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Pick *and Nebraska Employment Law: Interpreting Contracts and Good Faith*

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Nebraska has followed the national trend limiting employment at will. It recognizes oral contracts,[1] limits discharges that violate public policy,[2] and requires employers who promise jobs to deliver them.[3] None of these were recognized during the heyday of employment at will.

Last fall, the supreme court issued *Pick v. Norfolk Anesthesia, P.C.*,[4] an interesting addition to the development of employment law in Nebraska. In this brief article, I will comment on two aspects of *Pick*. First, *Pick* interprets employment contracts in an unusual way. Fortunately, the case isn't so specific that the Nebraska courts will be bound to continue down that path. I suggest an alternative way of interpreting employment contracts that is preferable and still open to the courts in Nebraska. Second, *Pick* alerted me to possibilities in Nebraska law that I thought had been foreclosed. I now think the covenant of good faith and fair dealing is recognized in employment contracts in Nebraska, despite language in prior opinions that made me think otherwise. And this is good.

The Case

The plaintiffs in *Pick* were seven nurse anesthetists who worked for Norfolk Anesthesia. They all worked under oral contracts that paid them about $120,000 each, plus an annual bonus that was paid near the end of the year.

In 2005, the nurse anesthetists all quit on September 16. When the end of the year rolled around, the employer failed to pay them their bonuses claiming that the bonuses only had to be paid if the nurse anesthetists were still employed at the end of the year. So the nurse anesthetists sued. Formally, the claim was a statutory one alleging a violation of the Nebraska Wage

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[1] *See*, *e.g.*, Mueller v. Union Pac. R.R., 220 Neb. 742, 371 N.W.2d 732 (1985).

[2] *See*, *e.g.*, Jackson v. Morris Commc'ns Corp., 265 Neb. 423, 657 N.W.2d 634 (2003); Schriner v. Meginnis Ford Co., 228 Neb. 85, 421 N.W.2d 755 (1988).

[3] Goff-Hamel v. Obstetricians & Gyns., P.C., 256 Neb. 19, 588 N.W.2d 798 (1999). *Goff-Hamel* illustrates both the trend away from employment at will and its limits. Not all employer promises to deliver jobs are enforceable—only those where there is detrimental reliance.

[4] 276 Neb. 511, 755 N.W.2d 382 (2008).

Payment and Collection Act (NWPCA). But practically, it was a case about oral contracts. If the oral contracts said that the bonuses had to be paid, then the NWPCA was violated; if not, it wasn't.[5]

The district court found for the plaintiffs. It held that the oral contracts provided that bonuses had to be paid if the company had a profit at the end of the year, which it did.[6] Importantly, the district court also found that the oral contracts did ***not*** require that the nurse anesthetists remain on staff until the end of the year to get their bonuses.[7]

The supreme court reversed in an opinion written by Chief Justice Heavican. The court applied the "commonsense notion that absent an express agreement otherwise, an employee ordinarily forfeits the right to receive a bonus by resigning before the [year] ends."[8] Here, the court said, there was no *express* agreement that a bonus would be paid if the employees left before the end of the year. Therefore, since they had resigned in September, they were not entitled to bonuses.

Interpreting Employment Contracts

The unusual thing about the supreme court's result is that the district court had found as a factual matter that the oral employment agreement did ***not*** require an employee to be working at the end of the year to remain eligible for the bonus.[9] Since the supreme court did not and could not properly overrule this factual finding, the court's holding rests on the thin reed of how express the contract was on this point. The court said that because the oral contracts did not expressly counter the legal presumption that one has to work to the end of the year to earn a bonus, the employees lose.[10] That is an unfortunate result, and it opens the door to more mischief in interpreting employment contracts.

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[5] Despite this, the NWPCA was in the case for an important reason. The NWCPA provides for attorney's fees; garden-variety contract claims do not.

[6] The case also involved a dispute about the size of the bonus, but that is not relevant to the issues I am discussing.

[7] The district court stated both these points clearly and strongly: "The bonus had been previously agreed to *by all the parties* . . . ." Pick v. Norfolk Anesthesia, P.C., No. CI05-686R at 2 (Dist. Ct. Madison County, Neb. Feb. 15, 2007) (emphasis added). "There is *no evidence* to establish that one of the requirements for the payment of the bonus was that the plaintiffs work the full year." *Id.* at 3 (emphasis added).

[8] 276 Neb. at 518, 755 N.W.2d at 388. The case actually references the end of the "corresponding bonus period" rather than the end of the year. I use "year" simply as shorthand.

[9] *See supra* note 7.

