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LETTER FROM THE EDITORS

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EMPLOYMENT AT-WILL

Ed Sentell, Mississippi College
Randall Robbins, Mississippi College

The doctrine of employment at-will emerged as the predominant rule in wrongful discharge cases in America during the latter part of the 19th century. This doctrine states that the business should have the freedom to discharge or retain employees at-will for good cause, for no cause, or even for bad cause, without thereby being guilty of an unlawful act. It is a right which an employee may exercise in the same way, to the same extent, for the same cause or want of cause as the employer. In essence, the doctrine recognizes that the wage owner's the full owner of his labor services, and the business the full owner of his capital. Each is free to exchange on whatever terms they see fit.

Thus, the doctrine of employment at-will is well established in the American legal system. In recent years, however, this doctrine has been eroding. Many employers now find that the legal environment relative to the right to fire is confusing and ripe with potential liability.

In essence, employment at-will - - - a term that is music in the ears of most employers - - - is under attack. This paper seeks to address the solvency of the employment at-will doctrine in the state of Mississippi. Recent court cases and rulings will be addressed to determine and suggest the direction and longevity of this doctrine.

HISTORICAL DEVELOPMENT OF THE EMPLOYMENT AT-WILL DOCTRINE

As early as the 16th century, England had a statute prohibiting employers from discharging employees unless it be done for some reasonable and sufficient cause or matter. Although this statute was repealed, the rule in England eventually became that an employment contract that did not specify a specific duration was presumptively for a one-year term. The person seeking to terminate the contract prior to one year had the burden of proving that the employment was terminable at the will of either party. This became known as the "English Rule."

During the early 19th century, the United States adopted the English Rule as part of their common law. By the late 1800's, however, most jurisdictions had abandoned this principle. Reasoning was that restrictions on terminating employment were inconsistent with the laissez-faire philosophy dominant in the United States. Thus, the "American Rule" became that an employment contract of indefinite duration was terminable at the will of either party, for cause, for no cause, or even for bad cause. Subject to specific statutory restrictions, an employer has the right to discharge an employee at any time without notice and for any reason or for no reason at all.

The Industrial Revolution planted the seeds for the erosion of the employment at-will doctrine. When employees began forming unions, the collective bargaining agreements they subsequently negotiated with employers frequently had provisions in them that required just cause for adverse employment actions, as well as procedures for arbitration employee grievances.[1] The 1960's marked the beginning of Federal legislative protections (including Title VII of the 1964 Civil Rights Act) from wrongful discharge based on race, religion, sex, age, and national origin.[2] The recognition of employment as being central to a person's livelihood and well-being, coupled with the fear of being unable to protect a person's livelihood from unjust termination, led to the development of common-law, or judicial, exceptions to the employment at-will doctrine beginning in the late 1950's. The bulk of the development of these exceptions did not take place until the 1980's, with the employment at-will doctrine being significantly eroded by statutory and common-law protections against wrongful discharge.

The most widespread exception prevents terminations for reasons that violate a state's public policy. Another widely recognized exception prohibits terminations after an implied contract for employment has been established; such a contract can be created through employer representations of continued employment, in the form of either oral assurances or expectations created by employer handbooks, policies, or other written assurances. Finally, a minority of states has read an implied covenant of good faith and fair dealing into the employment relationship. Interestingly, three southern States - Florida, Georgia, and Louisiana - and Rhode Island do not recognize *any* of the three major exceptions to employment at-will.

Under the public-policy exception to employment at-will, an employee is wrongfully discharged when the termination is against an explicit, well-established public policy of the state. For example, in most states, an employer cannot terminate an employee for filing a workers' compensation claim after being injured on the job, or for refusing to break the law at the request of the employer. The majority view among states is that public policy may be found in either a state constitution, statute, or administrative rule, but some states have either restricted or expanded the doctrine beyond this bound. The public-policy exception is the most widely accepted exception, recognized in 43 of the 50 States.[3]

The second major exception to the employment at-will doctrine is applied when an implied contract is formed between an employer and employee, even though no express, written instrument regarding the employment relationship exists. Although employment is typically not governed by a contract, an employer may make oral or written representations to employees regarding job security of procedures that will be followed when adverse employment actions are taken. If so, these representations may create a contract for employment. This exception is recognized in 38 of the 50 States.[4]

Recognized by only 11 states, the exception for a covenant of good faith and fair dealing represents the most significant departure from the traditional employment at-will doctrine.[5] Rather than narrowly prohibiting terminations based on public policy or an implied contract, this exception

- at its broadest - reads a covenant of good faith and fair dealing into *every* employment relationship. It has been interpreted to mean either that employer personnel decisions are subject to a "just cause" standard or that terminations made in bad faith or motivated by malice are prohibited.[6]

