

The Cause And Effect Of 'For Cause' Employment Clauses



Law360, New York (February 24, 2014, 5:28 PM ET) -- When an employee walks into a meeting, pulls down his pants and moons his boss, can his company fire him “for cause?” What if the employee fakes merchants’ signatures on credit card agreements? Or what if he ships boxes of the company’s confidential documents to his home?

The starting point for answering these questions is often the company’s written agreement with the employee. Employment agreements sometimes include provisions that allow the employer to terminate the employee “for cause” or with “just cause,” as opposed to “without cause.” A for-cause termination can affect the employee’s entitlement to severance benefits, and sometimes, it can deprive the employee of any severance at all.

When drafting employment agreements, employers should consider whether they want to include for-cause termination provisions, and if so, what cause should mean. The term cause has no uniform definition. However, agreements typically define it as “willful or gross misconduct, moral turpitude, failure to perform duties, or breach of fiduciary duty.” Less frequently, sexual harassment, substance abuse or incompetence are specifically included as grounds for termination for cause.

Sometimes, for-cause termination provisions can require the employer to notify the employee of inappropriate conduct and then allow a period to cure it. Before agreeing to this kind of language, an employer should consider whether there are some grounds for a termination with cause that cannot be rectified, and exclude those grounds from the notice provision.

Consider Flexibility Versus Certainty

When an employment agreement defines cause narrowly and specifically, for example when an employee commits a felony, it is harder for an employee to litigate a termination for cause. However, the employer might find itself in a situation where it wants to terminate an employee for cause but can’t fit the employee’s actions within the definition of that term. By contrast, a flexible definition of cause can benefit employers by allowing them to terminate an employee for cause in unforeseen circumstances. But a flexible definition is also more likely to lead to expensive litigation.

The case of Jason Selch provides a memorable example of this kind of litigation. *Selch v. Columbia Management*, 977 N.E.2d 287 (Ill. Ct. App. 2012). In that case, Selch was fired after he pulled down his pants and mooned his bosses. After the mooning, the employer issued Selch a formal written warning. Later, however, the company’s CEO — who wasn’t present for the “derriere display” — intervened and

fired Selch. Selch sued, alleging that the employer did not properly terminate him for cause. As a result, he claimed, he was entitled to severance benefits under his employment agreement.

Selch's agreement defined cause as "conviction of a felony, engaging in misconduct that injures the company, performing your duties with gross negligence or any material breach of your fiduciary duties as an employee of the company." This was a somewhat malleable definition, because it included matters of judgment such as "misconduct that injures the company." The employer prevailed, with the court finding that Selch's mooning was indeed such an act. However, the employer had to go through expensive litigation to get to that point.

Similarly, American International Group Inc. recently terminated an employee based on a more flexible definition of cause and found itself in litigation as a result. *Fitzpatrick v. AIG*, No. 10 Civ. 142(MHD) (S.D.N.Y. Feb. 26, 2013). In that case, AIG claimed that it fired Kevin Fitzpatrick because he took documents to his house in order to get a quick start in his new business.

Fitzpatrick's employment agreement defined cause as: (1) a "willful and material failure to perform your duties hereunder" after a notice and cure period; (2) "gross negligence, willful misconduct or significant breach of fiduciary duty" that injured AIG; (3) conviction or plea to a felony or material violation of securities laws or rules; or (4) fraud or embezzlement.

The court did not resolve the dispute. Instead, it left it to the jury to resolve whether Fitzpatrick's shipments of documents were "the sort of misconduct that would satisfy the contractual provision permitting termination for cause." Thus, AIG still had a viable claim that it terminated Fitzpatrick for cause based on his "willful misconduct," but it couldn't finally resolve that claim without a potentially expensive trial.

When the employee's misconduct is more seriously detrimental to the employer, the employer can possibly avoid trial even under a more flexible definition of cause.