[10] Justice Gerrard concurred in the decision. His decision was less damaging to employment law than the majority's, but it is probably even more difficult to justify. He found for the employer because working to the end of the year was "a known and negotiated condition of receiving the bonus." 276 Neb. at 519, 755 N.W.2d at 388. But this is impossible to square with the district court's finding that there was "no evidence" to establish such a requirement.

Consider two possible factual situations. First, the actual situation in *Pick* was that the fact-finder determined that the employment contracts (1) contained only one condition for an employee to receive a year-end bonus (the existence of company profits) and (2) did not require that the employees remain in employment at the end of the year to maintain eligibility for a bonus. The supreme court's holding was that there is a "commonsense notion"—read that as a legal presumption—that every employment contract providing for a bonus also has a condition that the employee has to be employed at the end of the year to get the bonus and that the legal presumption can be overridden only by an "express" provision. This is unfortunate. It is a throwback to employment at will in its heyday when the courts regularly ignored the parties' true intentions in favor of hard-to-override legal presumptions that heavily favored employers.[11]

Pick happened to be a case about year-end bonuses, but its analysis opens the door to lots of other post hoc court-discovered clauses in employment contracts. Thus, *Pick* presents the potential of being even more unfortunate. In most cases, when the parties agree on something, the courts should respect their decision.[12]

But *Pick* is troubling at a deeper level, too. Consider a slightly different situation than the one presented in *Pick*. Assume that the district court had found that the bonus only had to be paid if there were year-end profits, but it simply could not determine the parties' intent on the issue of what should happen if the employees resigned before the end of the year. (Note that this is different than the actual situation in *Pick* because there the district court found that the agreement had resolved the latter issue.)[13] What should a court do when the parties' agreement does not resolve an issue like this?

There are two general views on how courts should address this type of issue in employment contracts. First, the courts can use a mimic-the-parties approach where it applies the rule it thinks the parties would have agreed to had they thought about it. If working to the end of the year to qualify for a bonus really is a "commonsense" notion, then that is what the parties would have agreed to and, therefore, that is how the court should decide the issue. But this approach means that the courts have to try to divine the parties' likely intent. That is difficult in most employment contracts because the parties normally have quite different and opposing interests.

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[11] *See, e.g.*, Skagerberg v. Blandin Paper Co., 266 N.W. 872 (Minn. 1936) (holding that "permanent" employment means at-will employment and cannot be enforced without "extra" consideration). *See generally* STEVEN L. WILLBORN ET AL., EMPLOYMENT LAW: CASES AND MATERIALS 63-65 (4th ed. 2007).

[12] There are exceptions, of course. Most significantly, when third party interests are affected by an employment contract, the courts may intervene. An agreement to murder someone is not enforceable. That is the underlying theory of the modern tort limitations on employment at will. *See generally* Stewart J. Schwab, *Wrongful Discharge Law and the Search for Third Party Effects*, 74 TEX. L. REV. 1943 (1996).

[13] For two reasons, it will not do to say that the oral contract in *Pick* was silent on the end-of-the-year issue and the supreme court was merely filling in the gap. First, that's not consistent with the facts found by the district court. The district court found that the contract did ***not*** contain such a requirement. Second, and more broadly, no contract covers everything. If the supreme court can add a term anytime there's any gap whatsoever, there's just too much room for interference with the parties' intentions. ("We find that the parties didn't talk about whether the plaintiff had to hold his nose and spin three times to qualify for his bonus; the contract required that and the plaintiff didn't meet the condition.") There has to be a limit. "Commonsense" is a vague limit, of course, but it doesn't and can't carry the load.

Another approach to this issue is called the penalty-default approach. Instead of trying to divine the parties' intent, the court's goal in this approach is to encourage the parties to settle the issue themselves. The general idea is to set the default rule against the party who is most likely to know the rule and act to counter it. That is, to "penalize" that party to encourage it to address the issue in the agreement itself and, in so doing, to disclose valuable information to the other party.[14] In the *Pick* situation, this would mean setting the rule to disfavor the employer: Employees do *not* have to work to the end of the year to qualify for a bonus. Employers are repeat actors, they are more likely to know the default rule, they are more likely to be the drafters of the contract, and they are more likely to have legal counsel. If the default is set against the employer, it is likely the employer will know about it and, thus, address it (and counter it) in the employment agreement itself. When this occurs, the court won't have to guess the parties' intent—it will know it. And so will *both* of the parties before any dispute arises.

Again, the penalty-default approach creates incentives for the parties themselves to resolve contested issues, rather than the courts. And, when the parties do that, it makes it less likely the disputes will ever end up in court. Both of those are very good results.

