Nassau Lawyer

JULY/AUGUST 2010 | VOL. 59 | NO. 11 | WWW.NASSAUBAR.ORG

Banking/Bankruptcy Law Focus

Bankruptcy law vs. employment discrimination

Debt should never be the sole reason behind treatment of an employee or applicant

The ongoing economic crisis has caused a significant increase in the number of individuals who are filing for bankruptcy on Long Island, throughout New York, and across the nation. More and more people, in a final effort to escape crushing debt, have sought to obtain a financial "fresh start" by availing themselves of the protections of the Bankruptcy Code to stop creditors from attaching their assets or foreclosing on their property.

Stuart I. Gordon

Since individuals who seek bankruptcy protection are already financially burdened, the Bankruptcy Code bars employers from taking certain actions against bankrupt employees and job applicants which may be detrimental to their "fresh start."

In particular, Section 525 of the Bankruptcy Code, 11 U.S.C. § 525, protects persons who have sought bankruptcy protection from being terminated by their employer or otherwise discriminated against in respect to their employment. An employer may not terminate the employment of, or discriminate with respect to employment against, an individual solely because that individual: (1) is or has been a debtor; (2) has been insolvent; or (3) has not paid a debt that is dischargeable in bankruptcy.

Matthew V. Spero

Employers must be cognizant that they do not violate Section 525 as to employees and, perhaps, job applicants who have filed for bankruptcy protection or who indicate that they intend to file.

Employees Who Have Declared Bankruptcy

Section 525 is implicated in a variety of circumstances. Suppose, for instance, that the President of a company learns that an accountant employed by the company has filed for bankruptcy protection. The President may experience some trepidation in allowing that individual to have continued access to corporate records and funds. However, under Section 525 the company would be precluded from demoting or terminating the debtor solely on account of his or her bankruptcy.

For example, in *In re Hicks* 65 B.R. 980 (Bankr. W.D.Ark. 1986), the court relied on Section 525 in holding that a bank discriminated against a bank teller by transferring her to a position having no customer contact after the teller filed for bankruptcy under Chapter 7. The bank attempted to justify the transfer of the bankrupt teller into a bookkeeper position by arguing that the reassignment did not involve any decrease in compensation and that it was made: (1) to prevent the "embarrassment" of the teller; (2) to prevent any harm to customer relations and public confidence; and (3) because the bank could not bond a teller with financial difficulties. The court ruled in favor of the teller, and found that the discrimination prohibition of Section 525 is violated "when the

debtor/employee's job duties are affected by the employer's actions, even though there are no adverse economic consequences as a result of the change in duties." *Id.* at 983. The court also found that the discriminatory treatment directed toward the teller was solely because of the teller's bankruptcy, observing that: (1) the bank's supervisor admitted that the transfer was made as a result of a newspaper article announcing the teller's bankruptcy; (2) the bank had introduced no evidence that customer relations would be harmed; and (3) the bank had no valid concerns regarding the debtor's honesty in her previous position as a teller. *Id.* at 984.

Employees Who Intend to Declare Bankruptcy

More recently, in *Robinette v. WESTconsin Credit Union*, No. 09-CV-600-VIS, 2010 U.S. Dist. LEXIS 17085 (D. Wisc. Feb. 25, 2010), the court was asked to consider the application of Section a federal District Court was asked to consider the application of § 525 to an employee who had not yet filed for bankruptcy protection, but who had indicated that she was going to do so.

The plaintiff was employed by a federal credit union from August 18, 2004 to June 16, 2009. The plaintiff and her husband had also obtained a loan from the credit union. The plaintiff alleged that, on June 15, 2009, her supervisor questioned her about judgments that had been posted in the local newspaper listing the plaintiff's husband as a judgment debtor. The plaintiff thereafter told her supervisor that she and her husband had retained an attorney and were going to file a bankruptcy petition and planned to include the debt owed to the credit union in their bankruptcy petition.

The plaintiff alleged that the following day, her supervisor told her that she was terminated because she was "filing for bankruptcy," which would not "make [the credit union] look good." The plaintiff, apparently an exemplary employee, and her husband filed for bankruptcy protection on June 25, 2009.

The plaintiff argued that the credit union violated Section 525 by terminating her. The credit union responded that Section 525 did not apply since the plaintiff had not sought bankruptcy protection at the time she was fired, and that Section 525 only applied to debtors who were terminated after filing a bankruptcy petition.

The court rejected the credit union's argument, and ruled that the plaintiff had stated a claim for relief under Section 525 "because the statute can be fairly read as extending to employers who terminate or otherwise discriminate against an employee who intends to file a petition for bankruptcy and does so." *Id.* at 2. The court reasoned that reading Section 525 to restrict its protections solely "to those who win the race to the courthouse" would frustrate the statute's "clear purpose of providing debtors a fresh start." In effect, the court held, adopting the credit union's argument would permit employers to fire or demote an employee with impunity so long as it acted before the precise moment that the employee filed for bankruptcy. The court concluded that it was not reasonable to believe that Congress intended to encourage a "foot race" in enacting Section 525.

Courts disagree on this matter. Some have in dicta agreed with Robinette that Congress did not intend such a foot race. *See In re Tinker*, 99 B.R. 957 (Bankr. W.D.Mo. 1989); *In re Mayo*, 322 B.R. 712, 717 (Bankr. D.Vt. 2005). Others find the statutory language unambiguous and applicable only to those who have actually filed for bankruptcy. *See In re Majewski*, 310 F.3d 652 (9th Cir. 2002); *In re Davis*, 2009 Bankr. LEXIS 2258 (Bankr. M.D.Ala. 2009); *In re Kanouse*, 168 B.R. 441 (Bankr. S.D.Fla. 1994).

Job Applicants

It also is important to note that some courts have found that an employer may be liable under Section 525 even if a job applicant was discriminated against on the basis of a prior bankruptcy filing. In *Leary v. Warnaco, Inc.*, 251 B.R. 656 (Bankr. S.D.N.Y. 2000), the court found that Section 525 also can apply to discriminatory employment actions taken before an employment relationship has even been established. In *Leary* it was alleged that the employer had conditionally offered the plaintiff an executive position with the company subject to the results of a credit check. After the credit check revealed the plaintiff's prior Chapter 7 bankruptcy filing, the employer notified the plaintiff that it would not hire her The court found that Section 525 prohibited discrimination "with respect to employment" and that such language was "clearly broad enough to extend to discrimination with respect to extending an offer of employment." Other courts have held that § 525 does not extend to prospective employees. *See In re Burnett*, 2008 Bankr. Lexis 4059 (Bankr. S.D. Tex. 2008); *In re Martin*, 2007 Bankr. Lexis 3278 (Bankr. D. Kan. 2007); *In re Stinson*, 285 B.R. 239 (Bankr. W.D. Va 2002).

Given the current economic climate, it is likely that employers will see an increase in the number of both current and prospective employees who either have sought or will seek the protections offered by the Bankruptcy Code in search of a "fresh start." It is critical that employers not use the bankruptcy filing as the sole basis to make employment-related decisions relating to these individuals, lest they violate Section 525.

Stuart I. Gordon is a partner at Rivkin Radler LLP. Matthew V. Spero is an associate at the firm. The authors can be reached at stuart.gordon@rivkin.com and matthew.spero@rivkin.com, respectively.

1. 2010 U.S. Dist. LEXIS 17085 (D. Wisc. Feb. 25, 2010).