



*BOUCHER & BOUCHER* Co., L.P.A.  
Attorneys and Counselors at Law

Insights and Developments in the Law

Fall 2012

## Criminal Background Checks on Employees

It is not a new development in employment law that many employers take into account an applicant's or employee's criminal history information, including arrests or convictions, when making employment decisions. Nor is it unprecedented for the federal Equal Employment Opportunity Commission (EEOC) to come out with policies and guidance on the subject.

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*The EEOC has recently issued an updated Guidance on employers' use of criminal background checks in employment decisions under Title VII of the Civil Rights Act of 1964.*

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But in light of technological changes that have made criminal background checks easier to do, the passage of the Civil Rights Act of 1991, which codified the "disparate impact" theory of liability, and even some prodding from a federal court of appeals, the EEOC has recently issued an updated Guidance on employers' use of criminal background checks in employment decisions under Title VII of the Civil Rights Act of 1964.

Title VII does not directly regulate or speak to the acquisition of criminal history information. (Some state employment discrimination laws, however, give protections to individuals

concerning inquiries by employers about criminal histories.) Still, there are two ways in which an employer's use of criminal history information can violate Title VII.

The first theory, called "disparate treatment" discrimination, occurs when an employer treats job applicants with the same criminal records differently because of one of the prohibited bases

for discrimination in Title VII: race, color, religion, sex, or national origin.

The second concept, known as "disparate impact" discrimination, refers to the situation in which an employer applies criminal record information to its employment decisions uniformly, but the exclusions still op-

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## Lottery Winnings and Gift Taxes

If records were kept about such things, Tonda Lynn, a waitress at a pancake house, may have received the largest tip in history when a customer gave her a lottery ticket that turned out to be worth \$10 million. As the U.S. Tax Court put it in a heading in its opinion resolving gift tax issues arising from subsequent events, suddenly "She's Got a Ticket to Ride."

From the start, Tonda Lynn knew she wanted to share her good fortune with her family. With no shortage of advice and guidance, especially from her father, she settled on setting up a corporation that would claim the lottery proceeds. She and her spouse owned 49% of the stock, with family members owning the remaining 51%.

Similar arrangements, some set up before a lottery win and some after, are commonly made to share lottery winnings while trying to avoid gift taxes

However, the IRS will scrutinize shared lottery arrangements and assert gift taxes when such arrangements do not pass muster. Tonda Lynn and her relatives found this out when the IRS, backed up by the Tax Court, ruled that there had been no binding contract to share the lottery proceeds and that there was a taxable gift as to the 51% of the winnings that went to family members.

In principle, there was nothing wrong with what Tonda Lynn was trying to do after her big win. The problem was that the purported contract among the family members was too vague and indefinite to enforce under state law, and thus her contribution of the winning ticket to the newly formed corporation constituted a taxable, indirect gift to the family members.

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## Fair Housing Act Doesn't Apply to Roommates

An online roommate matching website helps compatible roommates to find each other. Part of the process requires users of the service to answer questions about their gender and sexual orientation and whether children will be living with them. Users are asked to give their preferences as to those same characteristics so that like-minded individuals can be matched. This process came to the attention of some nonprofit housing rights organizations that unsuccessfully sued the roommate service, alleging violations of the federal Fair Housing Act (FHA).

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*The FHA prohibits discrimination based on sex or familial status in the sale or rental of a "dwelling."*

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The FHA prohibits discrimination based on sex or familial status in the sale or rental of a "dwelling." The FHA defines "dwelling" as essentially a living unit designed or intended to be occupied by a family. The lawsuit against the roommate service failed because a federal court reasoned that "[i]t makes practical sense to interpret 'dwelling' as an independent living unit and stop the FHA at the front door." It would be difficult to divide a single-family house or apartment into separate "dwellings," and, in any event, the court concluded that when it passed the FHA, Congress did not mean to interfere with relationships *inside* a single home.

The court also found that constitutional concerns tipped the balance away from applying the FHA to roommate decisions. Because of the role of certain intimate human relationships in safeguarding individual freedom, choices to enter into and maintain such relationships must be secured against

undue intrusion by the state. The right of intimate association is not restricted exclusively to family members, and that right also implies a right *not* to associate.

To determine whether a particular relationship is protected by the right to intimate association, courts look to size, purpose, and selectivity and to whether others are excluded from critical aspects of the relationship. The roommate relationship easily qualifies: People generally have very few roommates; they are selective in

choosing roommates; and nonroommates are excluded from the critical aspects of the relationship, such as using the living spaces.

