THE EMPLOYMENT RELATIONSHIP

Law and Policy

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Colorado State University

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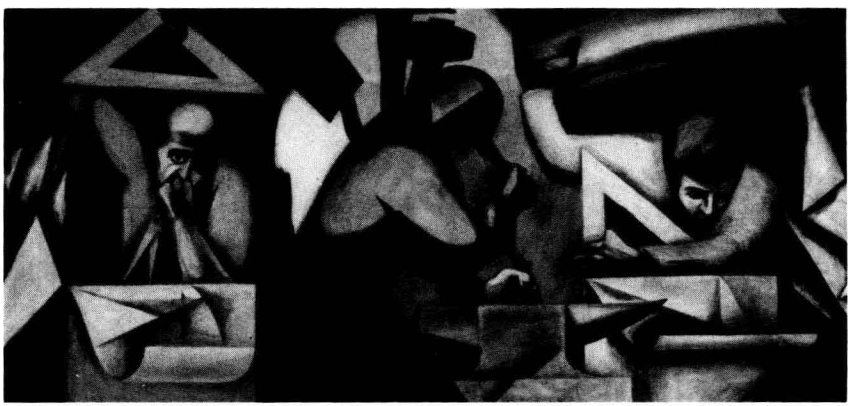

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Preface

Our society is infatuated with work. A salesman of livestock vaccine, for example, recently won $3.8 million in the Colorado lottery. When asked about his future plans, he said that he intended to continue working despite his six-figure annual income. He commented in the *Fort Collins Coloradoan:* "I love my job. I love the business that I'm in -- working with the people who grow the food that feeds the world -- and I'll just keep doing what I've been doing."

One explanation for such attachment to a job is that it satisfies our human need for creative activity. As Studs Terkel observed in his classic book *Working*, we typically experience labor on two important, but often contradictory, dimensions. Work, he wrote, is a search for "daily meaning as well as daily bread, for recognition as well as chaos, for astonishment rather than torpor; in short, for a sort of life rather than a Monday through Friday sort of dying."

For the 90 percent of Americans who receive their income in the form of wages, work involves both an opportunity for creativity and an acceptance of authority and control as a condition of employment. The nature of the wage relationship in this country confers upon employers the power to affect our lives in important respects. Even for the self-employed, who are not directly supervised by others, the governmental regulation of employment impinges on their activities in fundamental ways.

The American legal system historically has demonstrated a profound regard for the relations between workers and employers, and employment has been a subject of judicial and legislative regulation since the colonial era. Indeed, the most odious form of the master and servant relationship -- slavery -- was embedded in American culture from the founding of the nation and was supported by a complex legal system of property rights; the consequences persist today. The structure of employment relations clearly has profound implications for our society, which extend far beyond the workplace.

Work is also a subject of study for many professions. In the fields of business, sociology, public administration, law, and industrial relations, students pursuing a career may have an interest in issues of work. In these cases, the technical features of workplace regulation may be predominant.

Each dimension of employment has its own particular focus. First, as workers, we may have strong economic and psychological incentives to learn about employment; it directly affects our lives for the majority of our adult years. Second, as citizens, we may take a keen interest in the functioning of

our social and political system. Employment issues are an essential component of the system, and many facets of the regulatory framework are subject to modification through the political process. Third, as professionals, specialists in employment have a need for those skills that will enable them successfully to perform their jobs. The employment relationship deserves attention by all students on at least one of the three levels.

This text is designed around the foregoing principles. The book is not simply another treatment of the "legal environment of business"; in fact, it is assumed that the employment relationship has a broader importance than as a topic of study for those pursuing careers in business. All students, as educated members of our society, have a legitimate concern with such matters as social security, fair employment law, and safety and health in the workplace. Because we have the power to shape and alter the context of regulation, it is in our interest to understand the historical development and current issues in these and related areas. Accordingly, the text is intended for use in various disciplines.

