to the U.S. for law enforcement purposes.\(^{93}\) The Commission’s Draft Adequacy Decision, should be amended to include an analysis of these issues.

**D. Compliance Monitoring and Enforcement**

The Privacy Shield contains much more extensive monitoring requirements than existed under Safe Harbor. The Commerce Department standards for verification of an organization’s initial self-certification and annual re-certification are extensive, including review of the organization’s privacy policy, confirmation that it is public available, and confirmation that the independent recourse mechanism is identified.\(^{94}\) The Commerce Department also gave assurances that it would search for, and address, false claims of Privacy Shield participation.\(^{95}\) It noted that increased resources had been devoted to administration and supervision of program.\(^{96}\) With respect to enforcement, the FTC pledged to continue enforcement efforts begun under Safe Harbor and touted its record of enforcement of privacy rights, in general.\(^{97}\) It promised to prioritize referrals from EU Member States and investigate Privacy Shield violations on its own initiative.\(^{98}\)

In its Draft Adequacy Decision, the European Commission provided a detailed analysis of the steps for handling a complaint by a person in the EU against a U.S. organization for violating the terms of the

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\(^{91}\) See id. at §552a(d)(1).


\(^{93}\) See Id.


\(^{95}\) See Id. at page 8.

\(^{96}\) See Id. at page 9.


\(^{98}\) See Id. at page 71.
Privacy Shield. The steps include direct contact with the U.S. organization by the individual, the Commerce Department or a in EU data protection authority, use of an independent dispute resolution body, action by the FTC, an investigation by a panel of Data Protection Authorities in Europe and binding arbitration by a Privacy Shield Panel in the U.S. The Commission included a detailed listing of the obligations and commitments made by the Department of Commerce and FTC to monitor and enforce the Privacy Shield. The Commission concluded that these recourse mechanisms enable privacy violations to be “identified and punished in practice,” in accordance with the EJC’s standard in Schrems.

In addition to monitoring obligations of U.S. parties under the Privacy Shield, the Commission stressed that it would continuously monitor the overall framework through various activities, including an annual joint review with U.S. officials and data protection authorities from the EU Member States. The Commission also stated that, in the event of non-compliance, it would initiate the process for suspension, amendment or repeal of its adequacy decision as a result of non-compliance. It listed events that would lead to suspension or repeal including: (1) failure of U.S. authorities to comply with obligations regarding access for national security, public interest or law enforcement purposes, (2) failure to address complaints by EU data subjects, and (3) failure by the Privacy Shield Ombudsperson to provide timely and appropriate responses to requests from EU data subjects. These commitments appear to satisfy the EJC statement in Schrems that circumstances after an adequacy decision is made must be taken into account.

E. Correction of Flaws in the Decision to Approve Safe Harbor

In its Draft Adequacy Decision, the European Commission addressed both of the flaws in its Safe Harbor decision which were
identified by the European Court of Justice in Schrems. After describing the ECJ’s holding that the Commission lacks authority to restrict the power of a data protection authority to investigate a complaint that calls into question the validity of an adequacy determination, the Commission states that the determination is binding on the DPAs. However, the Commission then describes the steps to be taken when such a complaint it made. If the DPA considers the complainant’s allegation that an adequacy decision is not consistent with fundamental rights of privacy and data protection, national law in the Member State must provide the DPA with the ability to bring the claim before a national court, which may then refer the case to the EJC for a preliminary ruling. With respect to the exact language of the adequacy determination itself, the Commission consistently states that the United States ensures an adequate level of protection for data transferred to organizations in the U.S. under the Privacy Shield, thus avoiding the flawed language in its Safe Harbor decision which focused on the agreement rather than the country.

IV. DATA TRANSFER ALTERNATIVES TO THE PRIVACY SHIELD

U.S. organizations should be mindful of the existence of the full range of lawful alternatives under EU law allowing personal data to be transferred from the EU to the U.S. As was the case under Safe Harbor, not all U.S. recipients of EU data will be eligible to join the Privacy Shield system. Only organizations subject to the investigatory and enforcement powers of the FTC and Department of Transportation may join. Major sectors excluded include financial institutions, telecommunications carriers and the insurance industry. Moreover,

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108 See Draft Adequacy Decision, supra note 58, at ¶ 117.
109 See id. at ¶ 119.
110 See id.
111 See Draft Adequacy Decision, supra note 58, at Art. 1(1) (stating the Commission’s conclusion that “[T]he United States ensures an adequate level of protection for personal data transferred from the Union to organisations (sic) in the United States under the EU-U.S. Privacy Shield.”); see also Case C-362/14, Schrems v. Data Protection Commissioner, ¶ 97 available at curia.europa.eu/juris/documents.jsf?num=C-362/14# (Oct. 6, 2015) (last visited Nov. 29, 2015) (in which the ECJ wrote “However, the Commission did not state in Decision 2000/520, that the United States in fact ‘ensures’ and adequate level of protection by reason of its domestic law or its international commitments.”)
113 Businesses excluded from FTC jurisdiction under Section 5 of the FTC Act include
some U.S. companies may be doubt that the Privacy Shield will ever go into effect, or may prefer to rely on other transfer mechanisms. For large multinational companies that wish to transfer personal data among their affiliates, an attracting alternative might be Binding Corporate Rules, which allow lawful transfers from the EU to any other country, not just the U.S.\textsuperscript{114} For some companies which receive data from a limited number of sources in the EU, model data transfer contracts may be a realistic alternative.\textsuperscript{115} In addition, some U.S. companies might qualify to receive personal information under exceptions or “derogations” in the Data Protection Directive, including transfers qualifying under two narrowly defined contractual situations in which transfers are beneficial to the data subject.\textsuperscript{116} These alternative data transfer mechanisms, however, are not entirely free from legal problems under EU law. For example, data lawfully transferred to a U.S. organization under any mechanism could still be

banks, savings and loan institutions, Federal credit unions, telecommunications providers and air carriers. See 15 U.S.C. § 45(a)(2). The insurance industry is considered to be outside the jurisdiction of the FTC to the extent it is regulated by state law as specified by the McCarran-Ferguson Act, 15 U.S.C. § 1011, et. seq.

\textsuperscript{114} Binding corporate rules are not mentioned in the Directive but evolved under the provision in Art. 26(2) authorizing a transfer pursuant to a contractual clause with appropriate safeguards, provided that the transfer has been authorized by a Member State. In 2003, the Article 29 Working Party issued an opinion supporting the use of binding corporate rules. See Article 29 Working Party, Working Document: Transfers of Personal Data to Third Countries: Applying Article 26(2) of the EU Data Protection Directive to Binding Corporate Rules for International Data Transfers, available at http://ec.europa.eu/justice/policies/privacy/docs/wpdocs/2003/wp74_en.pdf (last visited Mar. 24, 2016.)

\textsuperscript{115} The Directive allows transfers pursuant to “standard contractual clauses” which the Commission has approved as providing sufficient safeguards to protect privacy. See Directive, supra note 1, at Art. 26(4).

\textsuperscript{116} One situation covers a transfer necessary for the performance of a contract between the data subject and the controller, which would include, for example, a contract between a depositor and a U.S. bank permitting cash withdrawals from an automatic teller machine in the EU. See Directive, supra note 1, at Art. 26(1)(b). Use of the automatic teller machine in the EU would require transmission of the depositor’s personal information to the bank in the U.S. before the withdrawal transaction could be completed. The other situation is for a transfer necessary for the conclusion or performance of a contract concluded in the interest of the data subject between the controller and a third party. See id. at Art. 26(1)(c). The latter situation would include, for example, a reinsurance contract between an insurance company in the EU and a reinsurer in the U.S. for the purpose of transferring risk with respect to homeowner insurance policies benefiting EU residents. The ability of the EU insurer to be reimbursed by the U.S. reinsurer following a loss would indirectly benefit the EU policy holders by enhancing the ability of the EU insurer to pay claims. Following a natural disaster damaging insured homes, the European insurer would transfer personal information of policy holders to the reinsurer in the U.S. for the purpose of establishing the right to be reimbursed for claims it must pay.
subject to U.S. intelligence activities in violation of privacy and data protection rights guaranteed by the EU Charter, as the EJC’s decision in *Schrems* makes clear.\(^{117}\)

V. CONCLUSION

The difficult task of finding lawful mechanisms for the transfer of personal information from the EU to the U.S. following the European Court of Justice’s invalidation of Safe Harbor in *Schrems* will be made much easier if the proposed EU – U.S. Privacy Shield goes into effect. Although much of the framework of Safe Harbor has been retained, the Privacy Shield includes many improvements in the obligations of participating U.S. companies. There also are stronger commitments by U.S. governmental institutions to monitor the system and enforce rights of people in the EU whose personal information has been transferred to the U.S. There is considerable documentation of limits on the ability of the U.S. government to access the information for national security and law enforcement purposes, but whether the Commission’s analysis supports a decision that the U.S. limits access to what is “strictly necessary” for those purposes is difficult to assess. Nevertheless, the Commission has provided a detailed review of U.S. law that can be used to protect rights of privacy and data protection of people in the EU whose personal information has been transferred to the U.S. Whether U.S. law provides privacy protection that is “essentially equivalent” to the protection in the EU, as the Commission contends,\(^{118}\) is extremely difficult to determine when the legal systems in the U.S. and EU are so different. A mechanism for a joint annual review is to be been put in place with participation from a number of parties from both sides of the Atlantic. The Commission has emphasized that lack of compliance by parties in the U.S. is likely to result in modification or suspension of the agreement. On face of the documents themselves, there appears to be a sufficient legal basis for implementation of the Privacy Shield through action by the Commission. However, before that can happen, other interested parties in the EU, notably the Parliament and the data protection authorities will have their say. Political considerations may play a role in the evaluations. As the EJC stated in *Schrems*, the effectiveness of a country’s legal system to protect privacy must be assessed in practice.\(^{119}\)


\(^{118}\) See Draft Adequacy Decision, *supra* note 58, at ¶ 113.

\(^{119}\) See Case C-362/14, Schrems v. Data Protection Commissioner, ¶¶ 74 – 75, *available*
Adequacy Decision instead focus primarily on what is written. It remains to be seen whether the Privacy Shield, if implemented, can produce privacy protection in practice which is “essentially equivalent” to the protection in the EU. If not, the Privacy Shield, like the Safe Harbor, will be vulnerable to a challenge in court.

at curia.europa.eu/juris/documents.jsf?num=C-362/14# (Oct. 6, 2015) (last visited Nov. 29, 2015) (stating at ¶ 74 that the third country’s law must “prove, in practice, effective in order to ensure protection essentially equivalent to that guaranteed within the European Union,” and also stating at ¶ 75 that the Commission must assess the content of the country’s rules from its “domestic law and or international commitments and the practice designed to ensure compliance with those rules . . .”).
DEFINING CORPORATE PERSONHOOD:
PREVENTING FRANKENSTEIN’S MONSTER FROM TERRORIZING THE VILLAGE — THREE THEORIES OF CORPORATE PERSONHOOD

by Eric Bellone and Grahan Kelder*

I. INTRODUCTION

Corporate personhood is very much in the news.¹ The Citizens United² and the Hobby Lobby³ cases have created quite a buzz. Proponents state these verdicts are logical extensions of prevailing legal doctrine with a consistent pedigree protecting First Amendment rights.⁴ Legal and business scholars know this is in relation to statutory and regulatory law.⁵ Detractors maintain the Citizens United⁶ and Hobby Lobby⁷ decisions are faulty.⁸ They often repeat what Mitt Romney told a crowd at the Iowa State Fair in 2011: “...[c]orporations are people, my friend,...”⁹ This quote became a

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⁵ Id.
⁶ Citizens United, 558 U.S. at 310.
⁷ Burwell, 134 S. Ct. at 2751.
⁸ Jorczak, supra note 4 at 287.
lightning rod highlighting the obvious differences between actual people and corporations: life span, procreation, etc.\textsuperscript{10} Can natural persons and the artificial person of the corporation be fairly equated for the purpose of determining a whole range of corporate personhood rights? Where does it all end? Critics fear such decisions allow too many rights for these artificially created people (corporations), and leave actual people wondering if corporations are similar to Frankenstein’s monster, artificial persons that will eventually break out and terrorize the village.\textsuperscript{11}

These observations and concerns beg the first question — what exactly are corporations? Are they merely economic entities? They obviously have concerns about tax issues, trade regulations, and consumer laws. But do corporations have rights outside the economic sphere? Do they have First Amendment rights concerning speech and religious civil liberties? The public is alarmed by the perceived expansion of corporate power from the economic sphere into the political sphere.\textsuperscript{12} “Corporations are managed aggressively to maximize shareholder return.”\textsuperscript{13} The powers of corporations are often misused to the detriment of the public and often to the advantage of a select few at the top.\textsuperscript{14} “Executives that run American corporations do not generally think of themselves as having an obligation to the public.”\textsuperscript{15}

This paper takes an interdisciplinary approach, examining the issues of corporate personhood concerning large, for-profit corporations. Part I will examine the history and legal precedents concerning corporations, giving background and context to the current examination of corporations. Historically, the concept of a corporation has evolved over time. How the courts have handled these evolutions have also changed.\textsuperscript{16}

Part II considers some of the legal theories of corporations. There is not one unified theory of what constitutes a corporation and its purpose. Some view corporations as a “legal fiction,” an artificial person created by natural people for their own purposes, as in the Artificial and Dependent Theory.\textsuperscript{17} In this definition of a corporation,

\textsuperscript{10} Id.
\textsuperscript{11} Jorczak, supra note 4 at 287.
\textsuperscript{12} Id.
\textsuperscript{14} Id.
\textsuperscript{15} Id. at 329.
\textsuperscript{16} Susanna Kim Ripken, Corporations are People Too: A Multi-Dimensional Approach to the Corporate Personhood Puzzle, 15 FORDHAM J. CORP. & FIN. L., 97, 106 (2009)
\textsuperscript{17} Id. at 105.
Defining Corporate Personhood

it is a creation of statutory law, and it is the law that gives it form and function.\textsuperscript{18}

Another characterization of corporations is defined in the Corporation as an Aggregate Person Theory. Under this theory corporations are formed by mutual agreement of individuals, and less as a creation of law.\textsuperscript{19} Under this definition of a corporation, the corporation takes its identity, function, and purpose from its members.\textsuperscript{20}

A third definition of a corporation is that it is a real and independent entity in its own right. This theory is the Real and Independent Person Theory and views the corporation as separate and distinct from its “owners.”\textsuperscript{21} Similar to a naturally born person, it exists before legal recognition. The state merely recognizes its reality, as the state would recognize the birth of a naturally born child. The corporation is distinct from the workers who serve it, as the workers come and go, while the corporation can potentially live forever.

Defining these three main theories, and examining their assumptions, this paper will address issues concerning the purpose of corporations and their rights and duties in relation to their purpose. The examination of these legal theories will lay the groundwork for an analysis of how corporations can be viewed through a legal lens.

In Part III this paper will explore the use of a theory, or combination of theories. It will analyze corporate rights and responsibilities in relation to the expansion of corporate rights, culminating in a three-part test to help alleviate the perceived fears of critics of the inequities between natural persons and artificially-created corporate persons in terms of power, money, and influence.

Part IV will conclude the analysis, and make policy recommendations addressing some of the concerns of corporate personhood.

II. PART I: HISTORY AND LEGAL PRECEDENTS

What is a corporation? Under the law, corporations can do many things that ‘people’ do. They can buy and sell property, lend and borrow money, sue and be sued, etc. Corporations allow natural people to pool their resources, take on large projects, create and develop new drugs, construct large buildings, or innovate intellectual property, to

\textsuperscript{18} \textit{Id.} at 99.
\textsuperscript{19} \textit{Id} at 105.
\textsuperscript{20} \textit{Id}.
\textsuperscript{21} Ripken, \textit{supra} note 15, at 107.
name a few. Also importantly, corporations act as a liability shield for shareholders.\textsuperscript{22}

Lately, many critics have become concerned that expanding corporate rights is creating a too-powerful corporate influence in society.\textsuperscript{23} Expanding the rights of corporations (to be treated like people) tears at the fabric of our society that was created to protect the rights of individuals.\textsuperscript{24}

Corporate constitutional rights are necessary to protect private property and ensure the rule of law.\textsuperscript{25} “The notion that corporations are people is ridiculous on its face, but often true.”\textsuperscript{26} Corporations do exercise many of the rights granted to human beings.

Opponents who do not want to expand the concept of corporate personhood are concerned that corporate power may overshadow the rights of natural persons.\textsuperscript{27} “As corporate persons are granted protections ‘equal’ to those of natural persons, the inequality between human people and corporate people becomes increasingly clear.”\textsuperscript{28} It is also obvious that clearer rules are needed to differentiate the constitutional rights enjoyed by natural persons and the rights that corporate persons need.

Case law has provided some guidance in differentiating corporate rights from the rights of natural persons. “Not all constitutional protections apply to corporations. In \textit{First National Bank of Boston v. Bellotti},\textsuperscript{29} the Court distinguished between “[c]ertain ‘purely personal’ guarantees, such as the privilege against self-incrimination” and “equality with individuals in the enjoyment of a right to privacy” as “unavailable to corporations … because the ‘historic function’ of the particular guarantee has been limited to the protection of individuals.”\textsuperscript{30} Recent cases have cast doubt on the durability of these past rulings, causing concern for those who oppose the expansion of corporate personhood.

They believe the courts are wrong to extend constitutional protections to corporations, because doing so will increase powers

\textsuperscript{22} \textit{Id.}
\textsuperscript{23} \textit{Id.} at 98.
\textsuperscript{24} Jorczak, \textit{supra} note 4, at 285.
\textsuperscript{25} \textit{Id.}
\textsuperscript{27} Jorczak, \textit{supra} note 4, at 287.
\textsuperscript{28} \textit{Id.}
\textsuperscript{29} 435 U.S. 765 (1978).
“inherent” in corporate personhood to the further detriment of the rights of natural persons. They view the current trend of expanding these rights as going too far, straining the logic of past decisions, and entering a realm that is unreasonable. The expansion of corporate status as legal persons was logical at first; if corporations are allowed to hold property, then it logically follows they should not be deprived of that property without due process. But corporations soon began to argue, when the Fourteenth Amendment was ratified, that Due Process and Equal Protection Clauses should apply to corporate persons as well as natural persons.

In *Santa Clara County v. Southern Pacific Railroad*, corporations maintained that California violated the Fourteenth Amendment by taxing railroad property differently from natural persons. But the Court focused narrowly on the taxation claim, and nothing in the opinion supports the corporation’s allegation that the Fourteenth Amendment applies to corporations. Yet a headnote to the case states:

“The court does not wish to hear argument on the question whether the provision in the Fourteenth Amendment to the Constitution, which forbids a State to deny to any person within its jurisdiction the equal protection of the laws, applies to these corporations. We are all of opinion that it does.”

This headnote was given the weight of settled law in the 1888 case of *Pembina Consolidated Silver Mining and Milling Co. v. Pennsylvania*. In this case the company wanted to avoid the State’s tax and licensing requirements on out-of-state corporations. Here the Court states, “Under the [Fourteenth Amendment’s] designation of person there is no doubt that a private corporation is included.” The court did not expand on this statement. As the 20th century unfolded,

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32 Jorczak, *supra* note 4, at 290.
33 Id.
35 118 U.S. 394 (1886).
36 *Id.* at 396, 409.
37 Hartmann, *supra* note 33, at 98.
39 125 U.S. 181 (1888).
40 *Id.* at 189 (1888).
41 *Id.*
the rise of corporations resulted in many cases over corporate rights and regulation.\(^{42}\)

The \textit{Santa Clara}\(^{43}\) headnote given weight by \textit{Pembina}\(^{44}\) was later used to expand and solidify corporate rights and put them on par with the rights of natural persons.\(^{45}\) In \textit{First National Bank of Boston v. Bellotti}, the court found it does not matter to the government whether a constitutional right comes from a natural person or a corporation. Their freedoms are protected by the Fourteenth Amendment (liberty, not property). There is no identified, separate source for the right when it is asserted by a corporation.\(^{46}\) Following \textit{Bellotti},\(^{47}\) in the cases \textit{Austin v. Michigan Chamber of Commerce} and \textit{McConnell v. Federal Election Commission} the Court found in both cases that it was constitutional to treat corporations differently from natural persons.\(^{48}\)

Despite the precedents set by \textit{Austin}\(^{49}\) and \textit{McConnell},\(^{50}\) in \textit{Citizens United v. Federal Election Commission} the Court further expanded the rights of corporations.\(^{51}\) Here the Court looked upon natural persons and corporations as constitutional equals, not making a distinction between the two.\(^{52}\) It is here that opponents began to take issue with the expansion of corporate constitutional rights.\(^{53}\) They believed distinctions needed to be drawn between corporate persons and natural persons.\(^{54}\) These differences (including a corporation's perpetual life, inability to vote, hold office, serve on a jury, etc.) between two classifications of "persons" needed to be considered in the application of constitutional rights.\(^{55}\)


\(^{43}\) \textit{Santa Clara}, supra note 35.