HISTORY OF EMPLOYMENT AT-WILL IN MISSISSIPPI

Absent a contract for a specified period of time, Mississippi has traditionally followed the employment "at-will" doctrine.[7] The common law concept of "employment at-will" has been broadly defined as a contract for employment for an indefinite period or term which may be terminated by the employer or the employee with or without cause at any time.[8]

Throughout most of Mississippi's jurisprudential history, the courts have been reluctant to infringe on the rights of employers and employees to enter into such a relationship.[9]

The basic premise underlying the employment at-will doctrine in Mississippi is that an employer who employs someone without entering into a written contract, employs someone without entering into a written contract, and who enters into a written contract that does not specify any period of time, is considered an "at-will" employer who may terminate an employee at his or her pleasure, with certain limited exceptions which will be explored below. Under Mississippi law, where there is no employment contract, either party may terminate the employment.[10]

Mississippi's former adherence to this rule is illustrated in the case of *Kelly v. Miss. Valley Gas Co.*, 397 So.2d 874 (Miss. 1981). In *Kelly,* the Mississippi Supreme Court was faced with the question of whether "to adopt a public policy exception to the common law rule that an employment contract at-will may be terminated by either party with or without cause or justification, and hold an employer liable to an employee in a common law tort action when an employer has discharged an employee for filing a workers' compensation claim." *Id.* at 874. Here, the Mississippi Supreme court rejected, in no uncertain terms, the opportunity to create a public policy exception to an employer's right to discharge an employee when he asserted his rights under the Workers' Compensation Act.[11]

The court reached its decision despite conceding that the employee in his declaration had posed a "valid public policy question" and resolved to leave for the legislature the job of fashioning any possible remedy in the situation where someone was terminated in retaliation for filing a comp claim. *Id* at 877.

INTEREST IN THE CREATION OF AN EXCEPTION TO THE EMPLOYMENT AT-WILL DOCTRINE

In recent years however, Mississippi courts have expressed their growing unease with the harshness of the rule authorizing an employer to terminate an employment contract for a good reason, a bad reason or no reason at all.

Foreshadowing the Supreme Court's position change, the case of *Shaw v. Burchfield*, 481 So.2d 247 (Miss. 1987), was decided in 1987. The Court, in this case, expressed an interest in altering the employment at-will rule. *Shaw* involved a longtime agent of a group of three Farm Bureau insurance agencies. Shaw, who was under contract with all three respective agencies, alleged breach of contract, unintentional interference with contract or prospective business advantage, in civil conspiracy. The Supreme Court, in a unanimous decision, expressed frustration with the employment at-will doctrine, but the Court was constrained to formulate a remedy in this situation due to the fact that the parties had signed contracts governing that their relationship which allowed for termination without cause and were, thus, subject to this privately made law.[12]

The Court used the opportunity in the *Burchfield* case to vent its displeasure at the results the at-will doctrine sometime produces. This case presents us with an all too familiar scenario upon the landscape of corporate America. A man invests twenty-six years of his impersonal, corporate organization, in this case an insurance company. Used up, he is discharged on ten-days' notice, no cause given and, it is contended, none required. In the end, the attendant rights and burdens are imposed by law, not sympathy or outrage.[13]

In this case, there was an indication the Court would be willing to reconsider the "at-will" doctrine under the proper circumstances:

> Were this a case where no employment contract established expressly the ground rules for termination and where the employer was calling upon the state to furnish the law which authorized termination, we might well be charged to reconsider the at-will termination rule.[14]

Shaw was then followed by *Perry v. Sears & Roebuck Co., 508* So.2d 1086 (Miss. 1987) and *Hartle v. Packard*, 626 So.2d 106 (Miss. 1993). Those cases ultimately upheld the proposition that Mississippi simply did not recognize a wrongful discharge action which was not founded upon a written contract. In *Hartle* and *Perry*, the Mississippi Supreme Court reiterated its position that employees at-will had no cause of action for a wrongful termination. The court did however, in *Perry* define the nature of two distinct wrongful termination causes of action it was rejecting - (1) the first described as being based on an implied covenant of good faith and fair dealing, and (2) the second based on a public policy exception. The Court did indicate that it would modify the employment at-will doctrine given the appropriate opportunity.

EXCEPTIONS TO THE AT-WILL DOCTRINE - EMPLOYEE HANDBOOK

The employee handbook exception to the employment at-will doctrine has evolved over a period of several years. In 1985, the Mississippi Supreme court held that a written contract can be modified by a policy handbook which then becomes part of the contract where the contract expressly provides that it will be performed in accordance with the policies, rules, and regulations of the employer.[15] By 1992, however, the Mississippi Supreme Court broadened and reaffirmed that exception holding that a contract no longer had to expressly provide that it be performed in accordance with company policies. Instead, the court held that when an employer publishes a manual setting forth the procedures which will be followed in the event of an employee's infraction of the rules, and there is nothing in the employment contract to the contrary, the employer will be required to follow its owner manual in disciplining or discharging employees for infractions or misconduct specifically covered by the manual.[16] Essentially, by creating an employee handbook, an employer can create contractual obligations that override the at-will employment doctrine. Although the court later explained that employee handbooks do not create a right to employment for a definite length of time, they can create rights and obligations on the part of the employers.[17]