Law is the primary means of regulation, and the materials necessarily focus on legal cases. But the cases are not used only to generate principles of law. They are used as well to demonstrate the evolution of law and the dynamics of legal thought. For this reason, the cases frequently include concurring and dissenting opinions. The point is not merely to set forth legal rules, but to illustrate, in depth, the analytical dimension of judicial activity. While the cases are in some instances fairly lengthy and complex, they are neither more demanding nor less rewarding than other intellectual achievements of our culture. The seminal opinions of the judicial branch of government deserve a place in the repertory of an educated individual; it is hardly appropriate that the law, which so significantly molds and influences our working lives, should be accessible only to a small segment of our population. One benefit of a close scrutiny of judicial decision making is to reveal that "legal reasoning" is not a process beyond the reach of the average citizen. An examination of the opinions shows that courts frequently make choices that are compelled neither by statute nor logic, but that are largely political in nature and could as properly be made by the electorate.

To provide a context for the cases, each section is preceded by a general overview, which describes the particular subject and addresses current problems. In addition, each case is followed by a series of questions designed to aid in understanding the reasoning of the case and the implications for policy. These two features supplement the basic principles set forth in the actual cases.

About the Author

Raymond Hogler is a Professor of Industrial Relations in the College of Business at Colorado State University. He previously taught in the Department

of Labor Studies and Industrial Relations at The Pennsylvania State University. A Former Woodrow Wilson Scholar and Fulbright-Hays Fellow, he has published articles in a number of periodicals, including the *Labor Law Journal*, the *Industrial Relations Law Journal*, *Labor History*, the *University of Colorado Law Review*, the *Dickinson Law Review*, and the *Employee Relations Law Journal*. His book *Public Sector Strikes* was published in 1988 by the International Personnel Management Association.

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General Overview

INTRODUCTION

The common law rule that has dominated employment relationships in this country for more than a century is known as the principle of "employment at will." In its most extreme form, it holds that absent explicit contractual restraint, an employer has the right to discharge an employee for a good reason, a bad reason, or no reason at all. The doctrine first appeared in American law in 1877 in a treatise on the law of masters and servants and represented an erroneous application of both English and American precedents. Despite the inaccuracy of the rule as a statement of legal principle, the U.S. Supreme Court would hold only three decades later that the rule was embedded in the Fifth Amendment of the Constitution, and that no congressional pronouncements could contravene the liberty and property rights inherent in the employment relationship. The constitutional dogma collapsed in 1937, and at present, employment is regulated legislatively at both federal and state levels. Further, the common law is being steadily eroded to protect employees from the most egregious abuses of the employer's power. That trend, according to many commentators, will constitute the most important area of employment law in this decade.

FROM MISCONCEPTION TO CONSTITUTIONAL MANDATE

During the middle of the nineteenth century, American law regarding employment contracts was in a state of transition. English common law generally provided some degree of protection for both parties to the

employment relationship through a presumption that, unless otherwise stated, employment was to be of one year's duration. In his *Commentaries*, Blackstone formulated the rule governing employment as follows:

> If the hiring be general, without any particular time limited, the law construes it to be a hiring for a year; upon a principle of natural equity, that the servant shall serve, and the master maintain him, throughout all the revolutions of the respective seasons, as well when there is work to be done as when there is not.[1]

Thus, unless otherwise stated, employment was for a fixed period of time, and employees could be lawfully terminated only when cause for discharge existed.

A second device that provided stability to the employment relationship was the requirement of notice of termination. Although the precise period varied, the mutual obligation to provide notice prior to terminating the relationship assumed considerable significance in English law.[2] In general, it prevented either party from precipitous action that would unduly disadvantage the other party.[3]

Prior to 1877, American law tended to adopt the principles originating in English precedent, although those rules were being somewhat eroded. Then, in 1877, Horace Gray Wood published his treatise on the master-servant relationship and declared the rule to be the "inflexible" one that "a general or indefinite hiring is prima facie a hiring at will, and if the servant seeks to make it out a yearly hiring, the burden is upon him to establish it by proof."[4] Wood's rule soon became recognized as the controlling legal principle in employment contracts. The rule, however, was supported neither in law or policy.