\(^{44}\) \textit{Pembina}, supra note 39.

\(^{45}\) \textit{Jorczak}, supra note 4, at 294.

\(^{46}\) \textit{Bellotti}, 435 U.S. at 780.

\(^{47}\) \textit{Bellotti}, supra note 29.

\(^{48}\) McConnell v. Fed. Election Comm'n, 540 U.S. 93, 115-122 (2003); \textit{Austin v. Mich. Chamber of Commerce}, 494 U.S. 652, 655-661 (1990). In both cases the Court upheld state campaign financing laws promulgated to help prevent corporations from dominating elections. The Court further stated the accumulation of corporate wealth and power would have a higher level or volume of political influence as compared to a natural person.

\(^{49}\) \textit{Austin}, 494 U.S. at 652.

\(^{50}\) McConnell, 540 U.S. at 93.

\(^{51}\) \textit{Citizens United}, supra note 3.

\(^{52}\) \textit{Id.}

\(^{53}\) \textit{Jorczak}, supra note 4, at 287.

\(^{54}\) \textit{Id.}

\(^{55}\) Sprague, supra note 42, at 509.
The court can be nuanced about corporate personhood. In Federal Election Commission v. Massachusetts Citizens for Life, Inc., the Court carved out an exception to a ban on corporate political speech for nonprofit groups.56 The Court found nonprofit groups which did “...not pose [a] danger of corruption [because they were] formed to disseminate political ideas, not to amass capital,” distinct from for-profit corporations which had “been the focus of regulation of corporate political activity.”57 The for-profit distinction is a key factor in differentiating between corporate persons and natural persons concerning constitutional rights and their application.58

These key factors have consequences. “The consequences of the ‘perpetual life and limited liability’ and other ‘special privileges and immunities’ granted corporations mean that any right granted to a corporation becomes infinitely easier for that corporation to assert than for a natural person trying to assert the same right.”59 The inequity of power to bring resources to bear on any political issue between corporations and natural persons can be massive. This difference in power begs for a different level of analysis and scrutiny in the evaluation of Fourteenth Amendment rights between corporate persons and natural persons.60 The apprehension for opponents of the expansion of corporate personhood is palpable. The special features that corporate persons do not share with natural persons are a major concern.

It is clear to opponents that corporate persons are fundamentally different from natural persons. This supposedly equal application of constitutional rights leads to inequitable results.61 In the Court’s line of reasoning, ignoring the differences between corporate persons and natural persons has created a subordination of individual rights to corporate rights.62

III. PART II: LEGAL THEORIES

A. Corporation as an Artificial and Dependent Theory

The Artificial and Dependent Theory believes that a corporation is not comparable to natural person and should not be viewed as such. “One way of describing the corporation is to say it is nothing more than
a legal construct. It is an artificial creation of human beings and the law. This legal construct is a convenience designed to aid people wanting to conduct commerce or band together for a mutual concern to conduct an endeavor that is greater than or possible for any single person. The law gives a corporation legal standing to enable it to conduct business. “We give it personhood status solely as a legal fiction to facilitate commerce. The corporation has standing to enter into contracts, to hold property, to sue and be sued, and ultimately to carry on business in the corporate name.” A corporation is only allowed to conduct business or actions that are incidental to the business it conducts.

The theory defines what a corporation is. “The Artificial Person Theory is thus composed of two separate elements: (1) the fictional aspect, and (2) the dependence aspect, i.e. the corporation’s dependence on the law to give it legal personality.”

The legal fiction of treating a man-made entity like a flesh and blood person is key to how the law determines how corporate persons are allotted constitutional rights. The fiction of corporate personhood is a practicality necessary for business in a modern economy (to enter into contracts, to hold property, to sue and be sued, and ultimately to carry on business in the corporate name). “The fictional component emphasizes that the corporation is a human invention, unlike the natural persons who create the corporation for their own use.” When we refer to it as a person, we do so only as a convenience, an abbreviation for practical purposes to carry out commerce.

Under this theory it is an assumption that everyone involved understands that corporations are not people. This point is so basic, it often is not mentioned. “No one actually believes a corporation is a real person. Everyone recognizes this fictional person is merely a legal abstraction. In fact, legal personality can be given to just about any object if it is deemed to serve the ends of justice.” Opponents to corporate personhood believe this basic point is being lost in the legal gymnastics taking place under current case law.

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64 See Model Bus. Corp. Act s. 3.02 (2005).
65 Ripken, supra note 16, at 106.
66 See Jeffery Nesteruk, Persons, Property, and the Corporation: A Proposal for a New Paradigm, 39 DEPAUL L. REV. 543, 564 n. 133 (1990) (“A Corporation is artificial in that it is human creation subject to human choices.”).
67 Ripken, supra note 16, at 106.
68 Id. at 107 (2009); see also John Chipman Gray, The Nature and Sources of the Law 27 (Rowland Gray ed., MacMillan 1921).
The dependence aspect of the corporation is that the corporation cannot exist without the law's consent. Corporations are legally formed when the state approves their charter, making a corporation a government allowance. As stated in *Trustees of Dartmouth College v. Woodward*: “A corporation is an artificial being, invisible, intangible, and existing only in contemplation of the law. Being the mere creature of the law, it possesses only those properties which the charter of its creation confers upon it.” When a corporation is chartered, a corporate purpose must be articulated. Without such purpose, the law cannot recognize a corporation, and it would have no legal existence. “The corporation is artificial, fictional, and conditional because it cannot come into being unless and until the law sanctions it.” When the legal paperwork for a corporation is successfully filled out, and the state approves it, it is only then that a corporation exists.

Corporations exist for a specific set of circumstances and in a specific environment. All of these are defined or approved by the state. The state plays a decisive role in creating corporations and circumscribing their actions within a limited sphere of activities. These activities are largely or solely profit driven.

**B. Corporation as an Aggregate Person**

This theory explains that as a corporation cannot be formed without the action or agreement of natural persons, so the corporation is an extension of the aggregation of the shareholders, existing to serve the private interests of the natural persons who constitute it. A corporation is less a legal construct and more of an augmentation of the existing rights of a group of natural persons.

“Under this view of the corporate person, “the rights and duties of an incorporated association are in reality the rights and duties of the persons who compose it, and not an imaginary being.” The corporation is as real as the rights of the individuals who compose it. The U.S. Supreme Court relied on this reasoning in *Santa Clara v. Southern Pacific Railroad* when it stated that a corporation is a person

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73 *Id.* at 108.
74 *Id.*, at 110-11.
75 1 Victor Morawetz, *A Treatise on the Law of Private Corporations* 1-2 (2d ed. Boston, Little Brown & Co., 1886) (It is “self-evident that a corporation is not in reality a person or thing distinct from its constituent parts. The word ‘corporation’ is but a collective name for the corporators or who compose [it] ...”).
for purposes of the Fourteenth Amendment with regard to property and cannot be taxed differently from natural persons. The extension of the property right from the natural persons to the corporation is the basis of this theory.

A weakness of this theory is that it only makes sense for small, closely held corporations with few employees and reach. The court relied on this type of reasoning in *Hobby Lobby*. In many situations, corporations are large, with widely scattered shareholders who are passive in their views (except for profitability), with small individual holdings. Others are more closely held corporations with many employees that can extend their influence across state lines whose range is more extensive than traditional small corporations. A larger corporation forms its identity by its corporate officers and working culture, rather than by its shareholders. Further, a corporation by nature has longevity and perpetual existence, which natural person shareholders do not share.

**C. Corporation as Real and Independent Person**

This theory maintains that a corporation’s existence is independent of the individual members who compose the corporation BUT is also independent of the state that legally recognizes its form.

As opposed to the Artificial Person Theory, this theory sees the corporation as an actual, real human person. “It is a full-fledged, living reality that exists as an objective fact and has a real personality in society.” The Real and Independent Theory maintains the corporation exists prior and separate from the state. “Just as the state may record the birth of every baby, or sale of every land parcel, so does the state record the formation of every corporation—a formation that occurs by virtue of agreement of the private parties who constitute the business, not by virtue of any state action.”

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76 118 U.S. 394 (1886).
77 Burwell, *supra* note 2.
79 *Id.* at 112.
80 *Id.*
83 *Id.* at 112.
84 *Id.* at 112-13; see also Robert Hessen, Editorial, *Creatures of the State? The Case Against Federal Chartering of Corporations*, Barron’s Nat’l Bus. & Fin. Wkly., May 24,
corporation is simply a natural outgrowth of the economic tendency towards business combination. Rather than being a creature of the state, the corporation is a natural existent entity "which has compelled the law to grant it official recognition."85

Unlike the Aggregate Person Theory, this theory views the corporation as much more than the sum of its individual parts.86 A corporation is an entity larger than and different from the shareholder/members themselves.87 The Real Entity Theory states the corporation is an independent "being" whose identity and existence remains constant while the membership of individuals changes over time.88 As large corporations have a perpetual life "...organizations can persist for several generations ... without losing their fundamental identity as distinct units, even though all members at some time come to differ from the original ones."89

As a person, a corporation can violate the law and be individually held responsible for its actions. “From a criminal law perspective, a corporation could be convicted of a crime, independent of any criminal conviction of any particular individuals within the corporation.”90 Fines and penalties can be imposed upon the corporation for its conduct.

The main characteristic of the Real and Independent Person Theory is that it has two differing versions. On one hand it states that corporations should be afforded the same rights and privileges as natural persons, in property rights as well as liberty rights.91 The Supreme Court has decisions that protect the rights of natural persons

1976, at 7. “The State merely adds ‘legal legitimacy’ to the corporation by its public recognition of the entity, but it has nothing to do with the actual creation of the corporation.”

85 Id. at 113 (2009); W. Jethro Brown, The Personality of the Corporation and the State, 21 L.Q. REV. 365, 370 (1905).

86 Id.

87 See Bryant Smith, Legal Personality, 37 YALE L. J. 283, 286 (1928).

88 Peter French, Collective and Corporate Responsibility, 19-30 (1984)(demonstrating that the identity of a corporation is independent of the aggregate identities of those associated with it at any particular time, in spite of the fact that its operations require that persons be associated with it.).

89 Peter M. Blau & W. Richard Scott, Formal Organizations: A Comparative Approach1 (1962). (“In fact, some argue that the existence of the organization typically predates the membership in it of any particular individual.”).

90 Ripken, supra note 15, at 115.

91 See Mark Hager, Bodies Politics: The Progressive History of Organizational “Real Entity” Theory, 50 U. Pitt. L. Rev. 575, 580 (1989); (See Covington & Lexington Tpk. Rd. Co. v. Sandford, 164 U.S. 578, 592 (1896) (“It is now settled that corporations are persons within the meaning of constitutional provisions forbidding the deprivation of property without due process of law, as well as a denial of the equal protection of the laws.”).
to justify the protection of property and liberty rights.\(^{92}\) On the other hand, if a corporation is the same as a natural person in society, it should have the same moral and social responsibilities.\(^{93}\) Under this version, the role of the law is to regulate corporations to use their powers, not just to maximize profits for their shareholders, but to also to promote the good of the general public.\(^{94}\)

The courts in many jurisdictions have used all of these theories to support opinions.\(^{95}\) Sometimes these courts have used more than one theory in a single case.\(^{96}\)

IV. PART III: ANALYSIS

The question of corporate personhood as it relates to constitutional rights has been an issue for centuries.\(^{97}\) “Of course corporations are not genuine human beings and should not automatically receive all the constitutional rights human beings claim.”\(^{98}\) It is also obvious corporations should be able to claim some constitutional rights. The question is which rights they can assert?

To get to the bottom of this issue, we must define the purpose of a corporation and, based on that purpose, what is the nature of the constitutional right asserted.\(^{99}\) Does a corporation exist solely for the purpose of its shareholders or, like natural persons, does a corporation enjoy a greater set of rights and duties in society?\(^{100}\) “… [T]here is indeed a broad consensus that for-profit corporations are economic entities, created for the purpose of benefiting society through the production of goods and services. The constitutional analysis should begin, then, with the presumption that for-profit corporations should receive rights necessarily incidental to serving that economic purpose, and should not receive rights that are not germane to that purpose.”\(^{101}\) The courts should use the same reasoning with regards to

\(^{92}\) Citizens United, 558 U.S. at 310; Hobby Lobby, 134 S. Ct. at 2751.


\(^{94}\) Ripken, supra note 16, at 117.

\(^{95}\) Id. at 118.

\(^{96}\) Hale v. Henkel, 201 U.S. 43, 70 (1906); Susanna Kim Ripken, Corporations are People Too: A Multi-Dimensional Approach to the Corporate Personhood Puzzle, 15 FORDHAM J. CORP. & FIN. L., 97, 118 (2009).

\(^{97}\) Greenfield, supra note 12, at 321.

\(^{98}\) Id.

\(^{99}\) Id.

\(^{100}\) Id. at 322.

\(^{101}\) Id.
constitutional rights that can only be exercised by natural humans.\textsuperscript{102} Corporations cannot have a conscience, serve on a jury, or vote, and as such, cannot exercise these constitutional rights.\textsuperscript{103} The best way to understand this point is to view it in terms of whether any right a corporate person asserts must be germane to its economic role. Or, is the right asserted ‘incidental’ to its very existence in the marketplace and, as such, warrants protection.\textsuperscript{104}

It is clear a corporation cannot exist without the law’s consent.\textsuperscript{105} Corporations are only formed when the state approves their charters.\textsuperscript{106} All fifty states issue charters as a prerequisite of corporate recognition.\textsuperscript{107} When a corporation is chartered, a lawful corporate purpose must be stated. Without a lawful purpose, a state cannot recognize a corporation and it would have no legal existence.\textsuperscript{108} These procedures are mandatory and must be adhered to. If the requirements of corporate formation are not met, the paperwork will be rejected and the corporation does not legally exist. A corporation only exists when the legal paperwork is filled out and approved by the state.

\textbf{A. The Three-Part Test}

A three-part test can be used to determine the extent of corporate personhood and the constitutional protections that may be granted based on that status.

The first part of the test, to determine the extent of corporate personhood and the constitutional protections they receive, should be applied in the context of the definition of a corporation. We can define for-profit corporations through their motivations and behaviors. “A corporation ... should have as its objective the conduct of business activities with a view to enhance corporate profit and shareholder gain.”\textsuperscript{109} Most corporations exist only to make profits for their shareholders while providing something useful to society. “Useful” can be a lifesaving drug or a good that is used for entertainment. From this, there is a consensus that for-profit corporations, which are

\textsuperscript{102} Id.
\textsuperscript{103} Hale v. Henkel, 201 U.S. 43, 70 (1906); See Greenfield, supra note 13, at 322.
\textsuperscript{104} See, U.S. v. Alvarez, 132 U.S. 2537 (2012) (making a differentiation as to the types of speech, even commercial speech that merits constitutional protections).
\textsuperscript{105} Ripken, Supra note 16, at 107.
\textsuperscript{106} Id., at 106; see also Phillip I. Blumberg, The Corporate Entity in an Era of Multinational Corporations, 15 DEL. J. CORP. L. 283, 292-93 (1990).
\textsuperscript{107} Id.
\textsuperscript{108} Id. at 107.
economic entities created for the purpose of benefiting society through the production of goods and services, should receive rights incidental to serving only those economic purposes. The courts should use the same reasoning with regards to constitutional rights that can only be exercised by natural humans. Corporations cannot have a conscience, serve on a jury, or vote and, as such, cannot exercise these constitutional rights. Any right a corporate person asserts must be germane to its economic role or ‘incidental’ to its very existence in the marketplace. Corporate personhood should be limited to the economic role it plays in society, and narrowly defined based on its production of goods and services. An example of such a right could be a First Amendment right to free speech in opposition of higher taxes on a corporation’s product, a prohibition (such as alcohol during prohibition), or a rationing of certain commodities (such as during World War II).

Secondly, the constitutional rights should be dependent upon whether they are consistent with the corporation’s economic purpose. Clear rules are needed to differentiate the rights natural persons enjoy; the same applies to corporate persons. Such rights must be germane to their business. Many for-profit corporations exercise a great deal of economic power, have perpetual life, and limited liability as part of the influence and legal status granted to them. Given this, any right granted to a corporation becomes infinitely easier for that corporation to assert than for a natural person trying to assert the same right. This includes commercial speech and political speech presumptively concerning other rights connected to business. These issues must be large matters of concern to the corporation and its very existence. An issue can be the difference between the prohibitions of a business versus a tax increase for that business. Given this, like the narrow definition given to corporations concerning personhood, corporate constitutional rights should be limited to its economic role, and only expanded as it relates to its very existence in the marketplace. An example of this could be a ban on economic advertising such as

110 Greenfield, supra note 13, at 322.
111 Id.
112 Hale v. Henkel, 201 U.S. 43, 70 (1906); see also Greenfield, supra note 12, at 322.
113 See United States v. Alvarez, 132 U.S. 2537 (2012) (making a differentiation as to the types of speech, even commercial speech that merits constitutional protections).
115 Jorczak, supra note 4, at 286. See also First Nat’l Bank of Bos. v. Bellotti, 435 U.S. 765, 827 (1978) and HARTMANN, supra note 34, at 98.
banning the advertising of cigarettes on television or of certain products to children.

B. Public Policy Consideration

The constitutional right in question, even if it meets the first two requirements, must be viewed in the context of public policy considerations. This prong of the test takes into consideration the common sense and common conscience of the country, and is applied to matters of public health, safety, and welfare. At its core is the duty of citizens (natural or corporate) to their fellow citizens. It considers the changing economic needs, social customs, and morality of all people, both natural and corporate. Issues like whether the country is at war, severe economic circumstances, or major common goals (i.e. the cold war or the space race) must be taken into consideration. This part of the test can be likened to the government exercising its eminent domain power. Notice and a process to be heard concerning a public policy consideration should be implemented.

V. PART IV: CONCLUSION

Currently, the status and purpose corporations hold in society is ambiguous.\textsuperscript{117} Fear and uncertainty are driving the argument both for and against corporate personhood. Corporate personhood, like that of natural persons, is complex.\textsuperscript{118} Having a legal definition of what a corporation and its purpose is will help alleviate those fears. Further, the test articulated in the previous section will aid courts and policymakers in making decisions concerning corporate personhood and the rights they enjoy.

\textsuperscript{117} Ripken, supra note 16, at 174.
**First Part**

The extent of corporate personhood and the constitutional protections they receive should be made in the context of the definition of a corporation. Any right a corporate person asserts must be germane to its economic role or 'incidental' to its very existence in the marketplace.\(^{119}\)

Corporate personhood should be limited to the economic role it plays in society and narrowly defined based on its production of goods and services.

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**Second Part**

Constitutional rights should be dependent upon whether they are consistent with the corporation’s economic purpose. Given this, like the narrow definition given to corporations concerning personhood, corporate constitutional rights should be limited to its economic role and only expanded as it relates to its very existence in the marketplace.

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**Third Part**

The constitutional right in question, even if it meets the first two requirements, must be viewed in the context of public policy considerations. This test takes into consideration the common sense and common conscience of the country and is applied to matters of public health, safety, and welfare.

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\(^{119}\) See United States v. Alvarez, 132 U.S. 2537 (2012) (making a differentiation as to the types of speech, even commercial speech that merits constitutional protections).
“The corporation is, of course, a fictional legal person with the capacity and standing to do things legal actors are entitled to do.”120 The public views corporate personhood with alarm and distain. All too often corporate power has been used against the public. The mismatch of economic power is often viewed devastating to the public good. The public sees this power of corporations now being put in political terms, such as free speech or religious liberty, and the public alarm only increases. “The power of corporations, to be sure, is frequently misused, usually to the advantage of the financial and managerial elite.”121

121 Greenfield, supra note 13, at 328.
ARE WELLNESS PROGRAMS GOOD FOR BUSINESS?
A LEGAL AND ETHICAL CHECKUP

by Elizabeth A. Brown*

I. INTRODUCTION

In workplaces from Wal-Mart to major universities, employees across the country are being asked to enroll in programs that ask them for personal health information. Many offer incentives for doing so: a discount on their insurance premium, an Amazon gift card, maybe even a free FitBit health monitor. These workplace wellness programs are designed to encourage employees to live healthier lives, thereby reducing employers’ health insurance costs in the long run. The increasing use of financial incentives in connection with these programs, however, is in effect compelling many employees to provide personal health information that may sacrifice their personal privacy and which may be used to discriminate against them at work. These hidden costs of wellness programs deserve more attention, especially

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1 For example, Bentley University asks full time employees to complete an online health profile as part of a program called “Bentley Balance” that collects data about the employees’ height, weight, physical activity levels and diet. BENTLEY U: BENTLEY BALANCE, http://www.bentley.edu/offices/human-resources/bentley-balance (last visited May 28, 2016).

as these programs become inescapable for those who cannot afford to give up the health insurance that so often requires compliance.