Although *Bobbitt* made it clear that an employee manual could "become part of a contract" and give employees additional rights, the mere existence of an employee manual will not necessarily prevent an employer from terminating an at-will employee. In *Hartle v. Packard Electric*,[18] the court held that the at-will relationship of an employee with a contract for month to month employment is not altered if he or she is given an employee handbook listing a number of reasons for which he or she "may" be discharged. The court found that simply because certain acts were identified as conduct that might lead to discharge did not indicate that those acts were the exclusive permissible grounds for discharge. The court in *Hartle* also reaffirmed that an employee handbook will not be deemed to create an employment contract between the employer and the employee where the handbook explicitly states that the employee can be terminated at-will.[19] The employer in *Hartle* gained some additional protection because the employment agreement itself provided that any modification to it had to be endorsed in writing and initialed by both the employer and employee.

On January 19, 2001, a divided Mississippi Supreme Court again addressed the employee handbook exception to employment at-will doctrine. In *Lee v. Golden Triangle Planning & Development District, Inc.,* No. 1999-CA-01849-SCT (Miss. 2001), the Court made clear the important of employers 1) promulgating a well-drafted employee handbook; and 2) properly documenting poor performance as a prelude to disciplinary action. The Court found disclaimer language in the employee handbook sufficient to preserve the at-will nature of Lee's employment. Therefore, *Bobbitt* did not apply to the facts of this case. Two judges dissented from the majority opinion because, in their view, *Bobbitt's* reach is not dependent on disclaimer language or premise analysis of disciplinary rules. In his dissent, Justice McRae stated handbooks must be governed as "a two-way street, informing the employee of their benefits as well as the consequences of their actions and the employer should not be allowed to disregard all the provisions in the employee handbook if the employees agree to abide by it."

EXCEPTIONS TO THE AT-WILL DOCTRINE - PUBLIC POLICY

After recognizing that employee handbooks could impose additional obligations on employers, the Mississippi courts were confronted with the question of whether a public policy exception should be carved out of the employment at-will doctrine for the refusal of an employee to participate in criminal activity. *In McArn v. Allied Bruce-Terminix Co.*,[20] the plaintiff alleged that he was terminated because he reported conduct by the employer which was arguably a crime under Mississippi law. In its review of the matter, the Mississippi Supreme Court observed that a federal district court in Mississippi had previously held that it believed Mississippi courts would recognize a narrow public policy exception to the at-will doctrine in such circumstances.

The *McArn* court then went on to track the history of the employment at-will rule in Mississippi since *Kelly,* quoting *Shaw v. Burchfield,* 481 So.2d 247 (Miss. 1985), as representing the first case in which the Mississippi Supreme Court openly questioned the wisdom of the employment at-will rule when it stated that "under fire is the notion that, absent an employment contract expressly providing to the contrary, an employee may be discharged at the employer's will for good reason, bad reason, or no reason at all, accepting only reasons independently declared legally and permissible." *Shaw,* 481 So.2d at 253-54.

The Mississippi Supreme Court embraced that prediction and held that: (1) an employee who refuses to participate in an illegal act shall not be barred by the common law rule of employment at-will from bringing an action in tort for damages against his or her employer; and (2) an employee who is discharged for reporting illegal acts of his or her employer to the employer or anyone else is not barred by the employment at-will doctrine from bringing an action in tort against his or her employer.[21] At the time of the *McArn* decision, the court did not address whether such conduct by an employer might give rise to punitive damages.[22]

The next case in which the Mississippi Supreme court dealt with this cause of action was *Willard v. Paracelsus.* The court added little in the way of additional definition of the "public policy" cause of action (with the possible exception of consistently, throughout the opinion, referring to this cause of action as one for "retaliatory discharge.') *Willard v. Paracelsus*, 681 So.2d 539 (Miss. 1996).

Applicability of the exception to the employment at-will doctrine for the termination of an employee who refused to participate in an illegal act does not require that a crime has already been committed, but it does require that the acts complained of warrant the imposition of criminal penalties, as opposed to mere civil penalties. *Hammons v. Fleetwood Homes of Mississippi, Inc.*, 2004 WL 2711313 (Miss. Ct. App. 2004).