Pick implies that the Nebraska Supreme Court is going to use a mimic-the-parties approach to uncertainty in employment contracts. But *Pick* doesn't make a holding on that point. Instead it uses its "commonsense" to insert a provision into an employment contract without any guidance at all about where the provision comes from. Maybe the court was guessing what the parties would have wanted. If so, *Pick* was using a mimic-the-parties approach. At least, that would provide lower courts, employers, and employees with some guidance about what discovered provisions we might find in employment contracts in the future. But we simply do not know if that's what the court thought it was doing.

The absence of guidance in *Pick* has its upside. The court has certainly not bound itself to any particular approach in interpreting employment contracts. When it has another opportunity to do so, I would urge it to consider a penalty-default approach that will encourage employers to reveal valuable information to employees about the terms of their agreement. Over time, this would mean that there will be fewer surprised and disappointed plaintiffs like those in *Pick*. It would also mean fewer court cases and, accordingly, fewer situations in which courts are put in the uncomfortable position of determining the parties' agreement for them.

Good Faith in Nebraska

For years, I have told my students that, although Nebraska does pretty well, there is one area where we have failed to keep up with modern trends in employment law. Based on unequivocal language from the supreme court, I would tell them that the court has failed to limit

[14] This idea is well received and supported in the legal literature both in employment law specifically and in contract law generally. *See* Cass R. Sunstein, *Switching the Default Rule*, 77 N.Y.U. L. REV. 106 (2002) (discussing the idea in employment law); Ian Ayres & Robert Gertner, *Majoritarian vs. Minoritarian Defaults*, 51 Stan. L. Rev. 1591 (1999) (discussing the idea in contract law generally). Recently, a popular and easy-to-read book has discussed the value and importance of "choice architecture," including how to set default rules appropriately. RICHARD H. THALER & CASS R. SUNSTEIN, NUDGE: IMPROVING DECISIONS ABOUT HEALTH, WEALTH, AND HAPPINESS (2008).

employers when they do not act in good faith.[15] But, I would tell them, it would be hard for the supreme court to deny such a claim if it were presented with a classic case, such as one where an employee had fully earned a bonus, but was fired just before receiving it so the employer could keep the money itself.[16] I did not realize until *Pick* that the supreme court *has* been presented with such a case, and that it *did* find for the plaintiff.[17]

Pick contains a "*cf.*" cite to *Sinnett v. Hie Food Products, Inc*.[18] *Sinnett* presented the court with an extreme version of the classic good faith and fair dealing case. The plaintiff was promised a bonus if he worked an entire year. He began employment on October 1, 1967, so he would have become entitled to the promised bonus if he had worked a full day on September 30, 1968. But the employer fired him during the day on September 30 and denied him the bonus. The Nebraska Supreme Court held that it did not matter that the employment agreement was terminable at will; the employee was entitled to the bonus anyway where he was fired without good cause.[19]

The court did not discuss the theory of its holding, but it has to be the covenant of good faith and fair dealing. Consistent with that view, *Sinnett* has been cited by other courts and authorities as resting on the covenant, including *Fortune v. National Cash Register Co.*,[20] the leading case nationally applying the covenant in an employment case.[21]

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[15] *See, e.g*., Renner v. Wurdeman, 231 Neb. 8, 15, 434 N.W.2d 536, 541 (1989) ("[T]his state continues to deny any implied covenant of good faith or fair dealing in employment termination."); Jeffers v. Bishop Clarkson Mem'l Hosp., 222 Neb. 829, 833, 387 N.W.2d 692, 695 (1986) (exactly the same quote; different cites).

[16] This is one of the two classic situations in which the covenant of good faith and fair dealing has been recognized. *See, e.g.,* Fortune v. National Cash Register Co., 364 N.E.2d 1251 (Mass. 1977). The other is a situation where the employer fires an employee for performing the duties required by his job. WILLBORN, *supra* note 11, at 183.

[17] Sinnett v. Hie Food Products, Inc., 185 Neb. 221, 174 N.W.2d 720 (1970). Two things in my defense: First, despite its importance, *Sinnett* is not mentioned at all in Bob Evnen's Bible of Nebraska employment law. Robert B. Evnen, Developments in the Law of Employment at Will, *in* TRYING MATTERS IN EMPLOYMENT LAW (Neb. Continuing Legal Educ. & Neb. State Bar Ass'n Labor and Employment Section, 2003). Mr. Evnen assures me that it will be in the next edition. Second, as I often tell my students, I'm an academic, not a *real* lawyer. For real law, it's always better to rely on real lawyers.

[18] 185 Neb. 221, 174 N.W.2d 720.