Several forces are helping to increase the number and scope of workplace wellness programs, including rising health insurance rates, the Equal Employment Opportunity Commission (EEOC)'s current guidelines expanding employers' powers to incentivize these programs, and case law affirming that expansion of power. Federal laws including the Patient Protection and Affordable Care Act (ACA), the Americans with Disabilities Act (ADA) and the Genetic Information and Nondiscrimination Act (GINA) operate in theory as a system of checks and balances on employers' ability to make employees provide sensitive health data at work.3

In practice, however, this system is breaking down at the expense of employee privacy, increasing the risk of discrimination based on health-related information. An increasing number of employees face an impossible choice: (1) provide personal health information that their employers can use against them without violating the ADA or GINA, as described in more detail below or (2) in effect, pay a penalty potentially amounting to thousands of dollars in order to maintain their health data privacy.

Given the hidden costs and inefficiencies of workplace wellness programs, their technological advancement, and strong federal policies of protecting employees from discrimination and privacy violations, it is now critically important to reassess the regulation and value of workplace wellness programs. This Article examines the hidden costs of wellness programs for employees, employers and policymakers in an effort to balance those costs against these programs’ more commonly accepted benefits.

II. WORKPLACE WELLNESS PROGRAMS ARE BECOMING MORE UBIQUITOUS AND INTRUSIVE.

The percentage of employers adopting workplace wellness programs has risen dramatically in recent years, as described below. This is due in part to regulatory incentives for such programs and to the perception that these programs will help stem the increasing costs of health insurance. These programs take a number of forms, aided by advances in technology that expand the extent to which these programs can provide detailed information about employees' health and fitness.

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A. Workplace Wellness Programs Take a Range of Forms.

Employee health data collection is big business. In January 2016, a consortium of companies including Humana, IBM, Johnson & Johnson, Merck, PepsiCo, and Unilever proposed a plan to disclose their employees’ aggregated health data to shareholders in their annual reports, 10-K reports, and other corporate disclosures. The collection and disclosure of employee health information is, in this way, on par with earnings, expenses, and other key economic data that affects a company’s profitability and attractiveness to investors.

Businesses collect employee health data primarily through wellness programs, which are effectively mandated by law. Starting in 2015, all employers with more than 100 full time equivalent workers were compelled by law to offer some kind of health benefit to full time employees or pay a penalty. A common element of employer-sponsored health benefits is the workplace wellness program.

A wellness program, broadly defined, is any program that seeks to promote health or prevent disease. Increasingly often, these programs include employee incentives. A simple typology of common wellness program incentives includes (1) Educational incentives, in which employers offer rewards for finishing things like an online assessment to help employees learn more about their own health and/or health risks; (2) action incentives, in which employers offer rewards for taking certain actions designed to improve their health; (3) progress incentives, in which employees are rewarded for reaching certain health benchmarks such as body mass index (BMI) or cholesterol levels; and (4) targeted incentives, which tailor incentives to an employee’s personal health goals.

B. More Employers Are Adopting Wellness Programs

The popularity of workplace wellness programs is growing. According to a 2015 survey by the Society for Human Resource Management (SHRM), 70% of U.S. employers offer a general wellness program. Another 8% planned to offer them in the following 12 months. That is a significant increase from 2008, when 58% of employers reported having wellness programs. Another survey found

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6 29 C.F.R. § 2590.702(f) (2012).
that 81% of large employers, defined as those with 200 or more employees, offer programs that help employees stop smoking, lose weight, or make other behavioral changes.\(^8\) Half of large employers now ask employees or offer them the opportunity to complete a biometric screening, which measures factors such as weight, blood pressure, cholesterol and stress.\(^9\)

Employers embrace wellness programs as a means of reducing health insurance and care costs.\(^10\) The cost of employer-provided insurance has risen dramatically in the past decade, causing employers to seek new ways of minimizing those costs.\(^11\) The average annual premium for family coverage in 2015 was $17,545.\(^12\) The cost of those premiums rose 27% between 2010 and 2015, the same rate of growth as from 2005 to 2010.\(^13\)

The price employers pay for health coverage will, for some, increase dramatically in the coming years. In 2018, a 40% non-deductible excise tax on employer-sponsored health coverage with high-cost benefits, popularly known as the “Cadillac Tax,” will go into effect.\(^14\) The “Cadillac Tax” will impose a significant cost burden on any employer that offers health benefits that are worth more than a certain threshold, effectively discouraging employers from offering high-cost health benefits. Nearly half of large employers responding to a 2015 survey recognize that at least one of their health plans will trigger the Cadillac tax when it is introduced in 2018.\(^15\)

The introduction of the Cadillac tax is driving even more workplaces to adopt wellness programs. Many employers view such programs as a means of lowering the cost of employer-sponsored health plans and mitigating the expected effects of the Cadillac tax. In a June 2015 survey, 70% of responding employers reported that they are expanding wellness programs to delay the impact of the tax.\(^16\) This makes sense given that unhealthy claimants increase health care costs overall;

\(^9\) Id.
\(^11\) Id. at 1518.
\(^12\) 2015 Employer Health Benefits Survey, supra note 8.
\(^13\) Id.
\(^16\) Id.
indeed, 43% of responding employers described high cost claimants as the number one driver of rising health care costs.17

C. Wellness Programs Use Increasingly Sensitive and Sophisticated Technology.

As wellness programs increase in popularity, the technology available to measure employees’ health is expanding in scope and capability. Employers’ use of FitBits and similar devices is already common in many workplaces.18 These devices are commonly used to track employees’ physical activity, heart rate, and other physiological markers. The data collected from these FitBits may be analyzed by third party data processors who specialize in performing these analyses for employers and insurers. A primary driver of corporate adoption of FitBit monitoring is the opportunity to reduce health insurance costs. For example, Appirio, a Bay Area startup, negotiated a $300,000 discount on its $5 million insurance costs by agreeing to share employee health data with its insurer and showing that the staff’s health was improving.19

Employers may also ask or require their employees to wear smart shirts and sensor-embedded badges to track their activity and productivity.20 Now that shoes can be built with pressure sensors to detect contact, speed and location, it may only be a matter of time before employers can track employees through their footwear as well.21

Some workplace wellness programs include the opportunity for genetic testing as well, since the cost of such testing has dropped dramatically. In 2015, it was possible to conduct a genomic sequencing test for less than $1,000, a feat that would have cost $100,000,000 in 2000.22 Genetic testing can provide important and increasingly wide-ranging information about an individual’s health. It can, for example, detect the presence of biological markers associated with an elevated

17 Id.
22 Cost per Genome, NATIONAL HUMAN GENOME RESEARCH INSTITUTE (last visited May 28, 2016), http://www.genome.gov/images/content/cost_per_genome_oct2015.jpg.
risk of colon cancer, cystic fibrosis or ovarian cancer, among other diseases.\(^{23}\)

Genetic testing will become even more common with the federal government’s recent decision to fund the collection of individual genetic information on an unprecedented scale through the Precision Medicine Initiative.\(^{24}\) Precision medicine (also called personalized medicine) refers to medical treatment that is tailored to an individual based on that individual’s unique genetic information.\(^{25}\) President Obama requested a $215 million investment in his 2016 budget for this program, which promised to “pioneer a new model of patient-powered research” that will “provide clinicians with new tools, knowledge and therapies to select which treatments will work best for which patients.”\(^{26}\) In December 2015, Congress voted to provide the National Institutes of Health with $200 million for the Precision Medicine Initiative.\(^{27}\)

III. FEDERAL REGULATIONS PROMOTE THE USE OF INCENTIVES IN WELLNESS PROGRAMS.

Whether an employee chooses to participate in a workplace wellness program depends on the relative costs of agreeing and refusing to do so. In recent years, regulatory guidance has encouraged employers to adopt greater financial incentives to persuade employees to participate in these wellness programs, while maintaining the legal fiction that such programs are “voluntary.”

A number of federal laws affect the development and operation of workplace wellness programs.\(^{28}\) The most significant are HIPAA, the ACA, the ADA and GINA. The most recent, the ACA, promotes the growth of workplace wellness programs by encouraging limited incentives for employee participation. The ADA and GINA were intended to protect employees from the potential discrimination and


\(^{26}\) Id.


\(^{28}\) State laws may also affect the operation of workplace wellness programs, but in general they are beyond the scope of this Article.
privacy violations that may stem from those programs, but their effectiveness may be limited as described below.

A. The ACA Expanded Support for Workplace Wellness Programs.

The ACA\textsuperscript{29} expanded the scope of permissible employee wellness program incentives, including financial penalties for employees who don’t comply with them. A major goal of the ACA was to encourage disease prevention.\textsuperscript{30} As Jennifer Bard characterizes it, the “ACA promotes prevention by supporting a wide variety of programs that focus on the public health model of identifying and minimizing risk.”\textsuperscript{31}

The ACA encourages wellness programs in part by increasing the incentives employers may offer for participation in some types of workplace wellness programs. It distinguishes “participatory” wellness programs from “health-contingent” wellness programs. Health-contingent wellness programs are subject to five requirements.\textsuperscript{32} First, they must give qualified employees the chance to qualify for the incentive at least once a year.\textsuperscript{33} Second, the incentive must not exceed 30\% of the total cost of the employee-only coverage of the plan, although this maximum extends to 50\% for programs designed to reduce or prevent nicotine use. If an employee’s dependents may participate in the program, then the total cost considered may be the cost of the coverage the employee and dependents are enrolled in, typically a family coverage. Third, the incentive must be equally available to all similarly situated employees.\textsuperscript{34}

Fourth, and most vaguely, the program must be reasonably designed to promote health or prevent disease. A wellness program “is reasonably designed if it has a reasonable chance of improving the health of, or preventing disease in, participating individuals, and is not overly burdensome, is not a subterfuge for discrimination based on a


\textsuperscript{32} 26 C.F.R. §§ 54.9802-1(b)(2)(ii) and (c)(3); 29 C.F.R §§ 2590.702(b)(2)(ii) and (c)(3); and 45 C.F.R. §§ 146.121(b)(2)(ii) and (c)(3).

\textsuperscript{33} See 71 Fed. Reg. 75018; see also 77 Fed. Reg. 70623.

\textsuperscript{34} See 77 Fed. Reg. 70625.
health factor, and is not highly suspect in the method chosen to promote health or prevent disease.” The generality of this language is designed to promote “flexibility and encourage innovation.” Finally, in all materials describing the plan, the plan must disclose alternative means of qualifying for the reward or whether it is possible to waive the otherwise applicable standard.

B. The ADA and GINA Prohibit Potentially Discriminatory Health Inquiries.

Both the ADA and GINA contain prohibitions on employer inquiries into certain aspects of employees’ health and medical history, subject to certain exemptions. Although employers cannot make inquiries that might reveal disability-related health information as a general matter, both the ADA and GINA allow safe harbors for such inquiries when they are made as part of workplace wellness programs, under certain conditions. In April 2015, the EEOC proposed a new rule that would clarify the terms under which employers could provide incentives to employees in exchange for confidential health information via wellness programs, as the ACA promotes, without violating the ADA. Six months later, the EEOC proposed a similar rule intended to clarify the ways in which employee incentives in wellness programs might steer clear of violating GINA’s protections.

1. The ADA Restricts Unnecessary Medical Inquiries at Work.

Under the ADA, employers may not discriminate against people with regard to their employment on the basis of any actual, perceived or historical disability. This protection against disability-based discrimination encompasses the collection of information that could indicate the presence or extent of a disability. The ADA provides that:

A covered entity shall not require a medical examination and shall not make medical inquiries of an employee as to whether such employee is an individual with a disability or as to the nature and severity of the disability, unless such examination or inquiry is shown to be job-related and consistent with business necessity.

Asking employees to reveal information about their own health, including their medical history and whether they are taking any prescription drugs, could elicit information about a disability. In

35 See supra note 80 at 33162.
36 Id. at 33173.
38 42 U.S.C. § 12112(a).
40 42 U.S.C. § 12201(c).
contrast, more general questions about an employee’s wellbeing, including the employee’s use of alcohol or tobacco, or a request for contact information in case of a medical emergency are not considered to be disability-related inquiries.41

There are two exceptions to these protections prohibitions under the ADA. First, covered entities may gather an employee’s health information as part of a voluntary wellness program.42 These entities may “conduct voluntary medical examinations, including voluntary medical histories, which are part of an employee health program available to employees at that work site.”43 A voluntary wellness program, according to the EEOC’s Enforcement Guidance, is one in which “an employer neither requires participation nor penalizes employees who do not participate.”44

Second, there is a safe harbor for wellness programs conducted as part of a “bona fide” insurance plan.45 The ADA provides that certain sections of the law, including the prohibition on medical exams and inquiries that are not “job-related and consistent with business necessity,” do not restrict “a person or organization covered by this chapter from establishing, sponsoring, observing or administering the terms of a bona fide benefit plan that are based on underwriting risks, classifying risks, or administering such risks that are based on or not inconsistent with State law[.]”46 In other words, a wellness program that is offered in conjunction with a benefit plan is exempt from the general ADA restrictions on unnecessary medical examinations and inquiries in the workplace. An employer-sponsored health insurance

41 Id.
44 Id.; See H.R. Rep. 101-485, 75, 1990 U.S.C.C.A.N. 303, 357 (“As long as the programs are voluntary and the medical records are maintained in a confidential manner and not used for the purpose of limiting health insurance eligibility or preventing occupational advancement, these activities would fall within the purview of accepted activities”).
45 42 U.S.C. § 12201(c).
46 Id.
plan would be an example of a “benefit plan” as this section accommodates.

2. GINA Restricts Employers’ Collection and Use of Genetic Information:

GINA limits the collection of information that might serve as a basis for the kind of discrimination the statute prohibits. Under GINA, it is “an unlawful practice for an employer to request, require or purchase genetic information with respect to an employee or a family member of the employee.”

“Genetic information” has an unusually broad definition under this statute. It includes not only genetically encoded information, such as that which might be revealed by genetic testing, but also “the manifestation of a disease or disorder in the family members of an individual.” GINA allows the collection of “genetic information, if the employee voluntarily agreed to its collection and the information is aggregated when passed on to the employer.

C. Regulatory Guidance Has Expanded the Range of Permissible Health Inquiries.

Regulatory guidance helps employers and courts determine the proper interpretation of federal regulations such as the ADA, GINA and ACA. This guidance is especially important because of the confusing and to some extent conflicting definitions of a “voluntary” and therefore permissible wellness program.

What does “voluntary” mean in the context of the ADA and GINA? Before the passage of the ACA, the EEOC’s guidance and federal regulations provided similar definitions for “voluntary” under both statutes. According to the EEOC’s enforcement guidance on medical exams and inquiries under the ADA, a program is “voluntary” “as long as the employer neither requires participation nor penalizes employees who do not participate.”

The regulations implementing GINA were similar in their definition of “voluntary.” An employer may offer incentives for completing assessments that reveal health information without violating GINA so long as “the covered entity makes clear […] that the inducement will

48 Id.
50 Enforcement Guidance: Disability-Related Inquiries and Medical Examinations of Employees Under the Americans with Disabilities Act (ADA), U.S. EQUAL EMPLOYMENT OPP'TY. COM'MN (Jul. 27, 2000), http://www.eeoc.gov/policy/docs/guidance-inquiries.html#N_12. Although the ADA was amended in 2008, this Guidance apparently remains in effect.
be made available whether or not the participant answers questions regarding genetic information. That would seem to limit the effectiveness of any incentive-based wellness program, since the employer would not be able to distinguish between employees who do and do not provide the information requested. This would create a problem because the employer would not be able to determine what impact, if any, the incentive had on employee disclosures.

1. The EEOC Expanded Wellness Incentives Under the ADA and GINA:

Scholars noted the potential conflicts between the ACA’s promotion of public health, in part through expanding the permissible scope of wellness programs, and the ADA’s prohibition on medical inquiries as well as GINA’s protection of genetic information privacy. In 2015, the EEOC tried to clarify the interaction of these laws. It proposed two rules to help employers understand how to offer incentives for health-related information through a wellness program without violating the ADA or GINA.

In April 2015, the EEOC issued a Notice of Proposed Rulemaking (NPRM) designed to clarify the permissible use of employee incentives in wellness programs with regard to the ADA. Observing that the ADA allows covered entities to “conduct voluntary medical examinations and inquiries, including voluntary medical histories, which are part of an employee health program available to employees at that work site,” it went on to say that wellness programs were, in its view, “employee health programs” within the meaning of that statute.

As noted above, before the ACA’s passage, the EEOC’s guidance on whether a wellness program is “voluntary” per the ADA stated that “a wellness program is ‘voluntary’ as long as an employer neither requires participation nor penalizes employees who do not participate.” Therefore, it conceded, one might “plausibly” conclude that offering rewards for participation might violate the ADA.

In this NPRM, however, the EEOC clarified that offering incentives in exchange for employee participation might not render a wellness

51 29 C.F.R. § 1635.8(b)(2)(ii).
52 See, e.g., Bard, supra note 31.
54 Id.
55 See supra note 50.
program involuntary.\textsuperscript{56} It proposed a rule allowing an employer to offer incentives up to “30 percent of the total cost of employee-only coverage, whether in the form of a reward or penalty, to promote an employee's participation in a wellness program that includes disability-related inquiries or medical examinations as long as participation is voluntary.”\textsuperscript{57}

Six months later, the EEOC took comparable action regarding incentives under GINA. In October 2015, the EEOC issued another NPRM clarifying the extent to which employers can get genetic information through wellness programs. In doing so, it proposed a rule clarifying that employers may penalize employees who do not provide information about their spouse’s health information without violating GINA.\textsuperscript{58}

Under Title II of GINA, employers covered by the law may not use genetic information in making decisions about employment for job applicants, current employees, former employees and trainees.\textsuperscript{59} “Genetic information,” as the statute defines it, includes not only an individual's genetic tests but the “manifestation of a disease or disorder in family members of such individual.”

Under GINA, employers may not ask for, require or buy the genetic information of an employee or an employee’s family member unless one of six exceptions applies.\textsuperscript{60} One of those exceptions is when the employee authorizes the employer’s acquisition of this information through a wellness program, but only if any individually identifiable information gathered is aggregated so as to anonymize that information.\textsuperscript{61} In other words, GINA allows employers to ask for genetic information via a wellness program. Employers may not, however, disclose that genetic information.

The EEOC’s proposed rule allows an employer to offer an incentive to an employee’s spouse through a wellness program if the spouse receives “health or genetic services” that are “reasonably designed to promote health or prevent disease.” That is identical to the ACA’s definition of a qualifying health-contingent wellness program. In addition, the total incentive is capped at 30% of the cost of the plan,

\textsuperscript{57} \textit{Id}.
\textsuperscript{58} \textit{Id}.
\textsuperscript{60} Id. at 42 U.S.C. §2000ff-1(b).
\textsuperscript{61} Id. at 42 U.S.C. §2000ff-1(b)(2).
also identical to the ACA’s cap. The employer may not, however, offer incentives for the genetic information of an employee’s children.\textsuperscript{62}

IV. RECENT CASE LAW ENABLES EXPANSIVE WELLNESS PROGRAMS

In recent years, courts have been asked to decide whether specific wellness programs violated the provisions of the ADA and/or GINA. Although the case law does not speak uniformly, most courts have interpreted the exceptions to the ADA broadly, increasing employers’ ability to impose wellness programs on their employees.