TORTUOUS INTERFERENCE WITH CONTRACT

The next breach of the hard line employment at-will doctrine came with the case of *Levens v. Campbell,* 733 So.2d 753 (Miss. 1999).[23] In that case Ann Levens, a nurse, was initially offered employment with Memorial Hospital in Gulfport, Mississippi. *Id.* at 755-56. Ms. Levens was informed that she would be hired and, after being so informed, was told that the hospital had suddenly invoked a "hiring freeze." *Id.* at 757. Ms. Levens was highly suspect of this "hiring freeze," as a woman, Cindy Campbell, the Chief Operating Officer of the hospital, was, at the time involved with Ms. Levens' ex-husband (the two, (Campbell and Levens' former husband) did ultimately marry in 1993). *Id* at 756. Ms. Levens believed that Cindy Campbell had been responsible for the "hiring freeze" and had used the excuse simply to maliciously and intentionally interfere with her ability to work at the Memorial Hospital in Gulfport. *Id* at 757.

Herein, it is of note that there was absolutely no allegation of any fraudulent, deceptive or illegal act, only that Cindy Campbell had *maliciously* and *intentionally* interfered with Ann Levens' at-will employment relationship with Memorial Hospital at Gulfport.[24] Thus, the cause of action addressed in *Levens* differs markedly from that recognized in *McArn* and *Willard.*

Mississippi Supreme Court found that, although Ann Levens had evidently been unable to adduce evidence to support the cause of action of wrongful termination, such cause of action did exist and is available to at-will employees in Mississippi. It held:

> This Court concludes that a claim for tortious interference with at-will contracts of employment is viable in this state as well. An action for tortious interference with contract ordinarily lies when a party *maliciously* interferes with a valid and enforceable contract causing one party not to perform in resulting in injury to the other contracting party.
>
> *Id.* at 760 (emphasis added).

The Mississippi Supreme Court also addressed Ann Levens' claim of a conspiracy to tortiously interfere with her employment. Ms. Levens' allegations were directed towards Ron Burton, Administrator of the hospital and Cindy Campbell, Chief Operating Officer at the hospital. These were the only two individuals that Levens alleged to have been involved in the conspiracy and, notably, *both were employees of the hospital*. Despite the fact that both such employees worked for the hospital, the Mississippi Supreme court found that Levens could maintain an action for such a civil conspiracy, had she had the necessary evidence to support the fact that their actions had been taken in bad faith. In so finding, the Court cited to *Shaw* for the proposition that:

> The individual Defendants here were officers and agents of the various Farm Bureau Insurance Companies. The record establishes without contradiction that they had

> responsibilities with respect to Shaw's employment with those companies and the three contracts in issue. Where a corporation has a contract with another, and where an individual who is an agent of the corporation has responsibilities with respect to the contract, *any actions taken in good faith* within the scope of those responsibilities *are privileged* and thus not actionable. [Citations omitted]. There being no showing of bad faith in the record sufficient to avoid summary judgment, and there otherwise being no genuine issue of material fact, we hold that the trial judge correctly determined the Defendant entitled to judgment as a matter of law.

Shaw, 481 So.2d at 254 (emphasis added). In summarizing its recognition of this cause of action, the court stated:

> Referring again to *Shaw v. Burchfield*, this court determined that civil conspiracy resulting in damage may well give rise to a right of recovery under our law, but there is no actionable conspiracy where all that is shown is the exercise in a lawful manner of a right to terminate a contract.
>
> *Id.*

> Although Mississippi does recognize this conspiracy cause of action in at-will employment situations, the record does not reflect the elements necessary for a conspiracy.
>
> *Id.* at 761.

The Mississippi court then, in 1999, revisited the *Willard* case, issuing a second opinion affirming a $3 million punitive damage award for the terminations in violation of public policy.[25,26]

REJECTION OF CLAIMS BASED ON IMPLIED COVENANT OF GOOD FAITH AND FAIR DEALING

Mississippi courts have consistently rejected claims based upon an implied covenant of good faith and fair dealing. Although the Supreme Court has never recognized an implied covenant in at-will employment, the attacks on the at-will doctrine have continued. *See Slatery v. Northeast Procurement, Inc.*, 747 So.2d 257 (Miss. 1999) (Slatery's claim for breach of an implied covenant of good faith and fair dealing "without merit'); *accord*, *Hartle v. Packard Elec.*, 626 So.2d 106 (Miss. 1993); *Perry v. Sears, Roebuck & Co.*, 508 So.2d 1086 (Miss. 1987). Justice James L. Robertson, joined by Justice Hawkins, penned a special concurrence in *Perry*, in which he stated that he found the argument for a duty of good faith and fair dealing appealing and that such had been adopted in other jurisdictions. 508 So.2d at 1090. He advised opponents and advocates of the employment at-will doctrine to do their homework, inviting further arguments on the issue. In *Adams v. Institute of Community Services, Inc.*, 727 So.2d 739 (Miss. App. 1998), *rehearing denied* (1999), *cert. denied*, (1999), the Mississippi Court of Appeals opined that implication of a duty of good faith and fair dealing would, in effect, destroy the very nature of at-will employment.