[19] *Id*. at 223-224, 174 N.W.2d at 722. *Sinnett* was cited in *Pick* because of dicta in the case that said that employees are not entitled to bonuses when they voluntarily quit before the end of the year. *Id*. at 224, 174 N.W.2d at 722. That only merited a "*cf.*" cite in *Pick* both because it was dicta and because it was made in a situation where the agreement was silent, not one like *Pick* where the fact-finder had found that working to the end of the year was *not* required by the parties' contract.

[20] 364 N.E.2d 1251 (Mass. 1977).

[21] In addition to *Fortune*, see *Maddaloni v. W. Mass. Bus Lines, Inc*., 422 N.E.2d 1379, 1384 (Mass. App. Ct. 1981) (citing *Sinnett* and saying situation "calls for implication of a covenant of good faith"). *See also* 14 WILLIAM MEADE FLETCHER ET AL., FLETCHER CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS § 6763 n. 8 (perm. ed., rev. vol. 2003) (citing *Sinnett* to support proposition that some courts have enforced implied covenants of good faith and fair dealing).

So what is one to make of a situation like this? On the one hand, in *Sinnett*, the court found for an employee in a holding that had to be based on the covenant of good faith and fair dealing. But in other cases, the court has held against employees while saying that the covenant does not apply in employment cases.

This is not such a hard problem. It presents standard-fare issues about how to harmonize two lines of cases. So let's examine what we know for sure, and what is still open to debate.

First, we know that, despite inconsistent language, Nebraska recognizes the covenant of good faith and fair dealing in employment cases. That is the only explanation for the holding in *Sinnett*. The court did not categorize its decision in *Sinnett* as one based on good faith and it may call it something else the next time to avoid direct conflict with its no-good-faith language in other cases. But for practical purposes, when the court is faced with a classic good faith claim (the *Sinnett* case), it is going to decide it as if it were a good faith claim.

Second, we know that Nebraska is not going to interpret the covenant of good faith expansively. In California, the covenant was once interpreted so broadly that it came very close to eliminating the underlying employment-at-will rule.[22] Nebraska will not do that. We know this from *White v. Ardan, Inc*.,[23] in which the court rejected a good faith claim where the basic argument was that the discharges were improper because an employer had said false and mean things about the discharged employees.

Third, somewhat less certainly, I would predict that Nebraska will follow those states that in *Sinnett*-like situations permit the covenant to be used only to recover damages, but not to challenge discharge decisions themselves.[24] Recovery of the bonus was the remedy in *Sinnett*, but that was all that the plaintiff was seeking. So the issue is not resolved. But the skeptical language about the covenant in cases like *White v. Ardan* makes it likely that the courts will be inclined to limit the cause of action in this way, rather than to treat it more broadly.

But there is much we do not know about good faith claims in Nebraska, too. Although we know the outer boundaries, we do not know the precise dividing line between successful and unsuccessful claims. We know that a classic *Fortune* case will be successful; that's *Sinnett*. We know that a *Foley*-type claim will fail; that's *White v. Ardan*. But we do not know precisely where Nebraska will draw the dividing line. Significantly, we do not know where Nebraska would come down on the other classic type of good faith case: a situation in which an employee is fired for performing the duties required by the job. The justification for finding a violation of the covenant in this situation is that it protects an employee against the catch-22 of being fired

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[22] *See* Foley v. Interactive Data Corp., 765 P.2d 373 (Cal. 1988) (termination without cause after working for an employer for about seven years violates covenant of good faith and fair dealing), *later limited by* Guz v. Bechtel Nat'l, Inc., 8 P.3d 1089 (Cal. 2000); *see also* Wagenseller v. Scottsdale Mem'l Hosp., 710 P.2d 1025, 1040 (Ariz. 1985) (accepting California's version of the covenant would "tread perilously close to abolishing completely the at-will doctrine . . . "; the court adopted a narrower version).

[23] 230 Neb. 11, 430 N.W.2d 27 (1988).

[24] *See* Wakefield v. N. Telecom, Inc., 769 F.2d 109, 112 (2d Cir. 1985) (covenant may not be used to challenge the "termination *per se*," but can be used to claim denied commissions).

for doing what the job requires him to do. But not all states have accepted it in that circumstance.[25]

Of course, many other variations on the good-faith theme also remain to be explored in Nebraska. But the message for Nebraska practitioners is that, despite language to the contrary, good faith claims are alive and well in employment cases. And that's as it should be. Nebraska courts shouldn't be in the business of protecting people who act in bad faith.

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[25] *See*, *e.g.*, Murphy v. Am. Home Prods. Corp., 448 N.E.2d 86 (N.Y. 1983).