In Seff v. Broward County, the court decided whether penalizing employees who refuse to participate in a wellness program renders that program involuntary for ADA purposes.\textsuperscript{63} The plaintiff, a county employee, alleged ADA violations stemming in part from his employer’s surcharge of $20 on each pay check for employees who refused to participate in its wellness program. The court did not reach the question of whether the surcharge rendered the program “involuntary” under the ADA because it affirmed that the practice fell within the ADA’s safe harbor provisions for a “bona fide benefit plan” that is “based on underwriting risks, classifying risks, or administering such risks[].”\textsuperscript{64} The court reasoned that the wellness program at issue was “a term of the County’s group health plan” that was designed to help develop “present and future benefit plans using accepted principles of risk management.”\textsuperscript{65} The court also noted that the wellness program helped mitigate risks of illness, stating “that encouraging employees to get involved in their own healthcare leads to a more healthy population that costs less to insure.”\textsuperscript{66} For these reasons, the court determined that the program at issue fell within the insurance safe harbor of the ADA.

The reasoning in Seff could apply to any wellness program that is part of a health insurance plan. It is hard to imagine a wellness program that is not directly associated with a health insurance plan or designed to mitigate the risks of higher health care costs.


\textsuperscript{64} Id.

\textsuperscript{65} Id. at 1373.

\textsuperscript{66} Id. at 1374.
A. The EEOC’s Triple Play: Flambeau, Honeywell and Orion

The EEOC was not pleased with the outcome in *Seff.* In 2014, it filed complaints alleging that three employers had violated the ADA by penalizing employees who did not take part in employers' wellness plans. The first of those three cases to be decided, *EEOC v. Flambeau,* expressly relied on *Seff* in ruling against the EEOC.

1. EEOC v. Flambeau

In *EEOC v. Flambeau,* the Commission alleged that Flambeau, Inc. violated the ADA by requiring employees to complete a health risk assessment and biometric screening test in order to participate in its health insurance plan. The wellness program consisted of a health risk assessment in the form of a questionnaire and a biometric test similar to a routine physical examination.

In 2011, Flambeau offered employees a $600 credit for anyone who completed the health risk assessment and biometric test elements of the wellness program. In 2012 and 2013, however, it made the program compulsory for enrollees in its health insurance plan. Dale Arnold, a Flambeau employee, participated in the wellness program in 2011, but not in 2012. Flambeau discontinued his insurance. The Commission sued Flambeau on Arnold's behalf, asserting that the program violated the ADA.

Flambeau offered a two-pronged defense. First, it responded that its requirements fell within the ADA's safe harbor for the administration of a bona fide insurance plan. Second, it characterized the assessment and test as "voluntary" in that employees were not obligated to take part in the health insurance plan.

Granting Flambeau's motion for summary judgment, Judge Crabb of the Western District of Wisconsin ruled that the wellness plan requirements fell within the safe harbor for insurance plans. She therefore found it unnecessary to address whether the assessment and test were part of a "voluntary" wellness plan.

67 See Memorandum in Support of EEOC’s Application For Temporary Restraining Order & an Expedited Preliminary Injunction, EEOC v. Honeywell (Oct. 27, 2014); see also Preamble, EEOC Proposed Rule, 80 Fed. Reg. 21662 n. 24 ("The Commission does not believe that the ADA’s ‘safe harbor’ provision applicable to insurance, as interpreted by the court in *Seff v. Broward County,* 778 F. Supp. 2d 1370, affirmed, 691 F.3d 1221 (11th Cir. 2012), is the proper basis for finding wellness program incentives permissible") (April 20, 2015).


69 Id.

70 Id.
insurance safe harbor to this wellness program, the Flambeau court followed the Seff court’s lead. It found that Flambeau’s wellness program was a “term” of the insurance plan, and concluded that the wellness program was “based on underwriting risks, classifying risks or administering such risks” as the safe harbor requires. Although it conceded that little case law analyzes these terms, it adopted the Seff court’s view that that phrase “refers simply to the process of developing an insurance plan.”

2. EEOC v. Orion

EEOC v. Orion was the first lawsuit filed by the EEOC directly challenging a workplace wellness program under the ADA. On August 20, 2014, the EEOC sued Orion Energy Systems, an energy-efficient lighting manufacturer. Orion implemented a wellness program in March 2009 that required employees to use a “range of motion” fitness machine at Orion and complete a health risk assessment. The assessment required the employees to self-disclose their medical history and included a blood test. Under the terms of Orion’s health insurance benefit, Orion would pay the full cost of the plan for employees who completed both the preliminary fitness test and the health risk assessment. Employees who refused to complete the assessment had to pay the full cost of the health plan themselves, while employees who did not complete the fitness test had fifty dollars deducted from their pay.

Orion employee Wendy Schobert objected to participating in the program, “question[ing] whether the health risk assessment was voluntary and whether medical information obtained in connection with it was going to be maintained as confidential.” In response, Orion urged Schobert to “quash any potential ‘attitude’ issue of hers relating to the wellness program” and ordered her not to express her opinions about the wellness program to her co-workers. She declined to participate, and was compelled to pay more than $400 per month in order to continue her single coverage health benefits at the same level as other employees. She was also fined $50 per month for her

71 Id. at *12.
74 Id. at ¶ 11.
75 Id. at ¶ 13.
76 Id. at ¶ 14.
77 Id. at ¶ 17.
noncompliance. She was fired the month after objecting to the test because, the EEOC alleged, she declined to participate in the wellness program. The EEOC and Orion moved for summary judgment in December 2015.

3. EEOC v. Honeywell

Perhaps the EEOC’s most controversial 2014 wellness program lawsuit was filed against Honeywell International on October 27, 2014. In September 2014, Honeywell informed employees that they would have to undergo biometric testing for the 2015 health benefit year. If their spouses were covered under the Honeywell plan, they would also have to submit to this test. Refusal to do so meant a series of penalties. First, the employee would have to forgo Honeywell’s contributions to his health savings account, which can be up to $1500. She would also face a $500 surcharge on their medical plan costs for the 2015 benefit year. Additionally, she would be charged $1000 as a “tobacco surcharge” regardless of whether she declined the test for reasons other than smoking. Her spouse would be charged another $1000 “tobacco surcharge” for refusing to submit to the test for any reason. In sum, Honeywell employees who refused to submit to the biometric tests could have lost $4000 in fees and foregone health savings account contributions. Employees Keenan Hall and SueAnne Schwartz filed a discrimination charge with the EEOC based on this plan.

The EEOC asked the District Court of Minnesota to enjoin Honeywell from imposing penalties on employees who refuse to consent to biometric testing, alleging that Honeywell’s practice of doing so violated ADA and GINA among other laws. The testing was not voluntary, the EEOC argued, because of the substantial financial penalty associated with noncompliance.

Among other arguments, Honeywell pointed out that its testing program complied with the HIPAA Final Wellness Program

78 Id. at ¶ 21.
80 Id. at ¶ 10.
81 Id. at ¶ 14.
82 Id.
83 Id.
84 Id.
85 Id.
86 Id. at ¶ 15.
87 Id. at ¶¶ 18-19.
88 Id.
Regulations. These regulations, Honeywell argued, expressed Congressional approval for exactly the kind of wellness program Honeywell established. The fact that the EEOC’s Enforcement Guidance may have offered inconsistent advice, Honeywell argued, did not outweigh the clear mandate set by the HIPAA Final Wellness Program Regulations.

On November 6, 2014, the Court denied the EEOC’s motion for injunctive relief, noting that there was no threat of irreparable harm since the only penalty associated with Honeywell’s program was financial. If the EEOC prevailed, the Court observed, the employees could be made whole through monetary damages. In declining to reach the merits, the Court noted that “recent lawsuits filed by the EEOC highlight the tension between the ACA and the ADA and signal the necessity for clarity in the law so that corporations are able to design lawful wellness programs and also to ensure that employees are aware of their rights under the law.” 89

The EEOC was responsive to these concerns. Less than six months after the Court’s ruling in EEOC v. Honeywell, the EEOC released its proposed rule providing guidance to employers on designing wellness programs that comply with the ADA discussed above. The Honeywell biometric testing program appears to comply with the ADA compliance guidelines that the EEOC issued shortly after suing Honeywell for violating the ADA.

4. Van Patten v. Oregon

Another recent case illustrates the expanded scope of workplace wellness programs. In Van Patten v. Oregon, the Court of Appeals of Oregon affirmed that the state of Oregon could require employees to submit to health questionnaires as part of the state’s own wellness program without violating the ADA. 90

In Van Patten, the five state employees held state-sponsored health insurance administered by the Public Employees’ Benefit Board (PEBB). 91 They claimed that the state’s insurance program violated the ADA and an analogous state law by requiring them to disclose disabilities in response to a self-assessment questionnaire. 92

Refusing to take the assessment was expensive. Employees who did not complete the assessment paid $17.50 more per month (for individuals) or $35.00 more per month (for couples) on their health

91 Id. at 478.
92 Id.
Non-participants also paid $100 more in deductibles than participants. Importantly, the parties in Van Patten agreed that the financial incentives attached to participating in the assessment meant that such participation was not “voluntary” as the ADA defines it.

The defendants had another out, however. The ADA provides that covered entity “shall not […] make inquiries of an employee […], unless such examination or inquiry is shown to be job-related and consistent with business necessity.” The Oregon employers contended that the assessment did not “make inquiries” within the meaning of the statute. Noting that the dictionary defines “inquiry” as “seeking truth, information, or knowledge about something,” the Court suggested that the defendants’ subjective skepticism about receiving accurate answers complicated the issue.

The court rejected the plaintiffs’ claims that the assessment violated their right to privacy of their personal medical information. Even if the respondents had a cognizable interest in informational privacy, the context of the data collection mitigated any risk of disclosure, in the Court’s view. “The conversion companies, the insurers and the healthcare providers are all subject to the stringent security protections required by HIPAA,” it reasoned. The facts that “wrongful disclosure of individually identifiable health information by a person in a HIPAA covered entity is a crime, punishable by a fine of up to $50,000, a prison term of up to one year, or both” are “significant.” Missing from the court’s analysis is the acknowledgment that plaintiffs could not bring a HIPAA claim against their employers because HIPAA offers no private right of action.

Van Patten, like Seff and Flambeau, expanded the powers of employers to compel employee participation in wellness programs by finding ways around the ADA’s general prohibition on unnecessary workplace health inquiries. Orion and Honeywell may do the same if they are not settled first. Together with the EEOC’s expansion of the permissible incentives associated with workplace wellness programs, these decisions effectively increase employers’ ability to pressure employees into providing health information through wellness programs or face often significant financial consequences.
V. THE RISKS OF WORKPLACE WELLNESS PROGRAMS MAY OUTWEIGH THE BENEFITS.

While employers have strong financial interests in collecting and analyzing their employees’ health data, there are significant but less obvious costs to this collection. One set of harms concerns the potential invasions of employee privacy and the risks of workplace discrimination that workplace wellness programs post. Another set of harms has to do with the ineffectiveness of wellness programs to achieve their stated goals of improving health. Despite these potential harms, the increased use of substantial financial incentives may make them effectively inescapable for lower income workers. The potential costs of workplace wellness programs may well outweigh the benefits.

A. Incentive-Based Wellness Programs Risk Creating Social Harms.

Employees are increasingly vulnerable to misuse of the health data collected through workplace wellness programs because of both legal and structural developments in these programs’ administration. While one of Congress’ purposes in enacting HIPAA was to protect the privacy of personal health information, the use of third parties, who are not necessarily “covered entities” under HIPAA’s reach, undermines the privacy protections HIPAA affords in practice. In addition, the risks of discrimination that stem from incentivized health data collection are not entirely mitigated by the anti-discrimination provisions of existing federal law.

1. HIPAA Offers Limited Privacy Protections for Wellness Program Data:

HIPAA was designed to protect the confidentiality of patients’ health information. Unfortunately, HIPAA’s protections are limited in important ways when it comes to workplace wellness programs. For example, HIPAA may not protect the kind of health and fitness data that wearable technology or fitness apps might collect. Health information collected through a third party intermediary between the employer and the employee may not be a “covered entity” subject to HIPAA restrictions. If an employee’s health information is passed to a third party that is not a “health care provider, health plan, employer, or health care clearinghouse” nor an agent for any such entity, the data

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falls outside of the statutory HIPAA protections. Even if HIPAA offered relevant protection, it does not offer a private right of action.

2. The ADA Does Not Uniformly Protect Employees From Misuse of Health Data.

While the ADA may protect employees from discrimination based on actual or perceived disability, it does little to shield them from discrimination based on many kinds of data collected through wellness programs. For example, such programs may collect information revealing an employee’s high cholesterol, relative inactivity, sleeplessness, or high levels of stress. This kind of information can be elicited through questionnaires and wearable sensors. It is easy to imagine a scenario in which an employer uses the health data they collect to make employment decisions. Evaluating an employee based on the likelihood that the employee will develop an expensive health condition later in life, based on her wellness program data,
would not invoke disability law because no specific disability is invoked or perceived.\textsuperscript{107} While those conditions may correlate with an increased risk of disability, none of them is in itself a current or perceived disability. An employer may discriminate against employees singly or as a group based on this kind of information without violating the letter of the ADA.

Making employment choices based even in part on sleep patterns, nutritional intake, or smoking — conditions which may correlate with lower productivity and/or higher health insurance costs in the future, and all of which can be measured by mobile sensors — may look like discrimination to a non-lawyer and indeed may well be unethical. It is not necessarily illegal, however. Lawyers analyze a potential discrimination claim by asking whether the employee was targeted because of membership in a protected class under Title VII of the Civil Rights Act,\textsuperscript{108} such as race or religion, or a disability as defined by the ADA.\textsuperscript{109} Anti-discrimination laws cannot protect employees against decisions made any basis other than, and not necessarily correlated with, a protected class.\textsuperscript{110}

3. Weight-Based Incentives Further Stigmatize Overweight Employees.

Another set of risks has to do with the stigmatization of heavier employees that wellness programs facilitate by collecting detailed information about weight. To the extent that employers make adverse decisions based on employees’ health or lifestyle, unhindered by federal law, some scholars have suggested that employers are engaging in a form of discrimination called “healthism.”\textsuperscript{111} When employers favor hiring healthier workers and reject those perceived as being less healthy, the candidates they reject must rely on exchanges instead of employers for their health insurance.\textsuperscript{112} The federal government then has to pay more to subsidize the cost of their insurance.

There are other adverse if unintended consequences. First, unemployment obviously makes it harder to get both access to preventative care and the wages needed to buy healthier food.\textsuperscript{113} Second, it tends to deny those populations the opportunity to engage in

\textsuperscript{107} Peppet, \textit{supra} note 106 at 125-126.
\textsuperscript{110} See \textit{generally} Peppet, \textit{supra} note 106.
\textsuperscript{111} See \textit{generally} Roberts, \textit{supra} note 106.
\textsuperscript{112} \textit{Id.} at 625-626.
\textsuperscript{113} \textit{Id.} at 626.
the workplace wellness programs designed to improve health. Favoring fitter employees “could - perhaps counter-intuitively – generate a healthier workforce but a less healthy total population.”

Wellness programs’ focus on exercise as a form of weight control is controversial in other ways as well. They have been criticized as “lifestyle discrimination,” in that they reward participation in activities more easily accessed by relatively affluent people. Others note that caregivers, most often women, have less time to exercise because of their other obligations outside of paid work.

4. The Social Injustice of Gutting the “Voluntary” Limitation on Medical Inquiries.

As discussed above, the EEOC’s position on whether a wellness program is “voluntary” for ADA purposes has shifted significantly. The extent to which a wellness program incentive burdens an employee, and is therefore “voluntary,” depends on its financial impact.

An incentive is, viewed from a slightly different angle, a cost. The Departments of Labor, Health and Human Services and the Treasury recognized this in their introduction of the amendments increasing the permissible incentives in wellness plans. “Rewards also could create costs to individuals and to the extent the new larger rewards create more costs than smaller rewards, these final regulations may increase the costs relative to the 2006 regulations,” they noted. “To the extent an individual does not meet a standard or satisfy a reasonable alternative standard, they could face higher costs.”

A more logical measure of incentives, then, might look at the financial impact of the incentive on the individual employee. Rather than comparing the cost of the incentive to the cost of the overall coverage, regulators instead might compare the cost of the incentive to the employee’s net income. The EEOC already uses net income as the basis for determining whether health insurance overall is affordable. Federal law determines that the cost of health insurance is considered

114 Id. at 626.
115 Id. at 625.
117 See, e.g., Matthew A. Stults-Kolehmainen and Rajita Sinha, The Effects of Stress on Physical Activity and Exercise, 44 SPORTS MED. 1, 81-121 (2014).
119 Id.
“affordable” if the employee’s cost does not exceed a certain percentage of household income (9.5 percent in 2015).120

The EEOC has expressed concern about the impact of wellness program incentives on lower-income employees, and may now be considering whether to gauge wellness programs incentives in terms of affordability. In April 2015, it sought public input on whether employers should be allowed to use incentives that would render the health care program unaffordable “and therefore in effect coercive” under federal law.121

It is hard to imagine a persuasive argument against using net income, rather than the cost of insurance, as the better standard against which to measure the impact of a wellness program incentive. Whether the EEOC will adopt a more direct approach to measuring the affordability of wellness program incentives remains to be seen.

Any significant cost is likely to render a wellness program involuntary, and there are strong arguments in favor of acknowledging that what makes a cost significant should be determined with respect to an employee’s livelihood overall. As Alexander Hamilton wrote, “[A] power over a man’s subsistence amounts to a power over his will.”122

B. Wellness Programs Are Often Structurally and Technologically Inefficient.

Another set of risks has to do with the fact that wellness programs may not work as effectively as employers may expect, due to inefficiencies and flaws in the structure and technology such programs commonly use.

1. Wellness Programs May Not Help Employees Become Healthier.

One of the strongest arguments against incentive-based workplace wellness programs is that they are ineffective in achieving their purpose. The assumption that paying people to lose weight may be flawed. A workplace weight loss study conducted from 2013 to 2015 compared weight loss rates among four groups and concluded that the incentive-based weight loss programs tested had no appreciable effect.123

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In fact, the federal agencies charged with analyzing the final rule on Incentives for Nondiscriminatory Wellness Programs admitted that the evidence was, at best, mixed as to the effectiveness of such programs. Writing in 2013, they noted that “currently, insufficient broad-based evidence makes it difficult to definitively assess the impact of workplace wellness programs on health outcomes and cost[].” The employers must know best, reasoned the authors, using “economic logic” to “conclude that employers will create or expand their wellness program and provide reasonable alternatives only if the expected benefits exceed the expected costs.”

Many employers, however, do not use economic logic to justify their wellness programs. The preamble to the final rule on Incentives for Nondiscriminatory Wellness Programs noted that more than half of employers surveyed in 2010 reported that they did not know their programs’ return on investment. Additionally, in a 2012 survey, “only about half of employers with wellness programs stated that they had formally evaluated program impact, and only two percent reported actual cost savings.”


Another downside of workplace wellness programs is their frequent reliance on devices, such as FitBits, that provide unreliable data because they are highly susceptible to user manipulation. As workplace wellness programs develop, many of them employ wearable fitness devices such as the FitBit and similar products. FitBits, which come in a range of models and styles, are wearable personal devices that can track a user’s heart rate, steps taken, location, and other data relating to their activity and health.

In many wellness programs, the employer provides some incentive for reaching a certain goal that the device can measure, such as an average number of steps taken per week. That may not work as the employer intends. As more employees are realizing, there are ways to make the FitBit reflect physical activity that the employee is not personally engaged in. One way is to hire someone else to wear the FitBit for you. Another kind of FitBit manipulation was shown on an episode of the Big Bang Theory entitled “The Perspiration

125 Id.
126 Id.
127 Id. at 46.
Implementation,” which aired in October 2015. In the first scene, a character invents a robot designed to add mileage to the Fitbit his wife wants him to wear. In the last scene, the character’s wife asks why his Fitbit says that he ran 174 miles the previous day. Although creating a robot for this purpose may be infeasible for many employees, an alternative hack would be to put it on your dog. According to FitBit, 47% of FitBit users surveyed live with at least one dog.


Another concern is the extent to which wearable devices used in workplace wellness programs provide accurate data even without user manipulation. In January 2016, consumers from California, Colorado and Wisconsin filed a national class action lawsuit against FitBit alleging that the heart rate tracking technology used in some of its fitness watches is “wildly inaccurate” and “consistently mis-record(s) heart rates by a very significant margin.” Eight months earlier, a California consumer had filed a class action complaint against FitBit alleging that certain FitBit devices’ sleep-tracking function does not work as advertised. The plaintiff complained that “[t]he FitBit sleep-tracking function simply does not and cannot inform the user how well they slept with any accuracy whatsoever.”