The Supreme Court is now sharply divided over the issue. *Young v. North Mississippi Medical Center*, 783 So.2d 661 (Miss. 2001). There, Justice Pittman, writing for the six-justice majority, reiterated, "this Court has specifically held that at-will employment relationships are not governed by a covenant of good faith and fair dealing." The Court did not rule out the possibility of reversing itself in the future, however, noting that the plaintiff, Mr. Young, could not claim the implication of such a duty in his case because he quit his employment and did not raise any issue of contractive or wrongful discharge until appeal. The three dissenters, in an opinion by Justice McRae, argue that the duty of good faith and fair dealing applies to all employment relationships.

WHERE THE LAW IS GOING

The Mississippi Supreme Court's dissatisfaction with the sometimes harsh results of the employment at-will doctrine has manifested itself in several exceptions to the basic employment at-will doctrine. *Bobbitt v. Orchard, Ltd*, 603 So.2d 356, 361 (Miss. 1992).

One possible additional public policy exception to the at-will employment rule may occur in the case of an employee who is fired for filing a workman's comp. claim. This has been one of the foremost causes of action recognized by other states. Most states have recognized an exception to the at-will employment rule where employees were fired for filing workman's comp. claims. Stressing the underlying public policy of compensating injured workers, the court's reason that unchallenged retaliatory discharges will undermine the purposes of the workman's compensation statutes.

The question arises as to just what possible scenarios additional exceptions to the employment at-will doctrine might extend. Employers will argue strenuously that *the McArn* exception is very limited. Courts outside Mississippi have recognized an assortment of exceptions based upon a wide array of fact situations - including everything from termination for filing a workman's compensation claim for termination for complaining of sexual harassment.

During the last few legislative sessions, the Mississippi Legislature has entertained a draft "fair employment practices act" which, if passed and signed into law, would have statutorily eliminated the employment at-will doctrine, and would generally have required an employerto have cause to terminate an employee. These Bills have died in Committee.

Only two states - Arizona and Montana - have enacted comprehensive wrongful termination legislation. Montana passed a Wrongful Discharge from Employment Act in 1987, and Arizona enacted its Employment Protection Act in 1986. Of the two, the Montana statute is broader in the scope of its protections for employees.

EXPANSION OF THE PUBLIC POLICY EXCEPTION IN MISSISSIPPI: ARGUMENTS FOR AND AGAINST

Arguments for the continued expansion of the exceptions to the Employment At-Will Doctrine are: 1) Where there is a shift in economic power to the employee, erosion of the at-will doctrine is a natural consequence. 2) Federal statutory inclusion has nullified the rule in many termination cases anyway. 3) The helpless employee must be protected from the all-powerful corporation.

Arguments against expansion to the exceptions of the termination at-will doctrine are: 1) The judiciary would be overwhelmed by law suits. 2) It is well known that Mississippi is in keen competition with other Sunbelt states in the area of economic development. By placing itself outside the mainstream, the erosion of at-will employment could seriously jeopardize Mississippi's competitive position. The thought of a jury playing Monday morning quarterback with termination decisions is not an appealing prospect to most employers. 3) While the public policy exceptions may be the least controversial incursions against at-will employment, problems with these exceptions abound. The term "public policy" evades precise and uniform definition. Can exception be declared by legislative action only? Or can it emulate from judicial and other sources?

WHAT MISSISSIPPI EMPLOYERS CAN DO TO MINIMIZE LIABILITY: CAVEATS FOR MANAGEMENT

1) *Document, document, document.* Keep good notes of counseling sessions with employees. Most potential or actual jurors interviewed believe that an employee is entitled to written warnings prior to termination. As a result, an employer who fails to document, in writing, performance issues will have uphill battle in preventing a trial.

2) *Recruiting*: Employers are carefully avoiding any suggestion that the prospective employee has a job for life or that an employment contract exists. Terms such as "permanent employee," "career" and "tenure" should be purged from job information and help-wanted advertisements.

3) *Interviewing*: Personnel interviewers and other company officials are making fewer promises during employment interviews, particularly since the successful appeal by Christine Craft, the former TV anchor-woman who claimed she was hired under false pretenses. Employers have become more specific about job duties and responsibilities that they expect the employee to perform. For example, job descriptions, often used to acquaint new or prospective employees with their jobs, now include more detail and clarity about the duties and responsibilities of the job.

4) *Employee Handbook*: Some companies have dropped references to the term "probationary period" (sometimes substituting the term "trial period") and "permanent employee" from their handbooks to avoid the impression that those who successfully, complete their probation have been granted a life-time job. Other employers have deleted statements which limit their right to dismiss employees, some have included "at-will" statements which broaden their right to dismiss employees who are considered unsatisfactory performers. The following is a sample disclaimer, which must be clear and unambiguous in the handbook or policy in order to be effective: "This policy is not intended as a contractual obligation of the company. The company reserves the right to amend this policy from time to time at its discretion and in accordance with applicable law."