In the court's view, aside from immediate family or a romantic partner, it's hard to imagine a relationship more intimate than that between roommates, who share living rooms, dining rooms, kitchens, bathrooms, and even bedrooms. Because of a roommate's unfettered access to the home, choosing a roommate also implicates significant privacy and safety considerations.

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## Land Purchasers Get Money Back

When a couple bought a lot for \$1.7 million in what was to become a luxury golf course community, one of the selling points for them was the involvement of a prominent real estate management company. Before committing to the purchase, the buyers received assurances from the developer that the management company could not just "walk away" from the project and that the company was legally bound to the development for 30 years. Two years after the lot was purchased and before any house was built on it, the management company and the developer parted ways, ending the involvement of the company that had drawn the couple to the property.

The buyers sued under the federal Interstate Land Sales Full Disclosure Act. The Act requires that the prospective purchaser receive from the seller timely notice of its rights under the Act, as well as a property report. It was undisputed that these two requirements had not been met, but the developer sought to defend the lawsuit on the basis of a statute of limitations and an exemption in the Act that is based on the size of the development. Neither

of these defenses was successful.

There is a two-year statute of limitations in the Act for automatic revocation by right that, had it been applied, might have made the buyers' claim untimely. But the federal court ruled that another, three-year limitations period in the Act was to be applied. Under that provision, the claim by the purchasers of the lot to rescind the sale was timely.

As for the exemption defense, the Act states that it does not apply to the sale of lots in subdivisions containing fewer than 100 undeveloped lots. The Act also does not apply to "the sale or lease of lots to any person who acquires such lots for the purpose of engaging in the business of constructing residential, commercial, or industrial buildings," the so-called sales-to-builders exemption.

The sales-to-builders exemption is to be applied before the lot count is made; however, the developer could not include future sales in determining the number of sales that fell under the sales-to-builders exemption. Without

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## LLC Member Personally Liable

The owner of a lot on which a four-unit condo complex was to be built contracted with a small residential construction company to build the condos. The construction company was formed as a limited liability company (LLC), the only members of which were a licensed home builder and his wife. The licensed builder served as general contractor on the project, overseeing subcontractors that the LLC had selected.

A couple of months into construction, some structural problems surfaced. At first the builder's assurances that the problems would be fixed calmed the tensions with the owner, but over time, old defects weren't fixed and new ones arose, and the relationship deteriorated. Eventually the builder walked off the project, leaving dozens of defects unremedied. When the owner sued for damages, based on negligence and breach of warranties, he named as defendants not only the LLC but one of its individual members, the licensed builder.

One of the appealing characteristics of a limited liability company, as its very name indicates, is that a member of the LLC generally is not personally liable for the LLC's liabilities. In fact, the state LLC statute that applied in this case states that a "member or manager is not personally liable for a debt, obligation, or liability of the company solely by reason of being or acting as a member or manager."

As the individual builder discovered when he was found personally liable for a judgment of nearly \$1 million, the LLC shield against personal liability is not impenetrable. The state supreme court ruled that the protection against personal liability applies only to vicarious liability for nontortfeasor members. An individual who has done

nothing wrong will not be held liable simply by virtue of being a member or manager of the LLC. Where, as in this case, the individual is guilty of negligence, the protection of the LLC business form is lost.

The court acknowledged that, at least at first blush, its decision appeared to strip away one of the main reasons why a person chooses to form an LLC. But it was satisfied that there are other unaffected benefits to choosing to start a business as an LLC. The controlling rationale is akin to the concept of "piercing the corporate veil," that is, under some circumstances holding an individual corporate officer liable for wrongful conduct. Or as the court put it: "You don't buy immunity from suits for your torts by being a member of a business corporation."

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## Land Purchasers

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subtraction of those future sales, the calculation did not bring the development under the 100-lot threshold, making the developer subject to liability for its violations of the Act.

In ruling for the purchasers, the court essentially canceled the contract of sale for the property, rendering it as though it did not exist. Thus, the remedy for the failure of the developer to disclose objectively material information was the return of the property title to the developer and the return of the purchase price, plus interest, to the purchasers.

## Umbrella Insurance Policies

As insurance prices continue to rise, many people are looking for more and better insurance coverage for less money, and "umbrella policies" are often a good option for increasing coverage. Umbrella policies get their name from the coverage they offer: Like an umbrella, they provide expansive coverage for you and your assets. Umbrella policies act as a kind of backup for your primary insurance and can provide a cost-effective way of increasing your insurance coverage.

