



## **Ninth Circuit Scrutinizes Facts To Revive Poorly Drafted Sexual Harassment Suit**

The Ninth Circuit Court of Appeals recently revived a Title VII sexual harassment case that had been dismissed by the trial court, finding a material issue of fact as to whether the employer had taken measures to remedy its employees' complaints of sexual harassment. In *Taybron v. City and County of San Francisco*, a federal district court dismissed the sexual harassment complaint of two San Francisco Municipal Railway (Muni) employees, finding that their employer had taken measures necessary to remedy their sexual harassment complaints. Under Title VII (but not California state law), if an employee is harassed but does not suffer a "tangible employment action," such as a termination or a demotion, the employer can avoid liability by proving it took "reasonable care" to prevent and promptly correct any sexually harassing behavior. On appeal, the Ninth Circuit reversed the summary judgment that had been entered for Muni, finding a question of fact whether Muni had done enough to prevent the harassment. The court pointed to evidence that Muni failed to remedy the situation despite the plaintiffs' numerous oral complaints; that there were substantial delays before an alleged harasser was disciplined; that the plaintiffs were discouraged from complaining about the harassment they faced; and that Muni's internal equal employment opportunity (EEO) office failed to interview several employees and managers involved in the harassment disputes. The appellate court went out of its way to search for evidence of disputed facts despite the poor quality of the plaintiffs' attorney's summary judgment filings. This case demonstrates how many courts will do all they can to protect employees if the employer's sexual harassment complaint procedures are not in full compliance with state and federal law.

## **Reorganization After Acquisition May Provide Legitimate, Nondiscriminatory Reason For Termination**

The California Court of Appeal recently dismissed an age discrimination suit against a company that had been acquired and reorganized, finding that the employee lacked the necessary skills for a new position. In *Gibbs v. Consolidated Services*, Robert Gibbs worked for Atlas Transport as an operations manager. When Consolidated Services acquired Atlas, it reorganized Atlas, resulting in an increase in the responsibilities of Gibbs' position. Gibbs admitted that he lacked computer skills and could not use Consolidated's new routing software, requirements for the restructured position, so he requested a transfer to a driver position. In response, his supervisor told Gibbs, "Maybe you're getting too old." On two other occasions, a subordinate employee made similar comments about Gibbs' age. In

view of Gibbs' lack of qualifications for the restructured position and the fact that Gibbs had recently received a written warning for harassment and often dealt with other employees in an overbearing and offensive manner, Gibbs' supervisor decided to terminate Gibbs' employment. When Gibbs again asked for a driver position, his supervisor told him none was available, even though there was, in fact, at least one such position available. The appellate court upheld summary judgment for Consolidated, finding Gibbs' inability to perform the new responsibilities of the reorganized position and his unprofessional demeanor constituted a legitimate, nondiscriminatory reason for the termination. The court further held that when an employer modifies its workforce for business reasons, it has no obligation to transfer an employee to another position within the company, so long as it does not treat other employees not in the protected category more favorably. The Court found the supervisor's statement that Gibbs might be too old for a driver position, as well as the subordinate's similar statements, to be nothing more than "stray remarks" that played no role in the termination decision. Companies involved in acquisitions and reorganizations should welcome this decision as a positive development, but should continue to be vigilant to prevent discrimination of any kind.

## **Punitive Damages, But Not Attorneys' Fees, Must Be Included In Successful Plaintiff's Taxable Income**

The Ninth Circuit Court of Appeals has held that economic and punitive damages in a wrongful discharge lawsuit are not excludable from an individual's taxable income where the lost wages damages are caused by the termination of employment and not alleged personal injuries. In *Banaitis v. Commissioner of Internal Revenue*, Sigitas Banaitis was awarded more than \$8.7 million, including \$5 million in punitive damages, in a wrongful discharge case against his former employer. The defendants paid approximately \$3.9 million directly to Banaitis' attorney based on a contingency fee agreement, and paid the rest to Banaitis. Banaitis did not report any of the award as taxable income, claiming it was excludable under the Internal Revenue Code's exception for damages received "on account of personal injuries or sickness." The IRS disagreed with Banaitis' characterization, and issued a deficiency notice that he owed an additional \$1.7 million in income tax. The Tax Court agreed with the IRS, holding that Banaitis was not entitled to exclude economic damages, punitive damages, or attorneys' fees from his gross income. The Ninth Circuit held that the economic and punitive damages were not excludable, because the underlying claim for lost wages was based on the employer's wrongful conduct, not based on any personal injuries that prevented Banaitis

from working. To arrive at that conclusion, the court applied a two-part test: (1) the underlying claim must be a tort-type claim, which wrongful discharge is, and (2) the damages received must be “on account of personal injury or sickness,” which Banaitis’ were not. The Ninth Circuit reversed the Tax Court on the issue of taxability of the attorneys’ fees portion of the award. While noting the general rule that plaintiffs cannot avoid the tax consequences of a personal injury judgment by assigning a portion of the proceeds to their attorneys in advance as part of a contingency fee agreement, the court found that the unique characteristics of Oregon law dictated a different result. Specifically, the court held that Oregon law provides an attorney with a special property right in a damages judgment, including an attorney’s lien which is superior to all liens except tax liens. California employers should note, however, that attorneys’ fees portions of judgments in California are, in contrast, includable in a plaintiff’s gross income. Employers should keep these issues in mind when entering into settlement agreements to ensure that proper withholdings are made and the proper documentation is issued.

**Prevailing Employer May Recover Litigation Costs Even Where Plaintiff’s Claims Were Not Frivolous**

A California appellate court has held that the discretion to award costs to a prevailing defendant is not limited to cases in which the plaintiff’s action was frivolous, unreasonable, or without foundation. In *Perez v. County of Santa Clara*, Maria Perez, a nurse at a county prison, sued Santa Clara County, alleging discrimination, retaliation and harassment relating to the County’s delay in promoting her and her complaints about that delay. At a bench trial, the trial court found

for the county, holding that although plaintiff established a prima facie case of discrimination, the County put forth a legitimate, nondiscriminatory reason for the delay in her promotion—performance problems and a lack of experience—and that there was no causal link between her complaints and the alleged retaliation and harassment. Even though the County prevailed, the trial court denied the County’s application for \$13,000 in deposition costs, witness fees, and other amounts expended in defending the lawsuit, based on its reading of the law that a defendant in an employment case can only recover costs and attorneys’ fees when the plaintiff’s case was frivolous, unreasonable, or groundless. The Court of Appeals reversed, noting that although the “frivolous” standard applies in deciding whether to award attorney’s fees to an employer, general litigation costs typically should be awarded “as a matter of course” to a prevailing employer, particularly given the low standard an employee must meet to state a prima facie case of discrimination. The appellate court sent the case back to the trial court so that court could decide—using this much lower standard—whether to award costs. Accordingly, prevailing employers should seek to recover general litigation costs at the conclusion of a successful lawsuit, even where they would not be entitled to attorneys’ fees.