5) *Performance Evaluation*: More and more, the courts are now holding employers responsible for fair and valid employee performance evaluations. As a result, companies are pressing their managers to be honest and candid and to follow a formal, progressive disciplinary procedure when unsatisfactory performance results. Before dismissing an employee, companies are now making sure that he or she has been warned, notified, and that complete, written documentation has been noted in the employee's personnel file. If an employer conducts employee evaluations in conjunction with wage increases and do not monitor the evaluations for objective accuracy, it is likely to find that the worse employee in the entire workforce is rated "above average." There are several reasons for this result. A supervisor may want to "help" an efficient employee by giving him another chance. A supervisor may try to establish a personal relationship with an uncooperative employee by doing an unmerited favor. Or a supervisor simply may want to avoid the unpleasantness of communicating a negative evaluation. The effect on the employer's defense, however, is the same. The employer is forced to explain, in effect, that it lied in rating the deficient employee "above average," but is not lying to the jury about the deficiency which required the employee's discharge.

6) *Grievance Procedures*: Traditionally, union employees have been able to air their grievances against management through a formal, step-by-step grievance procedure which often ended in binding arbitration. In the past, many organizations afforded no such protection for the non-union employee. However, as a result of the increasing rights of terminated employees, employers are creating and implementing formal, internal grievance procedures in order to handle employee complaints efficiently and fairly. Employers expect that these procedures will enable supervisors and employees to solve their problems before termination is considered. An employer should consider establishing and respecting a system through which an employee may (and perhaps must) present his side of the story. This will help an

employer identify his mistakes before they reach a jury, unless in the likelihood the employee will sue simply to get even, and may provide a legal defense to some claims.

7) *It is best not to have any type of formal procedure for termination*. But if you do have a procedure, you need to be sure that the procedure is followed when someone is terminated.

8) If an employee is terminated because the employee did or did not do something that you allow other employees to do or not do, your reasons for termination will not "play well" with a jury. The terminated employee will bring in other people who will testify that you have allowed other employees in similar situations to get by with the very thing that you have terminated the plaintiff for.

9) Try to set the best possible stage for the termination conference. Schedule and locate the meeting at a place to minimize the embarrassment to the employee. Be prepared to answer any questions concerning any post-termination benefits that the employee may have.

10) Limit the negative information about the employee to as few people as possible and only to those people who have a "need to know."

11) Look at the situation from the standpoint of how the company's handling of a particular case will look to a judge or to a jury. Keep in mind that the steps that you take in the termination process will be scrutinized very closely by the court, and you will want to do everything possible to demonstrate that the employee was treated in a fair and impartial manner.

Unlike other business related litigation, virtually all jurors in the employment related disputes empathize with only one party, the plaintiff. This is so because virtually all jurors are, or have been, employees, or very few, if any, have experience as an employer. Thus, right out of the box, an employer lacks a level-playing field.

One thing should be clear to the emp1oyer: being right is no longer good enough. The employer must be right and be able to explain why it was right to a jury of the former employee's peers. (Right) means more than "not guilty" of the charged offense. It means that the employer treated the employer fairly. For some employers, this may require a fundamental reexamination of their employer relations philosophies. But for many others, it means making the effort to fix common practices which make a justified firing look bad.

The decision to take an adverse personnel decision must be made only alter proper procedures have been followed, proper warnings administered, and full documentation obtained. Once all these elements are in line, it is equally important for the employer to act decisively and promptly - if it is going to act at all, in employment litigation, changing a juror's expectations is a losing battle. Instead, to obtain a favorable verdict, an employer must insure that proper groundwork is laid at the time the adverse personnel decision is made.

SUMMARY

1) The Mississippi Supreme Court has created exceptions to the Employment At-Will Doctrine based upon public policy and based on language in an employer's handbook.

2) Given the exceptions described in *Levens*, *Willard*, and *McArn*, there is a possibility that the Mississippi Supreme Court will further expand the public policy exceptions to include other matters such as a retaliatory discharge for filing a workman's compensation claim or for the reporting of or refusing to commit civil or criminal illegalities. Attorneys for employers will continue to argue strenuously that the exception should be very limited. Attorneys for employees will continue to argue that the public policy exception should be expanded to include filing workman's compensation claims, filing of a sexual harassment claim, or etc.

3) The handbook/contractual exception to the Employment At-Will Doctrine will continue to be very limited given the courts' position on employment at-will disclaimers which are routinely contained in most policy statements and handbooks. An employment at-will disclaimer in a handbook negates any contractual obligation on the part of an employer.

4) The Mississippi Supreme Court, in prior decisions, has discussed the possibility of application of a duty of good faith to employment contracts. The Court is currently split on this question.

5) Although the Employment At-Will Doctrine is still firmly established in Mississippi law, with the exceptions outlined above, Mississippi employers would be wise to approach all terminations very carefully. In this day and age, the decision to take an adverse personnel decision must be made only after proper procedures have been followed, proper warnings administered, and full documentation obtained. Once all these elements are in line, it is equally important for the employer to act decisively and promptly.