Wearable devices such as Fitbits are not monitored for accuracy by the FDA. Many health and fitness apps and devices that might transmit data of interest to employers fall into the FDA’s “general wellness products” category. One example is “a portable product that claims to monitor the pulse rate of users during exercise and

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129 Id.
134 Id. at ¶ 25.
hiking.” The FDA classifies this as a “general wellness product” because “claim relates only to exercise and hiking and does not refer to a disease or medical condition” and because “the technology for monitoring poses a low risk to the user’s safety.” The FDA suggests that it has no plans to regulate these “general wellness products.”


In addition to user manipulation, another risk employers face in using FitBits and other wearable devices in wellness programs is the possibility that the devices can be hacked and infected with malware by third parties. Fortinet, a security company, reported in October 2015 that FitBits could be hacked in as little as ten seconds by someone within Bluetooth range. Once hacked, the infected devices could “potentially install a virus, trojan or other vulnerability on your computer, even days later.” In other words, when an employee syncs her FitBit to a computer, including a work computer, she may transfer the infection to the computer. Once a FitBit has been hacked, the risk of infection persists even after the FitBit is reset.

Employers who collect health and fitness data also are susceptible to increasingly common security breaches, possibly leading to the unauthorized distribution of that data. According to one survey, there were over 300,000 reported cases of medical identity theft in 2013, a 19% increase over the previous year.

5. Sensor Fusion Facilitates the Re-Identification of Anonymized Data.

Another risk facing participants in some workplace wellness programs stems from the re-identification of supposedly anonymized health data. Data collected through wellness programs is usually aggregated to some extent before being passed on to employers, in

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136 Id.
137 Id.
138 Id.
order to avoid the HIPAA prohibition on conveying individually identifiable health information. The security of aggregating data, however, has largely been disproven. Employers can now re-engineer or re-identify data to link it back to an individual person. This process, known as “sensor fusion,” is now used to collate and synthesize data about a single individual from multiple sources. When HIPAA was passed in 1996, it was harder to re-identify data that had been unlinked to an individual user, but recent technological developments have made it easier to re-identify data. The expansion of data available about us from a range of sources, including where we take our phones and what websites we visit, facilitates re-identification. Courts have yet to rule on whether HIPAA or any other federal law protects such re-identified data.

VI. CONCLUSION

While advocates of workplace wellness programs may see the increased ability to compel employee participation as a good thing, there are serious costs and risks to this expansion. These risks include the provision of inaccurate information through employee misuse or device inaccuracy, the interception of sensitive health data by hackers, and the risks of re-identification through sensor fusion. Most importantly, the least affluent employees are the most susceptible to the financial pressures that incentives create, rendering the programs effectively involuntary for those employees.

The lure of workplace wellness programs, incentivized by the ACA and intended to offset the increasing cost of health insurance, exacerbated in many cases by the impending Cadillac Tax, may be inescapable. Both case law and federal regulations are converging to increase the scope of workplace wellness programs, especially those that penalize noncompliance. Although employers have a financial interest in their employees’ good health, they also have an ethical interest in protecting their employees from the risks of discrimination and privacy invasion that wellness programs create.


146 Paul Ohm, Broken Promises of Privacy: Responding to the Surprising Failure of Anonymization, 57 UCLA L. Rev. 1701, 1706 (2010).

The potential societal costs and privacy risks inherent in workplace wellness programs should cause employers at least to question the overall benefits of such an expansion, and should cause legal scholars to question the wisdom of expanding incentive-based wellness programs.
ANTI-SURCHARGE LAWS AND FREEDOM OF SPEECH

by Patricia Quinn Robertson*

I. INTRODUCTION

Total U.S. outstanding revolving debt was $915.4 billion as of January 2016.1 This revolving debt is primarily credit card debt.2 Credit card companies typically charge interest on outstanding balances, but the credit card companies also charge merchants an interchange fee, also known as a “swipe fee” every time a customer pays with a credit card.3 This “swipe fee” is typically two to three percent of the purchase amount, and a portion of swipe fee revenue pays for credit card reward programs for credit card customers.4 In fact, in 2005, Adam Levitin estimated that processing of credit card purchases costs merchants six times as much as processing cash purchases.5

According to a Federal Reserve Bank report in 2010, the swipe fee actually results in transfers from non-credit card customers to credit card customers because most merchants pass these fees on to the customer, but merchants do not charge different prices to these two groups.6

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2 Id.
3 See Rowell v. Pettijohn, 2016 U.S. App. LEXIS 3961, at *3 (5th Cir. Mar. 2, 2016);
5 Levitin, supra note 3, at 272.
sets of customers. In fact, “[o]n average, each cash-using household pays $149 to card-using households and each card-using household receives $1,133 from cash users every year.” Higher income households are more likely to use credit cards and receive credit card rewards than lower income households, so this uniform price for all customers results in a “regressive transfer from low-income to high-income households in general.”

Some merchants desire to charge a lower “regular price” to customers who pay with cash, check, debit cards, and similar instruments (referred to in this article as cash customers) but add a surcharge to the regular price for customers who pay with credit cards (credit card customers) because processing of credit card payments costs the merchant more than processing other types of payment. However, under some state statutes merchants are not permitted to add a surcharge to a lower regular price; instead, those merchants who want to engage in such dual pricing must quote a higher regular price to all customers and then give a discount to those customers who pay by means other than credit card. The positive and negative aspects of “surcharges” for consumers who pay with credit cards versus “discounts” for non-credit card customers have been debated by politicians and economists for many years.

In the early years of credit card usage, credit cards companies’ contracts with merchants prohibited merchants from charging surcharges to credit card customers and giving discounts to non-credit card customers. Then in 1974, Congress enacted a statute which provides as follows:

With respect to credit card which may be used for extensions of credit in sales transactions in which the seller is a person other than the

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7 Id.
8 Id.
9 See, e.g., Rowell, 2016 U.S. App. LEXIS 3961.
10 Id.
12 See Levitin, supra note 3, at 276-280.
card issuer, the card issuer may not, by contract or otherwise, prohibit any such seller from offering a discount to a cardholder to induce the cardholder to pay by cash, check, or similar means rather than use a credit card.\footnote{14}

This statute remains in effect.\footnote{15} In 1976, Congress enacted a statute that provided that “No seller in any sales transaction may impose a surcharge on a cardholder who elects to use a credit card in lieu of payment by cash, check or similar means,”\footnote{16} but that statute lapsed in 1984, after serious political debate and disagreement.\footnote{17} For years credit card companies’ contracts with merchants continued to prohibit surcharges for credit card use; however, those contract provisions are generally not used now due to a 2013 antitrust settlement.\footnote{18} Now the primary legal impediment to surcharges by merchants for credit card customers exists in those states which have enacted state statutes forbidding such surcharges.\footnote{19}

Several states have enacted anti-surgehe statutes which forbid merchants from adding surcharges for customers who pay with credit cards, including: California, Colorado, Connecticut, Florida, Kansas, Maine, Massachusetts, New York, Oklahoma, and Texas.\footnote{20} Governmental objectives for these statutes include: preventing merchants from charging a surcharge to credit card users that is higher than the actual swipe fee;\footnote{21} preventing merchants from using “bait and switch” tactics, i.e. surprising credit card customers at the cash register by charging them a higher price than the sticker price;\footnote{22} or avoiding customer confusion between merchants that offer discounts for cash

\footnote{15} Id.
\footnote{18} See, e.g., In re Payment Card Interchange Fee and Merchant Discount Antitrust Litigation, 986 F. Supp. 2d 207 (E.D.N.Y. 2013).
\footnote{20} Id.
\footnote{22} Id.
customers versus merchants that charge surcharges for credit card customers.23

Recently, merchants have filed suit in various federal courts to challenge some state anti-surcharge statutes under the First Amendment to the U.S. Constitution.24 A split among U.S. Circuit Courts of Appeals has recently developed in connection with whether state anti-surcharge laws violate the First Amendment.25 The First Amendment provides that “Congress shall make no law...abridging the freedom of speech,”26 and by virtue of the Fourteenth Amendment to the Constitution, the First Amendment is also applicable to states.27 This paper examines the circuit split. The Second and Fifth Circuits recently held that the anti-surcharge statutes of New York and Texas do not violate the First Amendment, but the Eleventh Circuit held that the anti-surcharge statute of Florida does violate the First Amendment.28 Soon the Ninth Circuit may also weigh in on this split as they review a California district court’s opinion that the California anti-surcharge statute violates the First Amendment.29 These cases provide a great current example of the difficulty in distinguishing between a law that regulates commercial speech and a law that regulates commercial conduct.

II. THE ELEVENTH CIRCUIT’S POSITION

In Dana’s Railroad Supply v. Attorney General, State of Florida30 the Eleventh Circuit Court of Appeals examined the anti-surcharge statute of Florida.31 This statute provided that it was a misdemeanor to “impose a surcharge on the buyer or lessee for electing to use a credit card in lieu of payment by cash, check, or similar means, if the seller or lessor accepts payment by credit card.”32 The Florida statute also

23 Id.
24 See Rowell, 2016 U.S. App. LEXIS at *2; Expressions Hair Design v. Schneiderman, 808 F.3d 118 (2d Cir. 2015); Dana’s RR Supply v. Fla. Atty Gen’l, 807 F.3d 1235 (11th Cir. 2015); Italian Colors Restaurant v. Harris, 99 F. Supp. 3d 1199 (E.D. Cal. 2015).
25 Id.
26 U.S. CONST. amend. I.
28 Rowell, 2016 U.S. App. LEXIS at *22; Expressions, 808 F.3d at 144; Dana’s, 807 F.3d at 1251.
29 Italian Colors, 99 F. Supp. 3d at 1212. The district court’s decision in Italian Colors about the constitutionality of California’s anti-surcharge statute has been appealed to the Ninth Circuit Court of Appeals. See Notice of Appeal at 2, Italian Colors, 99 F. Supp. 3d 1199 (E.D. Cal. 2015) (No. 2:14-cv-00604-MCE-DAD).
30 Dana’s, 807 F.3d at 1239.
32 Id. This statute provides in full as follows:

(1) A seller or lessor in a sales or lease transaction may not impose a surcharge on
defined a surcharge as “any additional amount imposed at the time of a sale or lease transaction by the seller or lessor that increases the charge to the buyer or lessee for the privilege of using a credit card to make payment.” Note that this statute expressly permitted merchants to give discounts to customers for paying by means other than a credit card.

The plaintiffs in Dana’s were four small business owners who received cease and desist letters after communicating to customers that an additional fee would be charged for credit card customers. The Dana’s court first determined whether the anti-surcharge statute regulated conduct or speech. According to Dana’s, regulation of commercial conduct is simply subject to a review of whether the regulation has a rational basis, but a regulation of speech is presumed invalid and violates the First Amendment unless it withstands the more stringent First Amendment scrutiny.

Imagine a restaurant telling customers that they have two choices of drink serving size. One is “glass half empty” and the other is “glass

the buyer or lessee for electing to use a credit card in lieu of payment by cash, check, or similar means, if the seller or lessor accepts payment by credit card. A surcharge is any additional amount imposed at the time of a sale or lease transaction by the seller or lessor that increases the charge to the buyer or lessee for the privilege of using a credit card to make payment. Charges imposed pursuant to approved state or federal tariffs are not considered to be a surcharge, and charges made under such tariffs are exempt from this section. A convenience fee imposed upon a student or family paying tuition, fees, or other student account charges by credit card to a William I. Boyd, IV, Florida resident access grant eligible institution, as defined in § 1009.89, is not considered to be a surcharge and is exempt from this section if the amount of the convenience fee does not exceed the total cost charged by the credit card company to the institution. The term “credit card” includes those cards for which unpaid balances are payable on demand. This section does not apply to the offering of a discount for the purpose of inducing payment by cash, check, or other means not involving the use of a credit card, if the discount is offered to all prospective customers.

(2) A person who violates the provisions of subsection (1) is guilty of a misdemeanor of the second degree, punishable as provided in § 775.082 or § 775.083.

Id. 33 Id.
34 Id.
35 Dana’s, 807 F.3d at 1239.
36 Id. at 1239-40.
37 Id. at 1241.
38 Id.
39 Id.
40 Id. at 1241-2.
In reality, the quantity of the drink is the same. Suppose a state law provides that restaurants can no longer use the words “glass half empty” to describe its serving size. Would such a law regulate the conduct of the restaurant or would it regulate the speech of the restaurant? The court in Dana’s used this example to illustrate the point that the law is regulating speech by requiring that certain words be used (and certain words not be used) to describe an objective fact, even though either phrase (glass half full or glass half empty) accurately describes reality. Similarly, according to the court in Dana’s, a law forbidding the use of the word “surcharge” while permitting “discounts” to describe the same reality (a dual pricing system for credit card users versus cash payers) is a law that regulates speech rather than a law that regulates economic activity. For this reason, the Dana’s court used First Amendment scrutiny to examine the anti-surcharge law.

The Eleventh Circuit examined the Florida anti-surcharge statute using intermediate scrutiny (the test for commercial speech), stating that if it fails that test, it would also fail a strict scrutiny test. Intermediate scrutiny provides that the law may be upheld if it advances “a substantial government interest and [is] narrowly tailored.” The Dana's court noted the political elements of the word “surcharge” in the context of anti-surcharge laws. The court held that the Florida statute failed the intermediate scrutiny test because it does not regulate conduct, i.e., it does not forbid dual pricing. Instead the Florida statute regulates the words used to describe the dual pricing conduct and thus “deprives the marketplace of ideas of the full range of public sentiment” and “applies only to how a merchant may frame the price difference between cash and credit-card payments.” It is a viewpoint-based restriction on speech because “it denies the expression of one equally accurate account of reality [surcharge] in favor of the State’s own [discount].” The court further stated that “a law enacted for the sole purpose of forbidding a price difference to be labelled a

41 Id. at 1245; Levitin, supra note 3, at 279-280.
42 Id.
43 Id.
44 Id.
45 Dana's, 807 F.3d 1235 at 1245-6.
46 Id. at 1246.
47 Id.
48 Id.
49 Id. at 1247.
50 Id. at 1246.
51 Id. at 1247-8.
surcharge, while allowing the same to be called a discount, does not impose an ‘incidental burden’ on speech.”

After determining that the Florida statute regulates speech, the Eleventh Circuit then applied a four-part test (known as the Hudson test) which requires that all four of the following criteria must be met in order for a statute to survive scrutiny: (a) the statute regulates speech that is “neither misleading nor related to unlawful activity;” (b) the government has a “substantial interest” served by the statute; (c) the statute “directly advances” that interest; and (d) a “more limited restriction” would not be adequate to serve that interest.

The Dana’s court held that Florida’s anti-surcharges law failed all of these tests. The word “surcharge” is not misleading to consumers. The court did not believe that a substantial interest of government is at stake. As the court stated when considering the third and fourth parts of the test, “Any of the asserted interests-preventing bait-and-switch tactics, providing advance notice to customers, and levelling the playing field among merchants-would be better served by direct and focused regulation of actual pricing behavior.” Examples include: prohibiting dual pricing, placing a ceiling on the price difference between credit card and non-credit card users, prohibiting deceptive trade practices, such as bait-and switch, or requiring that merchants disclose how their surcharge/discount policy works.

The California District Court in Italian Colors Restaurant v. Harris held that the California anti-surcharges statute singles out one particular group of speakers (merchants) and is a content-based restriction that is presumed unconstitutional and will not survive scrutiny unless it is “the least restrictive means to further a compelling interest.” The California anti-surcharges statute expressly encourages discounts to non-credit card customers, but prohibits surcharges to credit card customers, and it provides for retailer liability to the cardholder for triple the damages plus costs and

52 Id. at 1247-8 (citing Sorrell v. IMS Health, Inc., 564 U.S. 552 (2011)).
54 Dana’s, 807 F.3d at 1249 (citing Cent. Hudson, 447 U.S. 557, 564).
55 Id. at 1249-51.
56 Id. at 1249-50.
57 Id. at 1250.
58 Id.
59 Id.
60 99 F. Supp. 3d 1199 (E.D. Cal. 2015).
61 Id. at 1208 (quoting S.O.C., Inc. v. Cnty. of Clark, 152 F.3d 1136, 1145 (9th Cir. 1998)).
attorneys’ fees if the surcharge is not returned to the cardholder within thirty days of written demand.62

The California District Court applied intermediate scrutiny (the Hudson test) in a similar fashion to the Eleventh Circuit’s application in Dana’s Railroad Supply.63 In Italian Colors64, the government claimed that the purpose of the anti-surcharge statute was to reduce consumer deception.65 However, the Italian Colors66 court noted that the fact that the government is exempt from the anti-surcharge statute “undermined” the idea that consumers are somehow deceived by surcharges.67 As the court stated, “If this speech is so deceptive and harmful, why is the government allowed to engage in it?”68 The court stated that the California law was more broad than necessary to prevent a bait and switch situation.69 The court suggested that a better way to “prevent unfair surprise to the consumers at the cash register” would be to require that merchants disclose surcharges.70 This type of law would have the added benefit of not trouncing on the merchants’ First Amendment rights.71 The California district court also found California’s statute unconstitutionally vague because it was not clear what the definition of a surcharge is under the statute and exactly

62 Cal. Civ. Code § 1748.1 (2016) provides as follows:
(a) No retailer in any sales, service, or lease transaction with a consumer may impose a surcharge on a cardholder who elects to use a credit card in lieu of payment by cash, check, or similar means. A retailer may, however, offer discounts for the purpose of inducing payment by cash, check, or other means not involving the use of a credit card, provided that the discount is offered to all prospective buyers.

(b) Any retailer who willfully violates this section by imposing a surcharge on a cardholder who elects to use a credit card and who fails to pay that amount to the cardholder within 30 days of a written demand by the cardholder to the retailer by certified mail, shall be liable to the cardholder for three times the amount at which actual damages are assessed. The cardholder shall also be entitled to recover reasonable attorney’s fees and costs incurred in the action.

A cause of action under this section may be brought in small claims court, if it does not exceed the jurisdiction of that court, or in any other appropriate court.


64 99 F. Supp. 3d 1199.
65 99 F. Supp. 3d 1199, 1209.
66 99 F. Supp. 3d 1199.
67 99 F. Supp. 3d 1199, 1209.
68 Id.
69 Id.
70 99 F. Supp. 3d at 1210.
71 Id.
what behavior violates the statute.\textsuperscript{72} This case has been appealed to the Ninth Circuit Court of Appeals.\textsuperscript{73}

III. THE FIFTH AND SECOND CIRCUIT’S POSITION

The plaintiff merchants in Rowell v. Pettijohn\textsuperscript{74} complained because they desired to charge a lower price for cash customers and a higher price for credit card customers.\textsuperscript{75} These merchants expressed concern that they could incur civil penalties if they did so because of the Texas anti-surcharge law.\textsuperscript{76} Texas’ anti-surcharge statute provides that “[i]n a sale of goods or services, a seller may not impose a surcharge on a buyer who uses a credit card for an extension of credit instead of cash, a check, or a similar means of payment.”\textsuperscript{77} In Rowell,\textsuperscript{78} the Fifth Circuit decided two issues: (a) whether Texas’ anti-surcharge statute violated the First Amendment; and (b) whether Texas’ anti-surcharge statute was impermissibly vague.\textsuperscript{79}

In Rowell\textsuperscript{80} the Fifth Circuit held that the Texas law, as a price regulation, “regulates conduct, not speech.”\textsuperscript{81} The law does not prevent merchants from “informing customers about the cost of credit, encouraging them to use cash, or expressing views on pricing policy

\textsuperscript{72} Id. at 1211-2.
\textsuperscript{73} See Notice of Appeal at 2, Italian Colors, 99 F. Supp. 3d 1199 (E.D. Cal. 2015) (No. 2:14-cv-00604-MCE-DAD).
\textsuperscript{74} 2016 U.S. App. LEXIS 3961 (5th Cir. Mar. 2, 2016).
\textsuperscript{75} Id. at *2.
\textsuperscript{76} Id. at *23.
\textsuperscript{77} Tex. Fin. Code § 339.001 (a) (2016). The remainder of the statute provides as follows:
(b) This section does not apply to:
(1) a state agency, county, local governmental entity, or other governmental entity that accepts a credit card for the payment of fees, taxes, or other charges; or
(2) a private school that accepts a credit card for the payment of fees or other charges, as provided by Section 111.002, Business & Commerce Code.
(c) The consumer credit commissioner has exclusive jurisdiction to enforce this section.
(d) The Finance Commission of Texas may adopt rules relating to this section. Rules adopted pursuant to this section shall be consistent with federal laws and regulations governing credit card transactions described by this section.
(e) This section does not create a cause of action against an individual for violation of this section.
\textsuperscript{78} 2016 U.S. App. LEXIS 3961 at *2.
\textsuperscript{79} Id.
\textsuperscript{80} Id. at *14, 18.
\textsuperscript{81} Id. at *14, 18.
more generally.” The Fifth Circuit held that the Texas law is not a content-based restriction on speech, but “the speech is merely incidental to the regulated economic conduct.” The court further held that the Texas law was not unconstitutionally vague because “[a] plain reading of Texas’ law shows it forbids a merchant from imposing an extra charge for a purchase with a credit card, and is completely silent as to any other forms of pricing…[and] the law does not prohibit merchants from advertising two prices.”

