The Kolstad Umbrella Can Keep Employers Dry

William P.H. Cary
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Seven years after the U.S. Supreme Court explained that employers have a defense against punitive damages in employment-discrimination cases in *Kolstad v. American Dental Association*, many employers still are not taking the steps necessary to use it. It's as if the weather forecast is calling for rain, but you decide not to take your umbrella. You are betting on good luck.

The basics of liability
For most employment actions such as hiring, promotions and firing, the employer will be liable if the decision was based on an unlawful, discriminatory motive. The supervisor or manager may have been acting out of personal prejudice unknown to the company, but the company will still be liable if the manager was acting within the scope of his or her employment.

The company's liability will normally include back pay and benefits, compensatory damages (including damages for emotional distress) and legal fees. The company also may have to reinstate the employee.

In most cases, the company also could be liable for punitive damages. Since punitive damages are intended to punish the wrongdoer rather than compensate the victim, the bigger the corporate defendant, the larger the potential punitive damage award, which also makes reaching a reasonable settlement difficult. Removing the possibility of punitive damages early in the litigation by successful assertion of the *Kolstad* defense not only limits the company's total exposure, it also improves the possibility of a settlement.

In *Kolstad*, the Supreme Court first said that punitive damages are appropriate when the employer has acted "with malice or with reckless indifference" to the plaintiff's rights. To prove these elements, the plaintiff must prove that the decision was made by a manager acting within the scope of his or her employment and "in the face of a perceived risk of violating federal law" (for example, the manager knew that basing the decision on race or sex would be illegal). In cases involving hiring or firing, as opposed to hostile environment or harassment claims, these elements are typically uncontested or easily proved (particularly egregious conduct alone may satisfy the second element). If the plaintiff satisfies this burden, the employer still may avoid punitive damages by showing that the alleged discriminatory decision was contrary to the employer's "good-faith efforts" to comply with the law. The policy behind this defense is to motivate employers to detect and deter violations.

What are “good-faith” efforts? In the seven years since Kolstad, this has been the subject of much litigation, and while some principles are emerging, there is no brightline test. Following are some actions that case law indicates will help show good-faith efforts.

Elements of the defense

- *Officially adopting specific nondiscrimination and noretaliation policies is a necessary first step.* Employers have lost the *Kolstad* defense because their nondiscrimination policies did not specifically prohibit the specific kind of discrimination involved. For example, although gender discrimination was prohibited in one case, pregnancy discrimination was not specifically mentioned, and the company lost.
- *Adequately publicizing the policies.* Posting alone probably will not suffice. The policies should be included in handbooks and training materials.
- *Training supervisors and managers.* These are the people who are making or recommending most of the day-to-day employment decisions. They will be deposed by the plaintiff’s lawyer and asked to explain the antidiscrimination laws involved in your case. They don’t need to be lawyers, but it is important in establishing “good-faith efforts” that the employer has attempted to impart at least a rudimentary understanding of what the law requires or prohibits. Retain copies of training materials and attendance rosters. The existence of such training is an element of every case upholding assertion of the *Kolstad* defense.
- *Providing mechanisms for complaints.* Having open door, grievance or other reporting avenues helps establish that the employer is attempting to police its own workplace. Just as important is showing that these mechanisms are used and that they work. If the employees are afraid to complain, just having these procedures will not help establish the *Kolstad* defense.
- *Reviewing your personnel policies and practices.* How are hiring, promotion, discipline and discharge decisions made? In particular, what checks exist on the exercise of unfettered discretion, and hence potential prejudice or personal bias? These are factors which weigh against successful reliance on *Kolstad*.

These steps alone are no guarantee that the defense will be available. Increasingly, the courts are looking beyond checklists. “The mere existence of an anti-discrimination policy or the presence of seminars touching on the anti-discrimination laws does not automatically satisfy the good-faith requirement, although it is some evidence of good faith ... Evidence that an employer is not sincerely committed to enforcing the policy may undermine the existence of a companywide policy,” the court found in one case. Evidence of personal bias by top officials and their failure to follow through on complaints or reports suggesting the existence of discriminatory practices can undo the benefits of specific non-discrimination policies and

training. Conversely, the presence of “an extensively implemented organization-wide Equal Employment Opportunity policy, ... a grievance policy encouraging employees to bring forward claims of harassment, discrimination or general dissatisfaction, ... a carefully developed diversity training program ... and voluntarily monitoring departmental demographics” were key elements of what the court described as a company’s widespread anti-discrimination efforts that entitled it to avoid punitive damages in another case.

As these cases demonstrate, the totality of an employer’s efforts, and its sincerity in doing so, will be the test. Sophisticated plaintiffs’ lawyers will call experts to testify that an employer’s policies and training efforts are substandard and should not be considered “good-faith” efforts to comply with the law. As more companies undertake training and monitoring programs to assure compliance with employment-discrimination laws, the standard for what is reasonable will likewise continue to evolve: It will be a moving target. Trying to meet that standard will not only help avoid liability for punitive damages, it will help prevent illegal employment decisions in the first place. Like any summary of a complicated subject, this brief overview has made generalizations, and there are exceptions that may apply in particular cases. For example, in hostile-work-environment claims such as sexual harassment, the threshold elements noted above may not be so easily proved by the plaintiff and so there may be other defenses to punitive damages. As long as individuals are making employment decisions, and as long as individuals are not free of bias or prejudice, the employer runs the risk that a decision will be illegal and the employer will be liable. Therefore, the forecast is partly cloudy with a chance of rain.

The *Kolstad* umbrella might not keep you completely dry, but it could keep you from getting drenched.