ENDNOTES

[1] Jeanne Duquette Gorr, *The Model Employment Termination Act: Fruitful Seed or Noxious Weed?* 31 DUQLR 111 (Fall 1992); *see also* Robert W. Fisher, "When Workers Are Discharged - An Overview," *Monthly Labor Review*, June 1973, pp. 4-17.,

[2] 2 42 U.S.C. § 2000e.

[3] *Monthly Labor Review*, January 2001.

[4] *Monthly Labor Review*, January 2001.

[5] Shane and Rosenthal, *Employment Desk Book,* § 16.03(8) 1999.

[6] Shane and Rosenthal, *Employment Desk Book*, § 16.03(8) 1999. *Id.*

[7] *Coleman v. Mississippi Employment Sec. Comm'n*, 662 So.2d 626, 628 (Miss. 1995). *See Morrison v. Mississippi Enter. For Tech, Inc.*, 798 So.2d 567 (Miss. Ct. App. 2001) cert. Denied October 11, 2001; *Brown v. Inter-City Fed Bank for Sav.*, 738 So.2d 262 (Miss. Ct. App. 1999); *Rosen v. Gulf Shores, Inc.*, 610 So.2d 366 (Miss. 1992); *Perry v. Sears, Roebuck & Co,* 508 So.2d 1086 (Miss. 1987); *HeartSouth, PLLC v. Boyd*, 865 So.2d 1095 (Miss. 2003).

[8] *Cunningham v. 4-D Pool Co.*, 451 N.W. 2d 514 (Mich. Ct. App. 1989).

[9] *Solomon v. Walgreen*, 975 F.2d 1086, 1089 (5th Cir. 1992).

[10] *Brown v. Inter-City Fed Bank for Sav.*, 738 So.2d 262, 264 (Miss. Ct. App. 1999) (*citing Perry v. Sears, Roebuck & Co.*, 508 So.2d 1086, 1088 (Miss. 1987)).

[11] The terminated employee in *Kelly* argued: [t]hat even though Mississippi courts have not yet recognized a case of action for retaliatory discharge, it is likely that they will do so when faced with an appropriate case in light of recent precedents from other jurisdictions finding such a cause of action. *Id.* at 875. The Court flatly rejected this argument, holding: "We decline this invitation to create law for Mississippi given the conflicting nature of existing precedents." *Id.* at 875.

[12] *Shaw*, 481 So 2d at 253-54.

[13] *Shaw*, 481 So.2d at 249.

[14] *Shaw*, 481 So.2d at 254.

[15] *Robinson v. Bd. of Trustees of East Cent. Junior College*, 477 So.2d 1352, 1353 (Miss. 1985).
[16] *Bobbitt v. Orchard, Ltd*, 603 So.2d 356 (Miss. 1992).

[17] *Southwest Mississippi Regional Medical Center v. Lawrence*, 684 So.2d 1257, 1264 (Miss. 1996).

[18] *Hartle v. Packard Electric*, 626 So.2d 106 (Miss. 1993).

[19] *Hartle v. Packard Electric*, 626 So.2d 106, 109 (Miss. 1993) (*citing Perry v. Sears, Roebuck& Co.*, 508 So.2d 1086 (Miss. 1987)).

[20] *McArn v. Allied Bruce-Terminix Co., Inc.*, 626 So.2d 603 (Miss. 1993).

[21] *McArn v. Allied Bruce-Term/nix Co., Inc.*, 626 So.2d 603, 607 (Miss. 1993). *See Hurst v. Forrest Gen. Hosp.*, 762 So.2d 298 (Miss. 2000).

[22] *McArn v. Allied Bruce-Terminix Co., Inc.*, 626 So.2d 603, 607 (Miss. 1993).

[23] *Also see* Marcie M. Fyke, "Wrongful Termination in Mississippi", *The Mississippi Lawyer*, October 2001.

[24] These allegations by Levens seemingly fall comfortably into the first category of wrongful discharge claims described in *Perry*. . . as those "based upon an implied covenant of good faith and fair dealing, [which is] breached by a malicious termination or harassment." *Perry*, 508 So.2d at 1089. (emphasis added). However, the Mississippi Supreme Court has, since Levens, insisted there is still no duty of good faith and fair dealing in at-will employment settings. *See e.g., Cothern v. Vickers*, 759 So.2d 1241 (Miss. 2000) and *Slattery v. North Miss. Contract Procurement, Inc.*, 747 So.2d 257 (Miss. 1999)

[25] *Paracelsus Healthcare Corp. v. Willard*, 754 So.2d 437 (Miss. 1999).

[26] For a good discussion of a new foundation on which employment at-will terminations must be analyzed, *see* Marcie M. Fyke, "Wrongful Termination in Mississippi", *The Mississippi Lawyer*, October 2001.