For example, RBS WorldPay recently defeated, without a trial, its former employees' claims that it did not properly terminate them for cause. *Baker v. RBS WorldPay Inc.*, Civ. No. 10-0307-WS-B (S.D. Ala. Oct. 4, 2011). In that case, a group of employees sold credit card processing services to gas stations. Their employment agreements defined cause as "the commission of any fraud, misappropriation, embezzlement or other dishonest act" that breached company codes of conduct or could "reasonably be expected to have a material adverse effect on the financial interest or business reputation" of the company.

According to WorldPay, it terminated the employees because they signed merchants' names to a credit card agreement without permission of the credit card issuer, Wright Express. The court found no dispute that the employees faked the merchants' signatures and that WorldPay fired them because Wright Express, which was WorldPay's customer, complained about the issue. As a result, the court concluded, the employees' actions clearly had a material adverse effect on WorldPay's financial interest, such that WorldPay could properly terminate them for cause.

The Baker decision contains another important lesson about how to preempt an employee's claim that a firing for cause is actually pretextual. In Baker, the employees claimed that the merchant signing issue was a red herring. Instead, they said, they were actually fired because they had complained to their employer about its business practices. However, the company insulated itself from this argument by working through a human resources officer who had no idea of the employees' complaints at the time

she decided to terminate them. The court found that she didn't rubber-stamp the for-cause decision, saying that she was not a "mere puppet who blindly kowtowed to a termination recommendation made by someone else." On their side, by contrast, the plaintiffs only had "shadowy accusation[s]" of pretext.

The court's decision shows that an employer should consider asking someone who is not familiar with the employee's prior complaints to weigh in on whether their misconduct justifies a for-cause termination, because that person's recommendation can carry significant weight in defeating a claim of improper retaliation.

Employers Should Act Decisively and Consistently

An employer is more likely to lose a dispute over whether a termination for cause was proper when it doesn't act quickly to terminate an employee for cause, takes steps that are inconsistent with a for-cause firing or doesn't give the court evidence of what the employee actually did wrong. Employers should be careful to collect the evidence supporting an employee's termination for cause, and make a calm coherent, and consistent decision based on that evidence.

A recent case involving Tyco International Ltd. serves as a cautionary tale for employers who are unable to provide a court with reasons supporting a decision to terminate an employee for cause. *Conti v. Tyco Electronics Corp.*, H037607 (Cal. Ct. App. Oct. 9, 2012). In that case, before Conti finished his first year of employment, Tyco fired him and denied him his year-end bonus, which he sued to recover. The local human resources manager told Conti at the time of the firing that the termination was for cause for "performance issues."

Although Conti's agreement did not define the term cause, the court interpreted it as not including reasons that are "trivial, capricious, unrelated to business needs or goals or pretextual." The court said that Tyco could not defeat his claim that he was improperly terminated for cause in advance of trial, explaining:

"[I]n the context of a relationship where an employee may be terminated for good cause, it is the trier of fact who decides whether cause existed for the termination unless the undisputed facts show that the employer had good cause." According to the court, Tyco failed to meet its burden to show good cause, because it only pointed to its prior statements to him that it was terminating him for cause. It had to show more evidence about his job performance, and it didn't do that.

An employer can also impair a for-cause termination by first taking steps that are inconsistent with the termination, as *Cornett v. Lender Processing Services Inc.*, No. 3:12-cv-233 (M.D. Fla. Sept. 5, 2013), shows. In that case, Cornett worked for Lender Processing Services ("LPS") as president of its default solutions division until the spring of 2011, when he signed a new employment agreement for a newly-created, high-paying sales position. At the time Cornett signed the new agreement, LPS had uncovered a signing problem in the default solutions division — one individual would sign another's name on documents that were notarized and recorded. Later, Nevada's attorney general sued over another default solutions signing issue in late 2011, which was the last straw for LPS. It fired Cornett with cause, paid him no severance and asserted that he was bound by the noncompete provision in his 2011 agreement.