One legal historian, in tracing the background of employment at will, describes the genesis of Wood's rule as a "puzzling question." Wood enjoyed a reputation as an accurate, conscientious scholar, and his treatises were held in high esteem. Yet, three important criticisms can be made concerning his formulation of the at will doctrine:

> First, the four American cases he cited in direct support of the rule were in fact far off the mark. Second, his scholarly disingenuity was extraordinary; he stated incorrectly that no American courts in recent years had approved the English rule, that the employment at will rule was inflexibly applied in the United States, and that the English rule was only for a yearly hiring, making no mention of notice. Third, in the absence of valid legal support, Wood offered no policy grounds for the rule he proclaimed.[5]

But, despite its shortcomings, Wood's rule was widely adopted by 1895.[6]

One obvious consequence of the rule was to afford a much greater measure of power to employers in the employment relationship, thus enhancing the advantage of the capitalist owners. The at will doctrine can be viewed as the "ultimate guarantor of the capitalist's authority over the worker"[7] and an effective device to preclude workers from gaining any viable property interests in the enterprise.[8] Moreover, as applied in the late nineteenth century, it enabled the capitalist to shift the consequences of a business cycle to the worker, who could simply be discharged in a period of economic contraction.[9] Accordingly, the underlying thrust of Wood's rule was to allocate economic power. Its effectiveness in doing so can be illustrated by the case of *Payne v. Western & Atlantic Ry. Co.*, decided by the Tennessee Supreme Court in 1884.[10]

Payne, a merchant engaged in the business of selling consumer goods, sued the Western & Atlantic Co. for damage to his business. He alleged that one of the superintendents employed by the railway had distributed a notice to all employees stating that any worker "who trades with L. Payne from this date will be discharged."[11] Payne further alleged that his business had been ruined.

One issue addressed in *Payne* was whether or not the employer could threaten to or actually discharge its employees for violation of the prohibition against dealing with Payne. The majority of the court held that the railroad had a clear right to do so: "All may dismiss their employees at will, be they many or few, for good cause, for no cause, or even for cause morally wrong, without thereby being guilty of a legal wrong."[12] The right of discharge, said the court, obviously included the right to threaten discharge. Because the employment was at will, employees had no right to challenge the employer's prerogatives on any basis.

The dissenting judges, who would have permitted Payne's suit, very cogently analyzed the policy implications of the majority's conclusion. They observed:

> The principle of the majority opinion will justify employers, at any rate allow them, to require employees to trade where they may demand, to vote as they may require, or do anything not strictly criminal that [the] employer may dictate, or feel the wrath of [the] employer by dismissal from service. Employment is the means of sustaining life to himself and family to the employee, and so he is morally though not legally compelled to submit. Capital may thus not only find its own legitimate employment, but may control the employment of others to an extent that in time may sap the foundation of our free institutions.[13]

For the dissenting judges, the employment at will doctrine constituted a means of social and political, as well as economic, control over the worker.

The rule expressed by Wood attained its most potent application in the case of Adair v. *United States*,[14] in which the U. S. Supreme Court invalidated a federal statute affording railway workers a right to join and form labor unions. Adair, a foreman for the Louisville & Nashville Railroad Company, fired a mechanic named O.B. Coppage. Coppage, who was discharged solely because of his membership in the Order of Locomotive Firemen, initiated a criminal action against Adair pursuant to the statute. The federal district court upheld the constitutionality of the legislation, and a jury found Adair guilty of the offense.