Most of us carry several kinds of liability insurance policies: car insurance, homeowner's insurance, renter's insurance, etc. All of these different policies do essentially the same thing: They cover us for the different careless acts we might commit. However, the coverage available under these different policies varies, and their cost is often very expensive compared with the coverage they provide.

Umbrella policies begin where other insurance ends. They provide additional coverage—coverage that is available only after the underlying liability policy has been exhausted. Umbrella policies are often surprisingly inexpensive, given that they can provide additional coverage in amounts up to \$1 million or more. The reason umbrella policies are relatively inexpensive is that they are asked to cover only the largest of claims. Because of this, the number of claims brought against umbrella policies is lower than the number of claims brought against "regular" policies.

As with any kind of insurance, the coverage offered by umbrella policies and the rates charged for them can vary greatly. Consider the possibility of buying an umbrella policy. You may find that it is right for you.

*Actual resolution of legal issues depends upon many factors, including variations of facts and state laws. This newsletter is not intended to provide legal advice on specific subjects, but rather to provide insight into legal developments and issues. The reader should always consult with legal counsel before taking action on matters covered by this newsletter.*

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## Background Checks

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erate to disproportionately exclude people of a particular race or national origin. Under this second theory, the employer can be found liable for discrimination unless it can show that the application of the criminal history information is “job related and consistent with business necessity” for the position in question.

The new Guidance is the culmination of the EEOC’s examination of a wide array of information. However, there are no substantial changes in the EEOC’s positions on the fundamental issues raised by employer use of criminal background data. These EEOC policies are unchanged:

- (1) An arrest alone does not establish that criminal conduct has occurred, although an employer may act based on evidence of conduct that disqualifies an individual for a particular job.
- (2) Convictions, on the other hand, are considered reliable evidence that a crime was committed.
- (3) Nationally, studies show that exclusions from employment due to criminal histories have a disparate impact on the basis of race and national origin, prompting the EEOC to investigate charges of this kind.
- (4) A blanket policy of excluding every person with a criminal record from employment, unless such exclusion is required by other federal law, will not satisfy Title VII’s requirement that the application of criminal history information be job related and consistent with business necessity.

The legality of an employer’s use of criminal histories is highly dependent on the facts of a particular decision, making it difficult to generalize. Still, the Guidance includes the following nonexhaustive list of some “best practices” for employers considering criminal record information when making employment decisions:

- Eliminate policies or practices that exclude people from employment based on any criminal record.
- Train managers, hiring officials, and decision makers about Title VII and its prohibition on employment discrimination.
- Develop a narrowly tailored written policy and procedure for screening applicants and employees for criminal conduct.
- Identify essential job requirements and the actual circumstances under which the jobs are performed.

- Determine the specific offenses that may demonstrate unfitness for performing such jobs.
- When asking questions about criminal records, limit inquiries to records for which exclusion would be job related for the position in question and consistent with business necessity.
- Keep information about applicants’ and employees’ criminal records confidential. Use it only for the purpose for which it was intended.

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## Lottery

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The court focused on these factors: There was no requirement for each family member to buy lottery tickets, no established pattern of buying lottery tickets, no pooling of money, no predetermined sharing percentages, and no definition as to the meaning of “substantial” winnings to which the agreement would apply. In addition, who was party to the agreement was unclear, and the agreement was essentially imposed by the taxpayer’s father rather than arrived at by family discussion. All in all, the arrangement was not a joint effort.

In Tonda Lynn’s loss may be found some lessons for other regular players in lotteries who want to achieve what she set out to do, should their ship come in. These elements may help avoid the fate of Tonda Lynn’s effort to share the wealth without gift taxes taking a big chunk of it:

- regular and consistent purchases of lottery tickets;
- a clear agreement to share winnings;
- common knowledge of the ticket purchases on the part of all participants; and
- joint decision making about what to do with winnings.

In fact, the Tax Court that ruled against Tonda Lynn cited a successful sharing arrangement from another case in which the evidence established the existence of an agreement between two men to share equally in the proceeds of any winning lottery ticket, in view of a long-standing course of conduct in which the men would jointly purchase tickets and jointly “scratch” them to reveal any winnings. The mutual promise exchanged by the two men to share in the proceeds of a winning lottery ticket amounted to adequate consideration for a valid contract.

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## Car Safety

### What if Your Brakes Fail?

Although rare, total brake failure can be a terrifying and perilous experience. As in all emergency situations, remaining calm is the first and most important step. In addition to that:

- Shift into a lower gear if your car has an automatic transmission. If it has a manual transmission, downshift.
- Engage the emergency brake.
- Turn on your emergency flashers and carefully pull off onto the side of the road.
- Turn off the engine and call for help.