The district court held a trial, after which it found that Cornett wasn't properly fired with cause, awarded him severance pay and refused to enforce the noncompete provision. The fact that LPS

entered into the 2011 agreement was critical to this outcome, because that agreement reshaped LPS's employment relationship with Cornett. Under it, he had new responsibilities that did not involve managing default solutions, but rather, involved sales and business development. Because of this new agreement, LPS couldn't use the issues in the default solutions division to show that Cornett had deficiently performed his duties. In sum, the court wrote, while the CEO's desire to "right the ship" by firing Cornett made the case a close call, LPS had chosen to give Cornett a new employment agreement, under which it had no cause to fire him.

The Selch and Fitzpatrick cases also carry on this theme, although the employers eventually prevailed in those cases. In Fitzpatrick (the box shipping case), AIG raised the additional argument that Fitzpatrick had gotten it into a bad real estate deal in 2007. However, because AIG knew the facts about the deal at the time it fired Fitzpatrick and didn't rely on them for its for-cause decision, the court decided that AIG couldn't later rely on those facts to justify his termination. Similarly, in Selch (the mooning case), the employee argued that the company had acted inconsistently with a for-cause firing because it issued a formal warning to Selch before it terminated him. However, because the warning didn't promise or guarantee Selch that he would be able to keep his job, and wasn't a bargained or negotiated document, the court decided that it didn't limit the employer's options.

Employers Should Define Cause and Use Discretion

Employers should treat employees with respect when making and announcing the decision to terminate them for cause. A rashly made or indiscreetly communicated termination decision can have significant repercussions for the employer, as *Leyshon v. Diehl Controls North America Inc.*, 946 N.E.2d 864 (Ill. App. Ct. Dec. 27, 2010), shows.

In that case, Leyshon, the president of Diehl Controls North America, had signed an employment agreement that defined "cause" as "gross negligence, gross neglect of duties, gross insubordination and willful violation of any law applicable to the conduct of the [c]ompany's business and affairs."

On Feb. 1, 2006, the Diehl's new chairman marched into Leyshon's office and told him that he was fired. Leyshon asked why, but the chairman wouldn't tell him. After Leyshon summoned an human resources representative, the chairman told Leyshon that he was terminated for cause. Leyshon pressed, "You are telling me that you are firing me for gross insubordination, for gross misconduct, for gross negligence and willful violation of the law?" The chairman answered "Yes," but wouldn't answer further.

Leyshon sued for defamation, alleging that the company's termination for cause had damaged his ability to obtain future employment and had so humiliated him that he couldn't face the company's employees. A jury awarded Leyshon \$2 million in compensatory damages and \$6 million in punitive damages, based on testimony showing that Diehl's officials had a premeditated scheme to fire him with cause even though they had no basis for such a firing. An Illinois appellate court then affirmed the verdict, finding that the chairman's statement that Leyshon was terminated for cause had no innocent meaning that was not false or harmful to Leyshon's reputation, given the context in which the statement was made.

The Leyshon decision demonstrates that an employer should investigate an employee's potential misconduct and arrive at a sound basis for its termination decision. Leyshon also shows that an employer should not broadcast a for-cause termination, given the negative impact that such a termination can have on an employee's reputation. Otherwise, the employer may find itself on the wrong end of a big verdict.

Conclusion

Careful planning is key for prevailing in for-cause termination suits. The six cases described above teach several key lessons for employers.

When drafting employment agreements, an employer should consider the pros and cons of flexible language allowing a termination for cause versus language that is more circumscribed to particular situations, such as when the employee commits a crime. When an employer is considering whether or not to terminate an employee for cause, it should be sure to examine the language of the employee's agreements with the company and the evidence supporting its possible grounds for such a termination.

The employer should also explore using an internal decision maker who has not worked closely with the employee to review the facts and aid in the termination decision. The employer should act decisively, but only after arriving at a sound basis for a for-cause termination, and it should communicate its decision as discreetly as possible because of the potential harm that such a termination can cause to the employee's reputation.

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