In reversing the lower court, the Supreme Court ruled that the statute was repugnant to the due process clause of the Fifth Amendment. The Court stated that the concepts of "liberty" and "property" protected by the amendment included "the right to make contracts for the purchase of labor of others and equal the right to make contracts for the sale of one's own labor."[15] Thus, the legislation at issue that attempted to restrict the individual's liberty and property interest inherent in the sale or purchase of labor contravened certain freedoms established by the constitution.

The Adair decision was one case in a line of precedent that substantially impeded legislative efforts to regulate the employment relationship and meliorate the abusive power of employers.[16] That judicial trend, however, was brought to an abrupt end in 1937.

COMMERCE AND THE MODERN ERA

In *NLRB v. Jones & Laughlin Steel Corp.*,[17] the Supreme Court conceded the power of the federal government to legislate in the area of employee relations as an aspect of its power over interstate commerce and upheld the contitutionality of the Wagner Act. The Court reasoned that even the activity of manufacturing, which was essentially intrastate in character, might have such a "close and intimate relationship to interstate commerce" as to be subject to federal regulation. Consequently, the numerous unfair labor practices committed by the company in violation of the Wagner Act, which had been enacted in 1935, might reasonably lead to labor strife that, in turn, would have an immediate impact on interstate commerce. In the Court's view, "Experience has abundantly demonstrated that the recognition of the right of employees to self-organization and to have representatives of their own choosing for the purpose of collective bargaining is often an essential condition of industrial peace."[18]

With respect to the "liberty" and "property" concepts that figured so prominently in *Adair*, the Court simply concluded that its holding did not interfere with "freedom of contract." The company remained free to hire and fire employees as it chose; it could not, however, discipline or discharge an

employee for the purpose of interfering with the employee's protected rights. The Fifth Amendment thus posed no constitutional obstacle to the Act.

As a result of the *Jones & Laughlin* opinion, the employment at will doctrine suffered its first serious inroad. It was no longer sanctified by the Constitution and could be modified by legislative dictate. The rule, after *Jones & Laughlin*, was that an employee might be discharged for a good reason, a bad reason, or no reason, but not for an illegal reason. Even though the employee was not afforded comprehensive job security by the Wagner Act, he or she was at least protected in the endeavor to bargain collectively and to negotiate for job security in the form of a "just cause" standard for discipline.

Recent labor historiography has emphasized the cataclysmic social conditions that led to the Wagner Act, and the radical departure of that legislation from the economic tenets espoused in cases such as *Adair*.[19] Perhaps most importantly, workers readily perceived the larger social and political dimension of the Wagner Act and acted to implement its philosophy by means of overt conflict. The achievements in union organizing of the Congress of Industrial Organizations between the Wagner Act and the decision in *Jones & Laughlin* evidenced the fundamental shift in values that was occurring socially, as well as in the judicial system.[20] Workers indicated a greater willingness to join and support unions than at any previous time in our history.

After enactment of the NLRA, other legislative modifications of the employment at will doctrine were implemented. Such legislation prohibited employer discrimination on certain specified grounds, as with, for example, Title VII of the Civil Rights Act of 1964[21] and the Age Discrimination in Employment Act.[22] Other types of legislation may require that the employer have cause for the discharge of a particular employee.[23] As a result of that legislative activity, many workers are now afforded some protection in their employment.[24] The common law, at the same time, has developed important limitations on an employer's right to terminate employment.

MAJOR JUDICIAL EXCEPTIONS TO THE AT WILL DOCTRINE

Most broadly, there are two conceptual grounds upon which the employment at will principle has been avoided under common law.[25] The first, originating in the landmark decision of *Petermann v. Teamsters Local 396*,[26] relies on a theory of "public policy." The second line of cases rests on a theory of contract that may arise either from the understanding of the parties or by operation of law. Each theory is considered in more detail.

The *Petermann* case involved a Teamsters business agent who was subpoenaed to testify before a committee of the California state legislature. He was directed by his employer, the secretary-treasurer of the local union, to make certain false statements that would protect the business agent. At the hearing, the plaintiff testified truthfully, and the following day he was discharged.