In *Expressions Hair Design v. Schneiderman* the Second Circuit held that New York’s anti-surcharge law does not violate the First Amendment and is not unconstitutionally vague. The New York statute provides: “No seller in any sales transaction may impose a surcharge on a holder who elects to use a credit card in lieu of payment by cash, check, or similar means.” Violation of this statute is a misdemeanor punishable by fine and/or imprisonment.

The Second Circuit stated that prices, and therefore relationships between prices, are not “speech” protected by the First Amendment. The Second Circuit held that New York’s anti-surcharge statute “does not prohibit sellers from referring to credit-cash price differentials as credit-card surcharges, or from engaging in advocacy related to credit-card surcharges; it simply prohibits imposing credit-card surcharges.” The Second Circuit reasoned that the New York law regulates conduct rather than speech. If a single-sticker price seller charges a surcharge above the sticker price (regardless of the label the seller uses) this conduct would violate the anti-surcharge statute; however, if such a seller gives a discount and charges an amount below the sticker price to a cash buyer (even if the seller uses the word

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82 Id. at *19 (quoting Rumsfeld v. Forum for Acad. & Inst. Rights, 547 U.S. 47, 62 (2006)).
83 Id. at *19.
84 Id. at *22-23.
85 808 F.3d 118 (2nd Cir. 2015).
86 Id. This was a reversal of the district court’s holding in *Expressions Hair Design v. Schneiderman*, 975 F. Supp. 2d 430 (S.D.N.Y. 2013).
87 N.Y. C.L.S. Gen. Bus. § 518 (2015) provides as follows:
No seller in any sales transaction may impose a surcharge on a holder who elects to use a credit card in lieu of payment by cash, check, or similar means.
Any seller who violates the provisions of this section shall be guilty of a misdemeanor punishable by a fine not to exceed five hundred dollars or a term of imprisonment up to one year, or both.
89 808 F. 3d at 130.
90 Id. at 131.
91 Id.
“surcharge”), this would not violate the statute.\textsuperscript{92} It was unclear to the court whether the statute applies outside of the single sticker price sale, so the court refrained from deciding that any other applications of the law violated the First Amendment.\textsuperscript{93} In addition, because the court felt that the core of the law was single sticker-price sellers, and that it could be reasonably understood, the law was not unconstitutionally vague.\textsuperscript{94}

IV. SURCHARGES AS SPEECH

Consider this example. You are shopping for a product or service. The merchant says the price is $103, but there will be a $3 discount if you pay with cash or check.\textsuperscript{95} Does this induce you to pay with cash or check? Instead, suppose that the merchant says the price is $100, but there will be a $3 surcharge if you pay with a credit card\textsuperscript{96}. Does this change your decision about whether to pay with a credit card? Clearly, these pricing schemes have the same mathematical result, i.e., in both cases you pay $103 if you pay with a credit card, and you pay $100 if you pay with cash or check. Nevertheless studies have shown that consumer choice is more likely to be influenced by a surcharge than by a discount.\textsuperscript{97}

Credit card companies have an interest in ensuring that merchants use the word “discount” instead of “surcharge” if customers are charged two different prices based upon their method of payment.\textsuperscript{98} Studies show consumer bias when consumers look at identical pricing schemes that are described with different language.\textsuperscript{99} The negative human response to a perceived penalty is more intense that the positive human response to a perceived reward.\textsuperscript{100} As Adam J. Levitin points out, “[a]ccordingly although the credit card lobby has never embraced cash discounts, it has preferred them to credit card surcharges, because

\textsuperscript{92} Id.
\textsuperscript{93} Id. at 135.
\textsuperscript{94} Id. at 144.
\textsuperscript{95} See Dana’s, 807 F.3d at 1251-2 (Carnes, C.J., dissenting).
\textsuperscript{96} Id.
\textsuperscript{98} Liftin, supra note 3, at 280.
\textsuperscript{99} See Bambauer, supra note 97, at 681-4.
\textsuperscript{100} Id.
consumers perceive a discount as a gain, but a surcharge as a penalty and will prefer to use another payment system rather than be penalized for using credit. According to Levitin and Jonathan Slowik, a surcharge creates more transparency in connection with the transaction costs of credit card use. This surcharge might also help counteract the “underestimation bias” of consumers who frequently underestimate the costs of using credit cards. A large portion of the swipe fees charged to merchants are used to provide rewards to credit card users. If no portion of the swipe fees are passed on to consumers as surcharges, then consumers who earn these credit card rewards may be led to believe that their credit card use has a negative cost. In addition, as mentioned in the introduction to this paper, the increased prices charged by stores who do not use surcharges or discounts to cover the “swipe fee” may have a regressive effect on consumers.

The pivotal question asked by the courts in the First Amendment challenges to the anti-surcharge statutes is whether the anti-surcharge statutes regulate conduct or speech. The anti-surcharge statutes discussed in this paper permit a dual pricing system: i.e., charging one price for credit card users and a different (discounted) price for non-credit card users. Based upon what is known about consumer behavior and perception, these statutes prohibit merchants from using the most effective words to communicate the dual pricing scheme. As one Amicus Curiae Brief in Rowell states: “To draw an analogy, if the Texas statute addressed political speech, it would allow

102 Levitin, supra note 3, at 282; Slowik, supra note 97, at 1325-6.
103 Levitin, supra note 3, at 282-4.
105 Id.
106 Id.
107 Rowell, 2016 U.S. App. LEXIS at *14; Expressions, 808 F.3d at 130; Dana’s, 807 F.3d at 1241; Italian Colors, 99 F. Supp. 3d at 1207.
campaign statements that are relatively ineffective, but ban campaign statements that cause voters to change the way they vote.”\textsuperscript{110}

The inability of merchants to effectively communicate the true cost of credit cards to consumers may reduce the competition of credit card companies with each other and with other forms of payment.\textsuperscript{111} The economic model of perfect competition includes perfect information.\textsuperscript{112} Although in the real world consumers may not have perfect information, better information for consumers should result in more competition among credit card providers.\textsuperscript{113} Rational consumers should shop to maximize utility.\textsuperscript{114} If a consumer understands that the consumer’s cost of using a credit card is higher than the cost of using a debit card, a rational choice for that consumer would be using the lower-cost method of payment.\textsuperscript{115} This may induce credit card companies to offer their services at a more competitive price to attract those consumers.\textsuperscript{116} As Fumiko Hayashi states, surcharging “enhances efficiency in the retail payments system by improving price signals consumers face when making payments.”\textsuperscript{117} Of course, if a surcharge is greater than the actual swipe fee, then this may reduce efficiency;\textsuperscript{118}

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\textsuperscript{110} Id.
\textsuperscript{111} Id.
\textsuperscript{112} See J. Howard Beales III, Behavioral Economics and Credit Regulation, 11 J.L. ECON. & POL’Y 349, 349-351 (Fall 2015). Professor Beales concludes as follows: Behavioral economics offers many useful insights into consumer behavior, and can inform policy choices. Like other interventions, however, choices based on behavioral principles must be tested against actual market behavior. The need for testing behavioral approaches is particularly acute because of the absence of a clear theory of which biases apply in particular circumstances. Id. at 365.
\textsuperscript{113} Id. at 349-351.
\textsuperscript{114} Id. According to Beales, the fundamental result of welfare economics is that competitive market outcomes maximize consumer welfare as judged by consumers, given the initial distribution of resources. The model assumes that consumers act rationally to maximize their utility, choosing the products and services that best satisfy their preferences. Sellers, acting rationally to maximize their profits, respond to consumer preferences as revealed in the marketplace, which requires them to offer the kinds of products consumers most prefer. Competition among sellers prevents consumer exploitation, and pushes each seller to lower costs and offer the best possible deal to consumers. Beales, supra note 112, at 349-350.
\textsuperscript{115} Id. at 349-351.
\textsuperscript{116} Id.
\textsuperscript{118} Id.
\end{flushleft}
however, competitive market forces and regulation of surcharge amounts could discourage or prohibit excessive surcharges. The Fifth and Second Circuits’ recent opinions that anti-surcharge statutes regulate conduct and not speech ignore the economic reality that merchants are permitted to charge a lower price to cash customers and a higher price to credit card customers. Whether a difference in price is called a surcharge or a discount, the higher price for a credit card customer is the same. The statutes do not actually regulate pricing conduct of the merchants, but they do regulate how that pricing conduct is expressed, and many would argue that the anti-surcharge statutes suppress the most effective way to communicate the cost difference for credit card customers. The dissent in Dana’s pointed out that the Florida statute (unlike the other state anti-surcharge statutes examined in the court cases described in this paper) includes a definition that describes the surcharge as “any additional amount imposed at the time of a sale” (emphasis added). It is possible to read this as a regulation of conduct (i.e., prohibition of a bait and switch situation where a customer does not realize there will be a surcharge until the customer gets to the cash register). However, all charges and discounts are imposed at the time of sale. The fact that a surcharge is imposed at the time of sale does not necessarily mean that the consumer has no opportunity to know in advance that it will be imposed at the time of sale. If the statute was aimed at the timing of notice to the consumer, it could state that much more clearly. A discount for non-credit card customers would also be imposed at the time of sale, but such a discount is not prohibited by the Florida statute.

In 1976 the U.S. Supreme Court held in Virginia Pharmacy Board v. Virginia Consumer Council that speech such as “I will sell you the X prescription drug at the Y price” was entitled to First Amendment

119 Id. See Levitin, supra note 104, at 22-23 (2008).
120 See Rowell, 2016 U.S. App. LEXIS at 7; Expressions, 808 F.3d at 127; Dana’s, 807 F.3d at 1245; Italian Colors, 99 F. Supp. 3d at 1204.
121 Id.
122 Id.
123 807 F.3d at 1251.
125 Id.
126 Id.
127 Id.
128 Dana’s, 807 F.3d 1235, 1244.
As the court stated, a person may find the price of prescription drugs more important to his life than many political debates.132 Similarly, a person’s choice about whether to be a cash customer or credit card customer, with the attendant costs, can be very important in that person’s life because overusing credit cards “exacerbates a host of social problems, such as increased consumer debt levels, inflation, and increased consumer bankruptcy filings.”133

The Virginia Pharmacy Board134 court stated:

Advertising, however tasteless and excessive it sometimes may seem, is nonetheless dissemination of information as to who is producing and selling what product, for what reason, and at what price. So long as we preserve a predominantly free enterprise economy, the allocation of our resources in large measure will be made through numerous private economic decisions. It is a matter of public interest that those decisions, in the aggregate, be intelligent and well informed. To this end, the free flow of commercial information is indispensable.135

If expression of price was protected in the Virginia Pharmacy Board136 case, it seems reasonable that an expression of a dual pricing system (one price for cash customers and a higher price for credit card customers) should also be protected as commercial speech.137 The “real-world” substance of the anti-surcharge laws should be examined.138 If, in reality, anti-surcharge statutes do not prohibit charging two different prices, one lower price for non-credit card customers and another higher price for credit card customers, then those statutes do not clearly regulate conduct.139 Instead, those statutes regulate how the conduct is described by the merchant, and this type of speech has historically received First Amendment protection.140

According to Derek E. Bambauer, courts tend to focus on a time-honored concept of the “marketplace of ideas” when considering the

131 Id. at 761.
132 Id. at 763.
133 See Levitin, supra note 104, at 3.
134 425 U.S. at 765.
135 Id. Shortly after the Virginia Pharmacy Board decision, the U.S. Supreme Court held that a disciplinary rule that prohibited attorney advertising of prices violated the First Amendment. Bates v. State Bar of Arizona, 433 U.S. 350 (1977). Nevertheless, the Bates Court did leave room for regulation of the “time, place and manner” of such advertising. Id. at 384.
136 425 U.S. at 773.
137 Dana’s, 807 F.3d at 1245-6.
138 Id.
139 Id.
140 Virginia’s Pharmacy Board, 425 U.S. at 765; Dana’s, 807 F.3d at 1245-6.
protection level for commercial speech. Bambauer explains that some courts focus on advertising and pricing as ordinary communications that do not rise to the level of political speech; other courts treat such speech as “equally valuable as political speech because transactions are linked to policy judgments about structuring the economy,” and some courts vacillate between those two views. The Second and Fifth Circuits in *Expressions Hair Design* and *Rowell* have held that pricing in the form of surcharges is conduct, not speech, while the Eleventh Circuit in *Dana* disagrees. We may soon find out where the Ninth Circuit falls in this split, and it is possible that the U.S. Supreme Court may consider this issue.

Bambauer writes that the “marketplace of ideas” model is flawed. Bambauer opposes the use of the “marketplace of ideas” model to strike down regulations of speech in cases where framing and other similar biases can make consumers “vulnerable to strategic behavior by those with influence over our information environment.” Bambauer suggests that a better approach for courts would be to examine the following to determine whether a regulation should stand: “how we interact with information in the environment in question, and what rationale underlies protecting unconstrained communication in that space.” If courts adopt Bambauer’s approach, courts would examine how consumers interact with surcharge and discount information in the marketplace and the reasons that communication about surcharges for credit card customers should be unconstrained. The anti-surcharge statutes may actually require a framing of prices in a way that may cause consumers to misjudge the true cost of using credit cards.

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141 Bambauer, *supra* note 97, at 664.
142 *Id.*
143 *Id.*
144 808 F.3d at 144.
146 807 F.3d at 1251.
149 *Id.* at 698.
150 *Id.* at 703.
151 *Id.*
152 See *id.* at 698.
V. CONCLUSION

To help consumers gain needed information about the true cost of credit cards, Congress could pass a federal law expressly permitting surcharges and, to avoid any bait and switch tactics, this law or its corresponding regulations could include explicit, detailed requirements about how merchants must disclose these surcharges to customers before those customers get to the cash register.\textsuperscript{153} However, credit card lobbyists may encourage political opposition to such legislation.

Possibly the U.S. Supreme Court will review this Circuit split in the future. The Supreme Court is in a position to provide definitive guidance about the extent of First Amendment protection for surcharges to credit card customers, and this could increase transparency of pricing for all consumers.

\textsuperscript{153} Dana's, 807 F.3d at 1249-51.
COLETTA BENELI’S PLIGHT LEADS THE NLRB TO CHANGE ITS ARBITRAL DEFERRAL STANDARD: BUT, BASED ON ALLEGED “FAIRNESS,” HER EMPLOYER WAS GRANTED A GET-OUT-OF-JAIL-FREE CARD

by David P. Twomey

I. INTRODUCTION:

Employer actions may result in both a claim of a violation of employee contractual rights under the parties’ collective bargaining agreement (CBA) and also a claim of a violation of statutory rights under the National Labor Relations Act (NLRA). For example, a union may claim that the discharge of an employee is both a violation of the parties’ “just cause” provision in its collective bargaining agreement and also assert the discharge is an unfair labor practice in violation of Sections 8(a)(3) and 8(a)(1) of the NLRA. Where provisions of the collective bargaining agreement and sections of the NLRA both apply to a workplace dispute should the National Labor

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(a) It shall be an unfair labor practice for an employer –
(1) to interfere with, restrain, or coerce employees in the exercise of the rights guaranteed in Section 7;
...
(3) by discrimination in regard to hire or tenure of employment or any term or condition of employment to encourage or discourage membership in any labor organization: ...
Relations Board (NLRB or Board) be precluded from adjudicating unfair labor practice charges where the matter has been the subject of an arbitration proceeding and award?

Section 10(a) of the National Labor Relations Act expressly provides that the Board is not precluded from adjudicating unfair labor practice charges even though they might have been the subject of an arbitration proceeding and award.3 And, the courts have uniformly so held.4 It is well settled that the Board has discretionary authority to establish or modify standards for deferring to arbitral decisions involving alleged violations of Sections 8(a)(3) and (1) of the NLRA.5 Some sixty years ago, in its Spielberg Mfg. Co.6 decision, the Board held that it would defer, as a matter of discretion, to arbitral decisions in cases in which the proceedings (1) appear to have been fair and regular, (2) all parties agreed to be bound, and (3) the decision of the arbitrator is not clearly repugnant to the purposes and policies of the Act. 7 The deferral doctrine announced in Spielberg was intended to reconcile the Board’s obligation under Section 10(a) of the Act to prevent unfair labor practices with the federal policy of encouraging the voluntary settlement of labor disputes through arbitration.8 Some thirty years later, in its Olin Corp. decision the Board modified the deferral standard, holding that deferral is appropriate where the contractual issue is “factually parallel” to the unfair labor practice issue, the arbitrator was presented generally with the facts relevant to resolving that issue and the award is not “clearly repugnant” to the Act.9

In 2014, contending that the Olin deferral standard is inadequate to ensure that employees’ statutory rights are protected in the arbitral process the General Counsel of the NLRB urged the Board to adopt a more demanding standard in Sections 8(a)(3) and 8(a)(1) cases in the Board’s Babcock & Wilcox Construction Co. Inc. case.10 The Board majority subsequently announced a new standard for deferring to post-arbitral decisions in Section 8(a)(1) and (3) cases. And in doing so the

3 29 U.S.C.§ 160 (a): The Board is empowered … to prevent any person from engaging in any unfair labor practice… affecting commerce. This power shall not be affected by any other means of adjustment or prevention that has been or may be established by agreement, law, or otherwise....
5 Id.
6 112 NLRB 1080 (1955).
7 Id. at 1082.
10 361 NLRB. No. 132  (Dec. 15 2014) at 1.
Board modified its standard for prearbitral deferrals and deferral to grievance settlements. The Board declared that its new standard will apply only prospectively. Thus the Board applied the existing Spielberg/Olin standard to the facts of the Babcock & Wilcox case.

II. THE BABCOCK & WILCOX DECISION: STILL APPLYING THE EXISTING SPIELBERG/OLIN STANDARD

A. The Factual Summary and the Arbitration Decision

Charging party Coletta Beneli was employed by Babcock & Wilcox Construction Company (Babcock) as a forklift and crane operator at the Arizona Public Service (APS) coal power plant in Joseph City Arizona where Babcock provided field construction and maintenance service for APS. She served as union job steward there for the International Union of Operating Engineers Local 428 (IUOE). In February and March of 2009 Beneli challenged several of Babcock’s managerial actions as violative of the CBA. Only a few hours before suspending Beneli, Babcock’s project Superintendent Christopher Goff told the Union’s assistant business manager Shawn Williams that he wanted to discharge Beneli because she was raising contractual issues and trying to tell the company what it was supposed to pay employees. The administrative law judge (ALJ) summarized the facts as follows:

Williams testified that at about 8 a.m. on March 11, he received a call from Goff. Ralph McDesmond, safety representative was also on the call. Goff told Williams that he wanted to terminate Beneli because she had overstepped her boundaries as the Union’s steward and was crossing the line into management. Williams testified that Goff said Beneli was raising contractual issues and trying to tell Respondent what they are supposed to pay employees. Williams stated that in his view Beneli was acting as a steward should. Goff stated that Beneli should not be getting APS, Respondent’s customer, involved by raising contractual issues with APS. Williams said that in the future Beneli would raise contractual issues solely with Respondent. Williams stated that if Goff discharged Beneli, the Union would fight the discharge and file a grievance.

On March 11, sometime after 2:00 p.m., Alsop [a foreman and union member who had informed Beneli that he had not been paid properly] told Beneli that Goff had called him and wanted them both to go to

11 Id. at 4, 12, 13.
12 Id. at 13, 14.
13 Id. at 5, 37.
14 Id. at 37.
15 Id. at 5.
16 Id. at 6, 37.
Respondent’s office. Beneli and Alsop went to Goff’s office, where they found McDesmond and Matt Winklestine, safety representative, waiting. Winklestine told Beneli that she was being suspended for violating two safety policies earlier that day. Specifically Winklestine said Beneli had been observed eating a pastry during the jsa [job safety analysis] meeting, and that she had failed to fill out a separate jsa form. Beneli laughed and asked Winklestine where it stated she could not eat pastry during the jsa meeting. Winklestine said he would look for it. Beneli again asked to see it in writing. Winklestine said he did not have to show Beneli anything. Winklestine then stated that Beneli was being suspended for 3 days without pay for the safety violations.