In determining that the plaintiff had stated a cause of action under California common law, the Court of Appeals observed that "public policy" was a legal principle designed to protect against conduct that was "injurious to the public or against the public good." With respect to employment, the court concluded: "To hold that one's continued employment could be made contingent upon his commission of a felonious act at the instance of his employer would be to encourage criminal conduct upon the part of both the employee and employer and would serve to contaminate the honest administration of public affairs."[27] Thus, the plaintiff would be entitled to a civil remedy as a consequence of his wrongful discharge.

The public policy exception to the at will doctrine has been applied in several contexts. Courts have held, for example, that an employee cannot be discharged as a result of filing a workers' compensation claim, for refusing to falsify official reports, for serving on a jury, or for making public protest against the employer's unlawful or improper business activities.[28] Although the exception has been criticized in at least three distinct respects,[29] it is now an established legal trend.

The second exception arises out of the contractual nature of the employment context. The employer, for instance, may agree either explicitly or implicitly that the employee will only be terminated for cause. Or, to achieve the same result, a court may determine that the employment relationship inherently necessitates a covenant of good faith and fair dealing. California state law once again will illustrate the principle.

In *Cleary v. American Airlines, Inc.*,[30] the plaintiff was hired under an oral agreement for an indefinite term. He continued in his employment for eighteen years, with apparently satisfactory performance. When he was discharged for no apparent reason, he brought suit against the airline. The California Court of Appeals determined that plaintiff had stated a viable theory for recovery and the matter should have proceeded to trial. Its opinion concludes, "we hold that the longevity of the employee's service, together with the expressed policy of the employer (i.e., the adoption of specific procedures for adjudicating employee disputes) operate as a form of estoppel, precluding any discharge of such an employee by the employer without good cause."[31]

After reviewing *Cleary* and similar California cases, a federal court summarized that state's law of employment contracts as follows:

> California courts have recently applied the duty created by the implied convenant [of good faith and fair dealing] to the situation where the employee alleges no more than long service and the existence of personnel policies or oral representation showing an implied promise by the employer not to act arbitrarily in dealing with its employees. Such claims sound in both contract and tort and may give rise to emotional distress damages and punitive damages.[32]

Consequently, an employee in California may acquire an interest in employment by virtue of seniority that, combined with some evidence that the employer has assented not to act arbitrarily in the treatment of employees, will protect the employee against unjust discharge. If the employer violates that standard of conduct, it may be liable for substantial monetary damages.

The at will doctrine has been subjected to extensive academic criticism,[33] and the principle is being steadily eviscerated by judicial decision. Assuming that the notion of at will employment is to be discarded, some adequate legal policy must necessarily evolve to replace it. Organized labor, at this juncture, may perform a vital function in mediating the various interests implicated by transformations in industrial society.

RESOLVING AT WILL DISPUTES

One influential article proposed an approach to employment contracts based on the efficient allocation of economic resources.[34] In general, the author contends, courts should not attempt in wrongful discharge cases to redress inequalities in bargaining power between the employer and the individual employee. Rather, abandonment of the at will rule and adoption of a different judicial policy should be premised on an effort "to bring about the substantive outcome that the parties would have reached had transaction and information costs not precluded informed negotiations."[35] The analysis rests on two central theses: first, it is assumed that neither employee nor employer will bargain meaningfully concerning job security because the time involved in doing so on an individualized basis is prohibitive, and therefore "standard" terms are usually agreed upon; and, secondly, the theory assumes that most employees are not sufficiently aware of the value of job security to negotiate vigorously for it. The judicial system, by creating a rule of employer liability for wrongful discharge, could shift some costs of the loss of employment from the employee[36] to the employer, thus tending to meliorate the impact of high transaction and information costs. Employers, that is, would have an incentive to negotiate meaningful job-security terms.

In addition, the author argues, imposing a duty on the employer to terminate only in good faith would have the positive economic outcome of