Beneli turned to McDesmond and said, “So this is the f—g game you guys are going to play?” Almost immediately Winklestine and McDesmond pointed their fingers at Beneli and stated that she was terminated. McDesmond said that Beneli had threatened them. Beneli said that she did not threaten anyone but said, “is this the f—g game you are going to play?” McDesmond stated there you go again and once more accused Beneli of threatening them. McDesmond then told Rhonda Roberson to prepare termination papers and to cut Beneli’s final check. 17

The union grieved the discharge and it was progressed to step 4, which calls for a hearing before the grievance review subcommittee. A quorum of five representatives consisting of at least two management representatives, two labor representatives, and one NMAPC staff representative considers and decides a grievance at Step 4. All subcommittee determinations are based upon the facts presented, both written and oral, and any decision rendered is final and binding and not subject to any appeal.18

On October 8, 2009, the subcommittee hearing was conducted and the union argued that Beneli was fired for certain steward activities in violation of the NLRA and Board decisions.19 By letter also dated October 8, 2009 the subcommittee issued its decision denying the grievance and upholding Beneli’s discharge. As set forth in the ALJ’s decision the subcommittee noted:

The “issue was the Union’s contention the [Respondent] violated Article XXIII Management Clause of the National Maintenance Agreement by terminating the grievant, without just cause, for the grievant’s use of profanity” and that the subcommittee “reviewed all the information submitted both written and oral” and determined that

17 Id. at 37, 38.
18 Id. at 39.
19 Id. at 6.
“no violation of the National Maintenance Agreement occurred and therefore, the grievance was denied.\(^{20}\)

The majority decision of the Board stated:

The [subcommittee’s] decision states only that Beneli’s termination for using profanity did not violate the contractual prohibition against termination without just cause; it fails even to mention the statutory issue or the contractual prohibition against retaliation for union activity. In denying the grievance, the subcommittee may have considered the statutory issue, or it may not have, there is simply no way to tell.\(^{21}\)

**B: The Board’s Decision Deferring to the “Subcommittee Arbitration”**

Under the Spielberg/Olin standard, the Board defers to arbitral awards and final disposition of joint employer-union committees when: (1) all parties agreed to be bound by the decision of the arbitrator; (2) the proceedings appear to be fair and regular; (3) the arbitrator adequately considered the unfair labor practice issue \(^{(3)}\) under Olin the Board added the requirement that the contractual issue must be factually parallel to the unfair labor practice issue; and the arbitrator must have been presented generally with the facts relevant to resolving the unfair labor practice issue.]; and (4) the award is clearly not repugnant to the policies of the Act.\(^{22}\) Under Olin the Board also places the burden on the party opposing deferral to demonstrate that the standards for deferral have not been met.\(^{23}\)

Applying the above standard, the administrative law judge deferred to the Subcommittee’s decision.\(^{24}\) And the Board determined that the decision would appear to qualify for deferral under the above set forth current deferral standard, stating as follows:

As the judge found, it is conceded that the proceedings were fair and regular, and that all parties agreed to be bound by the panel’s decision. Further, under Olin, the Subcommittees would be deemed to have “adequately considered” the unfair labor practice issue – whether Beneli was discharged for her steward activities – even if it actually did not consider that issue at all, because it was “factually parallel” to the contractual issue – discharging Beneli for the use of profanity – and the Subcommittee was “presented generally” with the facts relevant to resolving the statutory issue. Additionally, the

\(^{20}\) *Id.* at 38.

\(^{21}\) *Id.* at 6.

\(^{22}\) Spielberg, 112 NLRB at 1082; Olin, 268 NLRB at 574.

\(^{23}\) *Id.*

\(^{24}\) 361 NLRB No. 132 at 39. The ALJ credited the testimony of Beneli and Williams, nevertheless the ALJ stated that the Subcommittee could have credited Babcock’s witnesses. And while the ALJ would have reached a different conclusion, he did not find the factual decision repugnant to the policy of the Act.
The absence of any evidence that the statutory issue was considered presents no impediment to deferral under the current standard because the General Counsel has the burden to show that the statutory issue was not considered. Finally, the decision to deny Beneli’s grievance was not found to be repugnant to the Act, because it was susceptible to an interpretation consistent with the Act.  

Because the General Counsel failed to demonstrate that the Subcommittee’s decision was clearly repugnant to the Act, the Board deferred to the Subcommittee’s decision and dismissed the complaint.  

III. THE CHANGE IN THE NLRB’S DEFERRAL STANDARD AFTER THIRTY YEARS UNDER OLIN

"Arbitration" according to Roberts’ Dictionary of Industrial Relations is a “procedure whereby parties agree to submit a dispute to a third party known as an arbitrator for a final and binding decision.” Usually this involves mutual selection of the third party by the parties themselves. The Federal Mediation and Conciliation Service, the American Arbitration Association and the National Mediation Board maintain panels of qualified labor arbitrators, from which the parties can select an arbitrator acceptable to both parties who will be guided in conduct and procedures by the Code of Professional Responsibility for Arbitration of Labor Management Disputes.

In the Babcock case Coletta Beneli’s grievance was progressed to step 4 of the grievance review subcommittee consisting of two management, two labor representatives and one NMAPC staff representative. The NMAPC staff representative is a non-voting facilitator. In effect the decision is made jointly by the union and management members.

25 Id. at 6.
26 Id. at 14.
27 Roberts, ROBERTS’ DICTIONARY OF INDUSTRIAL RELATIONS, 4th ed. (BNA Books, 1994) at 47.
29 361 NLRB No. 132 at 38.
30 Telephone interview with Brian Powers, GC, IUOE, on March 14, 2016. The absence of neutral voting member on a bipartite or joint panel would not necessarily preclude deferral. See Denver-Chicago Trucking Co., 132 NLRB 1416 (1961). But where, in addition it appears that all members of the bipartite panel are or would be arrayed in interest against the charging party, deferral would not be appropriate. Roadway Express Inc., 145 NLRB 513 (1963). The ALJ relied on K-Mechanical Services, Inc., 299 NLRB 114, 117 (1990) as authority to apply the Spielberg/Olin deferral standard to determinations by joint employer-union committees that are final dispositions of a grievance. Under the parties’ CBA should the NMAPC step 4 process have failed to yield a decision then at Step 5 the matter would have been submitted to the American
The decision rendered is final and binding and not subject to any appeal.\textsuperscript{31} On the same date as the step 4 hearing the Subcommittee also issued its letter decision that:

The “issue was the Union’s contention the [Respondent] violated Article XXIII Management Clause of the National Maintenance Agreement by terminating the grievant, without just cause, for the grievant’s use of profanity” and that the subcommittee “reviewed all the information submitted both written and oral” and determined that “no violation of the National Maintenance Agreement occurred therefore, the grievance was denied.”\textsuperscript{32}

The decision made without a neutral, professional arbitrator fails to even mention the statutory issue or the contractual prohibition in the CBA against retaliation for union activity. As the Board states: the Subcommittee may have considered the statutory issue, or it may not have; there is simply no way to tell.\textsuperscript{33} Under \textit{Olin} the Subcommittee would be deemed to have “adequately considered” the unfair labor practice issue – whether Beneli was discharged for her steward activities – even if it actually did not consider that issue at all, because it was “factually parallel” to the contractual issue – discharging Beneli for the use of profanity – and the Subcommittee was “presented generally” with the facts relevant to resolving the statutory issue.\textsuperscript{34} Moreover, the absence of any evidence that the statutory issue was considered presents no impediment to deferral under the current standard because the General Counsel has the burden to show that the statutory issues were \textit{not} considered.\textsuperscript{35} Thus, the standards established under \textit{Olin} may impede access to the Board’s remedial processes if disciplinary actions that are in fact unlawful employer reprisals for union activity are upheld in “arbitration.” Coletta Beneli was left without any forum to vindicate her Section 7 rights under the NLRA.\textsuperscript{36} Under the new \textit{Babcock} deferral standard the \textit{Olin} risk will no longer be countenanced by the Board. By utilizing Coletta Beneli’s untenable demise under the \textit{Olin} guidance, the NLRB has made a compelling case to change its \textit{Spielberg/Olin} deferral standard as set forth in \textit{Babcock}.

\textsuperscript{31} 361 NLRB No. 132 at 38.
\textsuperscript{32} \textit{Id}.
\textsuperscript{33} \textit{Id}. at 7.
\textsuperscript{34} \textit{Id}.
\textsuperscript{35} \textit{Id}.
\textsuperscript{36} Coletta Beneli is in the process of progressing a case against the NLRB to the 9\textsuperscript{th} Circuit Court of Appeals. \textit{See} Re: 9\textsuperscript{th} Cir. No. 15-73426—\textit{Coletta Kim Beneli v. NLRB}, Board case No. 28-CA-022625.
IV. DEFERRAL TO EXISTING AWARDS (POST ARBITRAL DEFERRAL)

Under Babcock, the Board will defer to an arbitrator’s decision in Section 8(a)(3) and (1) unfair labor practice cases where the arbitration procedures appear to have been fair and regular and the parties agreed to be bound,\(^37\) and the party urging deferral demonstrates that: (1) the arbitrator was explicitly authorized to decide the unfair labor practice issue; (2) the arbitrator was presented with and considered the statutory issue, (or was prevented from doing so by the party opposing deferral) and (3) Board law reasonably permits the arbitral award.\(^38\)

Moreover it is important to underscore that Babcock places the burden of proving that each element of the deferral standard is satisfied on the party urging deferral, typically the employer. \(^39\)

A. Explicit Authorization

The arbitrator must be explicitly authorized to decide the statutory issue. This requirement is met by showing either that: (1) the specific statutory right at issue was incorporated in the collective-bargaining agreement, or (2) the parties agreed to authorize arbitration of the statutory issue in the particular case.\(^40\)

B. Statutory Issue was Presented and Considered

The arbitrator must have been presented with and considered the statutory issue (or have been prevented from doing so by the party opposing deferral). The Board stated that either party can raise the statutory issue before the arbitrator.\(^41\) Merely informing the arbitrator of the unfair labor practice allegation in a pending charge will usually be sufficient to show that the issue was presented.\(^42\)

The Board stated in part:

We shall find that the arbitrator has actually considered the statutory issue when the arbitrator has identified that issue and at least generally explained why he or she finds that the facts presented either do or do not support the unfair labor practice allegation. We stress that an arbitrator will not be required to have engaged in a detailed exegesis of Board law in order to meet this standard. We recognize that many arbitrators, as well as many union and employer

\(^{37}\) These traditional requirements under Spielberg and Olin were not affected by the Babcock decision.

\(^{38}\) Babcock, 361 NLRB No.132 at 2.

\(^{39}\) See Memorandum GC 15-02 (Feb. 10, 2015) p. 2.

\(^{40}\) 361 NLRB No.132 at 5.

\(^{41}\) Id. at 7.

\(^{42}\) Id. at 7 note 14.
representatives who appear in arbitral proceedings, are not attorneys trained in labor law matters.\textsuperscript{43}

\textbf{C. The Arbitral Award is Reasonably Permitted Under Board Law}

Board law must reasonably permit the award. By this the Board means that the arbitrator's decision must constitute a reasonable application of the statutory principles that would govern the Board's decision, if the case were presented to it.\textsuperscript{44} The arbitrator need not reach the same result as the Board would reach, only a result that a decision maker reasonably applying the Act could reach.\textsuperscript{45} In deciding whether to defer, the Board will not engage in the equivalent of \textit{de novo} review of the arbitrator's decision.\textsuperscript{46}

\textbf{D. Prospective Application of the New Babcock Postarbitral Deferral Standard}

The Board's \textit{Babcock} standard will apply only prospectively, with certain exceptions, because the Board stated it would be unfair to parties who relied on the continued applicability of the current \textit{Spielberg/Olin} standard when they negotiated their existing contracts.\textsuperscript{47}

\textbf{V. REQUIRED GRIEVANCE ARBITRATION MACHINERY INSTEAD OF BOARD PROCEEDINGS (PREARBITRATION DEFERRAL)}

In \textit{Babcock} the Board modified its standard for prearbitration deferral set forth in \textit{Collyer Insulated Wire} \textsuperscript{48} and \textit{United Technologies Corp.} \textsuperscript{49} The Board stated:

\textsuperscript{43} \textit{Id.} at 7.
\textsuperscript{44} \textit{Id.}
\textsuperscript{45} \textit{Id.}
\textsuperscript{46} \textit{Id.}
\textsuperscript{47} \textit{Id.} at 13-14. \textit{See Memorandum GC 15-02 (Feb. 10, 2015) p. 9}, where the General Counsel lists the following rules to determine whether to evaluate an arbitration award under \textit{Olin} or \textit{Babcock} in pending or future cases raising allegations of Section 8(a)(1) and (3). \textit{Olin} applies if the arbitration hearing occurred on or before December 15, 2014, the date the \textit{Babcock} decision issued; \textit{Babcock} applies if the collective-bargaining agreement under which the grievance arose was executed after December 15, 2014. If the collective-bargaining agreement under which the grievance arose was executed on or before December 15, 2014, and the arbitration hearing occurred after December 15, 2014, which standard applies depends on whether the arbitrator was explicitly authorized to decide the statutory question (either in the collective-bargaining agreement or by agreement of the parties in a particular case). If the arbitrator was so authorized, then \textit{Babcock} applies, even if the Region initially placed the case on administrative deferral. If the arbitrator was not authorized to decide the statutory issue, then \textit{Olin} applies.

\textsuperscript{48} 192 NLRB 837 (1971).
\textsuperscript{49} 268 NLRB 557 (1984).
The AFL-CIO argues that the Board should not defer to the arbitral process unless the first prong of the postarbitral deferral standard is satisfied, that is, unless the arbitrator was explicitly authorized to decide the unfair labor practice issue. We agree. There is no apparent reason to defer to the arbitral process if it is plain at the outset that deferral to the arbitral decision would be improper. Thus, we shall no longer defer unfair labor practice allegations to the arbitral process unless the parties have explicitly authorized the arbitrator to decide the unfair labor practice issue, either in the collective-bargaining agreement or by agreement of the parties in a particular case.  

VI. DEFERRAL TO GRIEVANCE SETTLEMENTS

Under Babcock, the Board will apply essentially the same deferral standard to grievance settlements as it does to arbitral decision in Section 8(a)(1) and (3) cases. In such cases, it must be shown that: (1) the parties intended to settle the unfair labor practice issue; (2) they addressed that issue in the settlement agreement; and (3) Board law reasonably permits the settlement agreement. In assessing whether the negotiated settlement is reasonably permitted, the Board will assess the agreement in light of the factors applicable to other non-Board settlement agreements, as set forth in Independent Stave Co.

VII. THE NEW BABCOCK DEFERRAL STANDARD IS WARRANTED.

Dissenting to the changes in the deferral standard Member Miscimarra asserted that the Board’s Babcock & Wilcox decision damages the parties’ reliance on their collective bargaining agreements as “final and binding.” Moreover, he argued that the standard undermines the parties’ ability to negotiate contract terms voluntarily and requires a wholesale rewriting of CBA “cause” and arbitration provision. Member Johnson’s dissent urged that departure from the current longstanding deferral policy is unwarranted.

50 361 NLRB No. 132 at 12, 13.
51 Id. at 13.
52 287 NLRB 740, 743 (1987). The Board in Independent Stave identified the following non-exclusive list of factors to consider in evaluating settlements: (1) whether all parties involved agreed to be bound by the non-Board settlement; (2) whether the proposed settlement is reasonable in light of the alleged violation, the risks of litigation, and the stage of litigation; (3) whether there is any indication of fraud, coercion or duress regarding the parties’ settlement; and (4) whether the respondent has a history of violations or of breaching previous settlement agreements resolving unfair labor practices.
53 See 761 NLRB No. 132 at 16, 24.
54 Id. at 20-23.
55 See id. at 36.
A. Board Treatment of Statutory Section 8 (a) (3) and (1) Cases

In a situation where an individual has been disciplined or discharged by an employer allegedly in retaliation for employee activity specifically protected by the NLRA in a work environment where no collective bargaining agreement is in effect, the case will come before the Board members after: (1) unfair labor practice charges are filed with the Board’s regional office alleging violations of Sections 8 (a)(3) and (1); (2) an investigation is conducted and the Regional Director finds that formal action on the unfair labor practice allegations should be taken; (3) the General Counsel issues a complaint; (4) a hearing is held before an administrative law judge (ALJ) with a “Board attorney” representing the General Counsel (and the employee) and a retained attorney representing the employer, and the ALJ issues a decision and order in the case; and (6) an exception to the ALJ’s decision and order is filed with the Board, at which point the Board will find the employer either guilty of the unfair labor practice and order appropriate remedial action or find the employer not guilty and dismiss the case.

B. Comment on the Step 4 Decision by the Subcommittee: The “Arbitrators” In This Case.

Unlike the resolution of an unfair labor practice complaint before an administrative law judge, the matter in this case was resolved under Step 4 of the grievance procedure of the parties, set forth in their collective bargaining agreement. While consisting of five members and giving the illusion of a neutral member, only the two union members and the two management members had authority to vote on the disposition of the grievance, with their joint decision being final and binding on the parties. Had the joint committee of four deadlocked, the matter would have progressed to Step 5 with an actual arbitration, as administered by and under the procedures of the American

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56 The Administrative Law Judge (ALJ) function was created by the Administrative Procedure Act of 1946 to ensure fairness in administrative proceedings before Federal Government agencies. ALJs serve as independent, impartial triers of fact in formal proceedings requiring a decision on the record after a hearing. ALJs must have a full seven years of experience as a licensed attorney involving litigation in the government sector, and pass an examination testing their competency, knowledge, skills and abilities essential to their works. ALJs are held to a high standard of conduct to maintain the integrity and independence of the administrative judiciary. U.S. Office of Personnel Management, http://www.opm.gov/services-for-agencies/administrative-law-judges/.

57 See 361 NLRB No. 132 at 9; See also David P. Twomey, LABOR & EMPLOYMENT LAW, 66 (2013).

58 Telephone interview with Brian Powers, GC, IUOE, March 14, 2016.

59 361 NLRB No. 132 at 38.
Arbitration Association. Nevertheless, under existing Board law, the Board defers to such joint employer-union committees that are final dispositions of a grievance. Unlike an administrative law judge, a highly qualified, independent and impartial trier of fact obligated to properly apply Board law to the facts of record culminating in a written decision available to the parties, four individuals, two union representation and two management representatives made a final and binding decision on Coletta Beneli's contract claim and, without identifying the statutory issue or explaining facts supporting an unfair labor practice decision, they conclusively foreclosed her statutory rights under Section 8(a)(3) and (1) of the NLRA as follows:

The “issue was the Union’s contention the [Respondent] violated Article XXIII Management Clause of the National Maintenance Agreement by terminating the grievant, without just cause, for the grievant’s use of profanity” and that the subcommittee “reviewed all the information submitted both written and oral” and determined that “no violation of the National Maintenance Agreement occurred and therefore, the grievance was denied.

Under the NLRB’s rewriting of its deferral standard in Babcock, the employer would be obligated to show that the Subcommittee had been explicitly authorized to decide the statutory issue. No such showing existed in Ms. Beneli’s case. Moreover, at Step 4 the employer would have to show that the Subcommittee actually considered the statutory issue and generally explained in a decision why the facts presented do not support Ms. Beneli’s unfair labor practice allegations. Thus the joint decision of the Subcommittee, under the Babcock ruling would have required a statement of the facts for the record, including Beneli’s

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60 National Maintenance Agreement, Article VI – Grievances, Step 4 and 5...
62 361 NLRB No. 132 at 38.
63 Id. at 5.
64 See id.
activity as union steward enforcing the CBA, which led to the employer assessing a suspension without pay for failing to fill out a safety form and for eating a pastry during a safety meeting, which led to Beneli’s response “is this the f---g game you are going to play”; at which point two managers pointed their fingers at her and said she was terminated. Can you imagine two union representatives on a joint grievance decision, no longer able to hide behind a conclusionary statement as actually issued at Step 4, upholding the termination of a union steward on these real facts, in the construction industry? These facts simply “won’t write” as a basis to uphold a discharge under a just cause “standard” contained in a CBA. Nor, would a similar subcommittee appear to have the training and competency to apply “Board law” to the facts to make a determination on whether Section 8(a)(3) and (1) of the Act had been violated.

C. The Effect of the Babcock Decision on Deferring to Joint Employer-Union Committee Decisions Involving Statutory Rights.

In the Babcock case, Step 5 of the contractual grievance procedure required the progression of the case to true arbitration, where the parties would have an opportunity to select a mutually acceptable arbitrator, under the administration of the American Arbitration Association, to hear and decide the case. Under the new deferral standard, the parties would thus be able to select a neutral arbitrator with the background and experience to apply the Babcock standard and reach a final and binding decision on the contractual and statutory claims.

Broadly speaking it is highly unlikely that future Step 4 type contested subcommittee decisions, or joint employer-union committee decisions could be made to conform to the meticulous Babcock deferral standard. Future cases will therefore have to be progressed to the next step in the parties’ grievance – arbitration procedures which will likely provide for the selection of a neutral arbitrator highly qualified to resolve the contractual and statutory issues in question. It is highly likely, however, that a genuine settlement at a Step 4 type grievance hearing between a union and employer, acceptable to the grievant-charging party, could be drafted to meet the new deferral standard on settlements.

65 See id.
66 Id. at 38.
67 Id.
68 National Maintenance Agreement, Article VI, Step 5.
VIII. CONCLUSION

Judge Pollack, the impartial trier of fact in this case, credited the testimony of Ms. Beneli and union assistant business manager Shawn Williams. The Board majority compellingly used the plight of Ms. Beneli to demonstrate that the Olin deferral standard is inadequate to ensure that employees’ statutory rights are protected in the arbitral process. The Board, as a result, changed its deferral standard! The Board’s usual practice is to apply all new policies and standards in “all pending cases, in whatever stage.” However, stunningly, the Board left Ms. Beneli without a remedy, on the meritless position that “it would be unfair to the parties [nationwide] that have relied on the current standard in negotiating contracts....” It is difficult to imagine that any party in contract negotiations actually consciously “relied” on the continuation of the Spielberg/Olin standard. Moreover, only a fraction of the cases decided by the Board involve deferral issues. Basic fairness requires that the individual whose circumstances compelled the changed deferral policy, Ms. Beneli, should have the new policy apply to her, along with an appropriate remedy.

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69 361 NLRB No. 132 at 39.
70 Id. at 13.
71 Id. at 14.
72 Id.
73 Ms. Beneli has recently progressed a case against the NLRB and Babcock & Wilcox Construction Co., Inc. to the 9th Circuit of Appeals, No. 15-73426.
RELIGIOUS DISCRIMINATION AND REASONABLE ACCOMMODATION: THE IMPACT OF EEOC V. ABERCROMBIE

by Christine M. Westphal* and Susan C. Wheeler**

I. INTRODUCTION

The Supreme Court’s June 1, 2015 decision in *E.E.O.C. v. Abercrombie & Fitch Stores, Inc.* comes at a time when the number of claims of discrimination based on religion are increasing significantly. Between 2000 and 2010 the number of claims of religious discrimination made to the EEOC increased 96 percent. In 2015 the EEOC received 3,502 charges of religion-based discrimination; in 2000 there were only 1,939. Approximately one quarter of the claims are filed by Muslims. The 2016 primary election cycle, coupled with terrorist attacks in Europe that have been linked to immigrants from the Middle East, has witnessed a significant increase in the expression of anti-Muslim sentiments. At least one major party candidate is advocating for a moratorium on allowing Muslims to enter the United States. The increase in the public expression of anti-Muslim sentiments, particularly in the political context, highlights the importance of understanding the legal implications of religious discrimination and the role of the EEOC in enforcing anti-discrimination laws.
sentiments may lead to both an increase in requests for religious accommodations and claims of religious discrimination by Muslim employees. This paper will review the Supreme Court’s Abercrombie decision, and discuss the Abercrombie policies that prompted the litigation, some of the reasons for the increase in claims of religious discrimination, and the possible implications of this decision for businesses.

II. E.E.O.C. V. ABERCROMBIE & FITCH STORES, INC.

The case came to the Supreme Court on appeal from a summary judgment motion. Initially, the U.S. District Court for the Northern District of Oklahoma granted the EEOC’s motion for summary judgment as to liability. The U.S. Court of Appeals reversed and remanded. The EEOC appealed and certiorari was granted on October 2, 2014. There is some slight variation in the facts depending on the moving party, but those factual variations bear no significance to the outcome of the case. The Supreme Court summarized the facts:

Respondent Abercrombie & Fitch Stores, Inc., operates several lines of clothing stores, each with its own “style”. Consistent with the image Abercrombie seeks to project for each store, the company imposes a Look Policy that governs its employees’ dress. The Look Policy prohibits caps—a term the Policy does not define— as too informal for Abercrombie’s desired image.

Samantha Elauf is a practicing Muslim who, consistent with her understanding of her religion’s requirements, wears a headscarf. She applied for a position in an Abercrombie store, and was interviewed by Heather Cooke, the store’s assistant manager. Using Abercrombie’s ordinary system for evaluating applicants, Cooke gave Elauf a rating that qualified her to be hired; Cooke was concerned, however, that Elauf’s headscarf would conflict with the store’s Look Policy.

Cooke sought the store manager’s guidance to clarify whether the headscarf was a forbidden “cap.” When this yielded no answer, Cooke turned to Randall Johnson, the district manager. Cooke informed Johnson that she believed Elauf wore her headscarf because of her faith. Johnson told Cooke that Elauf’s headscarf would violate the Look

6 Supra, note 1.
8 Id.
Policy, as would all other headwear, religious or otherwise, and directed Cooke not to hire Elauf.\textsuperscript{11}

The only discrepancy in the record at the lower court was that Johnson testified that Cooke never informed him that Elauf wore the headscarf for religious reasons. However, Cooke was the manager charged with hiring new employees, and Cooke clearly testified she believed that Elauf wore the headscarf for religious reasons. After Cooke’s discussion with Johnson she altered Elauf’s evaluation so that Elauf was no longer qualified to be hired, and Elauf was not given an opportunity to work in the store.\textsuperscript{12}

The Petition for a Writ of Certiorari stated:

The question presented is whether an employer can be liable under Title VII for refusing to hire an applicant or discharging an employee based on a religious “observance and practice” only if the employer has actual knowledge that a religious accommodation was required and the employer’s actual knowledge resulted from direct, explicit notice from the applicant or employee.\textsuperscript{13}

The Court held that “explicit notice” from the applicant or employee of a religious basis for the request to be exempted from a company policy was not required and highlighted the difference between the Civil Rights Act and The Americans with Disabilities Act (which does require explicit notice).\textsuperscript{14} The Court also held that a showing of “actual knowledge” on the part of the employer was not necessary for the applicant or employee to succeed on a claim of disparate treatment; rather, the court stated that the applicant or employee need only show that the perceived need for religious accommodation was the “motivating factor” in the adverse employment decision, stating that “an individual’s actual religious practice may not be a motivating factor in the adverse employment decision, in failing to hire, in refusing to hire…” or in making any adverse employment decision.\textsuperscript{15}

The Court specifically reserved the decision as to whether knowledge of the religious nature of perceived need for an accommodation was required to show motivation, since in the case presented Cooke clearly stated that she believed Elauf wore the headscarf for religious reasons.\textsuperscript{16} By focusing on the concept of religion or religious practice as a “motivating factor” it would appear that the Court would also allow an action to go forward even where the employer is mistaken about the applicant or employee’s need for religious accommodation, if that mistaken belief that the applicant or employee requires accommodation based on religion “motivated” the employer’s adverse action.

\textsuperscript{11} Supra, note 1 at 2031.
\textsuperscript{12} Supra, note 7 at 1278.
\textsuperscript{13} Brief for Petitioner EEOC v. Abercrombie, 135 S.Ct. 44 (2014).
\textsuperscript{14} Abercrombie, 135 S.Ct. at 2032-3.
\textsuperscript{15} Id. at 2032.
\textsuperscript{16} Abercrombie, supra note 1.
This may be important because there is significant confusion about non-Christian religions and religious practice, particularly among recent immigrants. There are over 4,200 religions and it may well be impossible for an employer to determine if an activity, action, or request for accommodation is motivated by a “sincere religious belief” or is simply a personal preference or made out of respect for a cultural tradition. In the academic literature, Muslim identity has been “…analyzed in terms of race, ethnicity, culture, and religion…” In addition, only 73 percent of recent immigrants from the Middle East and Asia are Muslim, and while many immigrants from Pakistan and India are Muslim, many are not. Coptic Christians from Egypt, other sects of Christian Arabs, religious and non-religious immigrants from India and Sikhs might all face discrimination based on an employer’s mistaken belief that that are Muslim.

III. THE ABERCROMBIE “LOOK POLICY”

Abercrombie & Fitch Stores, Inc. (hereafter A&F) is a retailer with stores that target specific segments of the youth market. Abercrombie Kids, targets young children, Hollister targets middle and high school aged shoppers; Abercrombie & Fitch focuses on high school and college aged shoppers, and Gilly Hicks and Ruehl No. 925 for those who are in their twenties and early thirties. The “Look Policy” was instituted by Mike Jeffries shortly after he took over as CEO of A&F in 1992. At that time A&F was known primarily as a retailer of tropical safari clothing. Jeffries sought to change the image and marketing strategy of the retailer. In his own words the focus of his strategy was to “market to cool, good-looking people.” He achieved that goal by hiring what he termed “Good looking people”, who initially turned out to be young white men, and carefully controlled both the “look” of employees and the atmosphere in their stores. Employees, especially employees who worked on the floors of the retail stores, were not only expected to be attractive, but to wear A&F clothing (or clothing consistent with the A&F look); to keep the personal grooming in compliance with the “Look Policy” which dictated appearance down to the acceptable length of their fingernails. Up until approximately 2008 the strategy was very successful in terms of sales and company profitability, but the focus on employee youth and appearance lead to a series of lawsuits.

17 Ghumman et al., supra note 2 at 450.
19 Ghumman et al., supra note 2 at 450.
20 Id.
22 Id.
Beginning in 1999 the EEOC received complaints “… alleging national origin discrimination and wrongful termination…”23 In 2003, A&F was the subject of a class action suit which alleged the company “discriminated against minorities on the basis of race, color, and/or national origin….”24 In 2004, a gender class action suit was filed. All three actions were resolved as part of a Consent Decree in November 2004.25

In 2009, A&F was charged with disability discrimination for firing a worker in its London store because she violated their “Look Policy” by covering her prosthetic arm with a non-A&F sweater.26

In 2013, when A&F announced that it would no longer sell clothes larger than size 10, change.org27 sponsored a petition28 signed by more than 80,000 people in protest of the policy.29

In 2009, A&F was sued by the EEOC in the first case involving the refusal to hire a Muslim job applicant because of her headscarf (hijab). That case ultimately reached the Supreme Court becoming EEOC v. Abercrombie & Fitch. A second case was brought in 2010, but was settled, and A&F announced that it would accommodate applicants and employees wearing headscarves for religious reasons in the future.30 In 2015, A&F also settled an immigration discrimination charge.31

In December of 2014, Michael Jeffries resigned from A&F. While the Look Policy he instituted had led to early success the value of the brand had suffered

24 Id.
25 Id. Abercrombie agreed to take affirmative steps to, among other things, implement Equal Employment and Diversity practices, create an Office of Diversity, institute an internal complaint procedure, provide EEOC compliance training for store and general managers, institute a written recruitment and hiring protocol, and hire a diversity consultant.
27 Change.org is a Certified B corporation that allows individuals, business and institutions to start petitions on its website https://www.change.org/start-a-petition (last visited May 20, 2016).
through the various lawsuits and the failure to evolve the marketing strategy in the new millennium.

Finally in April 2015, A&F essentially abandoned its Look Policy. It was reported that the company would “no longer hire employees based on their physical attractiveness… relax the dress code… and no longer station shirtless men at its stores to help lure in customers.”

Losing in the Supreme Court was anti-climactic.

IV. RELIGIOUS ACCOMMODATION

One of the issues that Abercrombie presented that was not considered on appeal is its potential impact on the “undue hardship” defense to the denial of a religious accommodation requests. Courts presently rely on the standard articulated by the Supreme Court in *Trans World Airlines, Inc. v. Hardison* that an accommodation burdens the employer if it requires “more than a de minimis cost.” It should be noted that the accommodations requested by Hardison, which involved relieving him of work shifts on Saturdays, would have required Trans World Airlines to incur actual, quantifiable monetary costs, but by holding that any de minimis cost would meet the undue hardship threshold, the Court left employers wide discretion to claim that any accommodation would result in an undue hardship. As a result, courts have given great deference to a company’s assertion that projecting a positive image or protecting a company’s brand would be sufficient to support a claim of undue hardship. Typical of the earlier cases where courts have tried to balance a request for an exemption from a company’s dress code based on religious practice against the company’s desire to protect its brand and public image would be *Cloutier v. Costco Wholesale*. In *Cloutier*, the First Circuit Court discussed “undue hardship” citing the same cases as the lower court in *Abercrombie* but reached a different decision. The *Cloutier* Court gave greater deference to Costco’s assertion that allowing its cashier to have facial piercings would impair the professional image of its workforce and therefore create an under hardship.

In contrast, the District Court in *Abercrombie* seemed to require that Abercrombie demonstrate through specific examples, studies or data that the accommodation would pose an undue hardship citing the 10th Circuit holding in *Hardison* that “the magnitude as well as the fact of hardship must be determined by examination of the facts of each case.”

Because the Abercrombie Look Policy was so thorough and specific, Abercrombie was forced to make multiple adjustments and exceptions to the

32 Kaplan, *supra* note 27.
35 Cloutier is also interesting because the Court accepts the sincerity of the plaintiff’s religious belief in the Church of Body Modification, an online religion with approximately 1,000 other adherents.
policy and its failure to determine the actual impact of these exceptions on sales or customer perception caused the Court to discount the testimony of Abercrombie’s expert witness. The District Court stated: “if Abercrombie has never granted exceptions, or perhaps even if it had never granted exceptions for headscarves, this omission might be understandable.” But the expert’s failure to analyze the impact of the exceptions, according to the District Court, caused his opinion to be too speculative to “establish actual hardship” if Abercrombie had allowed Elauf to wear a headscarf while at work.

It is unlikely that Costco would have been able to prove “undue hardship” if it had to meet the standard articulated by the lower court in Abercrombie that it provide specific examples, studies or data. Costco offered no specific examples, studies or data; while Cloutier stated that she had not received any negative remarks or complaints from customers about her facial piercings, the Court discounted her statements and opined, “it is axiomatic that, for better or worse, employees reflect on their employers.” It is possible that a conservative judge simply found the facial piercings unacceptable and could not imagine why the Court should penalize Costco for failure to accommodate Cloutier’s facial piercings even if she claimed they were religious in nature. As one writer noted, the District Court “… often employed derogatory terms or placed cynical quotes around the word “religious” when referring to Cloutier’s beliefs.” This would seem to indicate that the Cloutier courts might have felt that The Church of Body Modification was not a real religion. It remains to be determined if lower courts will use the holdings in Abercrombie to require that employers provide more significant proof when claiming that an accommodation of its dress or hygiene policies would result in an undue hardship.

The lower court holdings in cases where religious accommodation is denied because it might damage a corporation’s brand or image have not been decided in a consistent manner, as the contrast between the lower court decisions in Abercrombie and Cloutier demonstrate. Some writers have argued that either the courts, the EEOC or Congress should set a consistent standard so that employers can be confident of the burden they should meet.

V. INCREASES IN CLAIMS OF RELIGIOUS DISCRIMINATION

Much of the recent increase in religious discrimination cases can be attributed to the “increased religious diversity in the American workforce.” Fully a quarter

37 Id.
40 Ghumman et al., supra note 2 at 439.
of the claims have been brought by Muslims and Muslims are the fastest-growing religious group in the United States. This growth is fueled both by “native” converts and by recent immigrants. As the political situation in the Middle East continues to deteriorate, millions of Muslims and Non-Muslim Arabs are finding themselves displaced. The United States can expect to receive a steady stream of new immigrants from the Middle East in the foreseeable future.

It is important for employers to recognize that although the “American workplace may be secular in nature, the majority of work policies and procedures favor Christian practices and observances.” Devout Muslims might request a wide range of possible accommodations from prayer breaks to office decorations during the holiday Eid ul-Fitr which celebrates the end of the Ramadan fasting period and has been compared to Christmas in both significance and spirit. When Muslims’ requests for religious accommodation are denied and employees are subjected to Christian traditions in the workplace, such as Christmas parties and decorations or taking an optional day off on Good Friday, they will reasonably feel that there has been religious discrimination.

The intersection between evangelical Christianity and other conservative religious movements and liberal political initiatives such as gay rights and the Affordable Care Act (sometimes characterized as the culture wars) may also continue to drive religious discrimination suits. On one side, evangelical Christians and other conservative religious groups feel that they are forced to accept actions and behaviors that they consider sinful. The Religious Freedom Restoration Act of 1993 was enacted to protect freedom of religion and served as the basis of the Hobby Lobby decision which allowed Hobby Lobby to eliminate birth control coverage from its employee health plan even though such coverage was required by the Affordable Care Act. Since that decision a number of states have enacted Religious Freedom Acts which at least some activists and authors believe will allow discrimination particularly against gay and lesbian employees and potential customers.

On the other side, reverse religious discrimination claims have been described as “a popular method for redressing sexual orientation discrimination in jurisdictions where such discrimination is not prohibited.” With the Supreme Court’s decision in Obergefell, same-sex marriage is now established.
nationwide and it is likely that there will be more claims of reverse religious
discrimination brought by gay people. For example, in states where the law does
not prevent discrimination on the basis of sexual orientation, there are likely to be
numerous situations where newly married gay employees are fired when they
attempt to add their new spouse to the company health plan.

Finally, employers are already struggling to accommodate evangelical
Christians and others with strong religious beliefs who find diversity training
which seeks to incorporate acceptance of all religions and lifestyles offensive. All
of these trends will continue to impact the number of religious discrimination
complaints in the future.

VI. CONCLUSION

Because the Supreme Court’s decision in *EEOC v. Abercrombie* focused on
the motivation for adverse employment actions, it has potentially made it more
difficult for employers to avoid religious discrimination claims. While the Court
has suggested that some knowledge of the religious nature of the applicant or
employee actions or requests for accommodations may be necessary to meet the
motivation standard, the justices have specifically reserved decision on that issue.
Best practices would suggest that all employers have a clear and reasonable dress
code and employee policies and when employees violate the policies, the
employer should first ask the employee to correct the violation. If the employee
claims the action is the result of “a sincerely held” religious belief, then the
employer should attempt to provide a reasonable accommodation. The employer
may feel that accommodating the employee presents an “undue hardship” but that
may be more difficult to prove in the future, particularly if more courts require
actual evidence to support employer claims of “undue hardship.”

The focus on motivation may also prove problematic in other circumstances.
If a prospective employee comes to an interview wearing a tee shirt with “Gay
People Will Burn in Hell” printed on the front, is the employer’s refusal to hire
the perspective employee religious discrimination? If the employer never hires
prospective employees who come to the interview wearing a tee shirt with a
slogan, the “motive” for denying the applicant employment may be non-
discriminatory. If the employer states that he or she does not think someone
wearing a “religious” button or tee shirt slogan would be a good fit with their
company culture than a religious discrimination claim may be successful. That
would also be true if the employer took an adverse employment action against an
employee who wore a tee shirt or button with the slogan “Gay People Will Burn
in Hell” on casual Friday or at an informal company function such as the annual
picnic. In both cases it would be easy for a court to find that the employee’s
religious belief was the “motivating factor” in the adverse action, leaving the
employer to prove that the belief could not be reasonably accommodated.

The decision may also prove problematic for job applicants and employees.
They will have to balance their desire for employment against their potential need
for religious accommodation. In the *Abercrombie* case the applicant, Samantha
Elauf, tried to minimize the impact of her religious practices on her job search. Before applying for the position at Abercrombie, she tried to determine if Abercrombie would accommodate her headscarf by making an informal inquiry of a friend who worked in the store. She only applied after she informally received information that Abercrombie might accommodate the headscarf because her friends had witnessed other workers wearing “caps” in different Abercrombie stores. What would she have done if she had been told in the interview that her hijab violated the dress code? Employers may need to be more aggressive about notifying employees of dress codes or other restrictive policies during interviews without necessarily asking about religious practices or beliefs. That will leave prospective employees with a potential ethical dilemma; do they declare their religious beliefs or possible need for accommodations during the interview, even where they suspect it might limit their opportunity for employment, or do they wait until after they have been employed to request an accommodation. By waiting to request an accommodation of a religious practice, they may increase the possibility for employment but the employer may feel tricked or deceived. Beyond the legal implications of Abercrombie and other religious accommodation cases lie the complex interpersonal issues that will need to be faced as employers adjust to an increasingly diverse workforce.