FEDERAL EXPRESS DRIVERS: EMPLOYEES OR INDEPENDENT CONTRACTORS?

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ABSTRACT

Federal Express Ground has created a business model that has made it highly competitive in the package delivery industry; FedEx hires its drivers as independent contractors. This business model is not unique. In many industries workers are customarily hired as independent contractors to avoid the liability and expense associated with an employer/employee relationship. While potentially profitable, this business model also exposes the hiring party to lawsuits by workers claiming that they are employees rather than independent contractors. Currently Federal Express Ground is facing a wave of such lawsuits. This paper considers the employment status of FedEx drivers by examining the tests used to classify workers as either employees or independent contractors and by comparing FedEx drivers to drivers in the courier service industry who have been found to be employees rather than contractors.

INTRODUCTION

As most employers discover, hiring an employee can be burdensome. The employer becomes responsible for minimum wage and overtime payments, payroll taxes, workers' compensation, medical leave, workplace safety and in some instances, their employee's torts. Many employers try to avoid these burdens by hiring workers or reclassifying current employees as independent contractors, a practice that if done incorrectly can actually compound the employer's problems should a court determine that a worker hired as a contractor is actually an employee.

Such misclassification claims can be brought by a variety of plaintiffs bringing suit under a myriad of legal theories. Plaintiffs can include workers alleging they have been misclassified as independent contractors, injured parties seeking to impute liability to the alleged employer under the doctrine of respondent superior, unions attempting to represent workers, and the federal and state governments seeking employer contributions to worker compensation funds and payment of employment taxes. Such plaintiffs can contest a worker's status under numerous legal theories including common law negligence claims, workers' compensation and unemployment statutes, the Age Discrimination in Employment Act (ADEA), the Americans with Disabilities Act (ADA), the Employee Retirement Income Security Act (ERISA), the National Labor Relations Act (NLRA), the Federal Insurance Contributions Act (FICA), the Family Medical Leave Act (FMLA) and Title VII of the Civil Rights Acts of 1964.

EMPLOYMENT STATUS

Hiring parties can hire a worker in one of two ways, as an employee or as an independent contractor. Should a plaintiff allege that the hiring party has misclassified the worker, courts apply a variety of somewhat similar tests to determine a worker's proper classification. These tests categorize the worker by examining the nature of the employment relationship and as such, the tests are very fact intensive.

For claims based on common law legal theories courts use the "common law test" which the U.S. Supreme Court described in *Nationwide Mutual Insurance Company v. Darden (1992)* as follows:

> In determining whether a hired party is an employee under the general common law of agency, we consider the hiring party's right to control the manner and means by which the product is accomplished. Among the other factors relevant to this inquiry are the skill required; the source of the instrumentalities and tools; the location of the work; the duration of the relationship between the parties; whether the hiring party has the right to assign additional projects to the hired party; the extent of the hired party's discretion over when and how long to work; the method of payment; the hired party's role in hiring and paying assistants; whether the work is part of the regular business of the hiring party; whether the hiring party is in business; the provision of employee benefits; and the tax treatment of the hired party. (p.322)

Under this test no one factor is determinative. The classification must be based on a thorough analysis of all the relevant facts; however, in most cases particular attention is paid to the hiring party's ability to control the worker, whether exercised or not.

Worker classification tests can also consider the purpose promoted by a particular statute, as well as the interests of the class protected by the statute. For claims based on the FLSA, the FDEA, and FICA courts have employed an economic realities test that focuses on the degree of the worker's dependence on the hiring party's business. The test uses six factors to determine if the worker is in business for himself or whether the worker is economically dependent on the hiring party's business for which the worker merely provides a service. The six factors, as stated in *Herman v. Mid-Atlantic Installation Servs., Inc.* (2000), are:

> (1) the degree of control that the putative employer has over the manner in which the work is performed; (2) the worker's opportunities for profit or loss dependent on his managerial skill; (3) the worker's investment in equipment or material, or his employment of other workers; (4) the degree of skill required for the work; (5) the permanence of the working relationship; and (6) the degree to which the services rendered are an integral part of the putative employer's business. (p. 671)

In other instances states apply more inclusive tests based on statutory definitions that consider the "purpose of the protective legislation" (*JKH v. Dept. of Indus. Relations*, 2006) to determine a worker's status. For example, in *Boston B.C. v. D.D., Div. Emp*. (2002) the court considered whether a hiring party was required to make contributions to the state's unemployment fund for workers that had been hired as independent contractors. The provisions of the applicable statute specifically rejected the common law standard for determining employment status and set forth a more inclusive three part "ABC" test. The court in *Boston B.C. v. D.D., Div. Emp*. (2002) held that the test required that the alleged employer establish that the worker:

> (a) is free from direction and control by the employing unit; (b) performs services outside the usual course of, or places of business of, the employing unit; and (c) the worker — albeit performing services of the same nature as the employing unit — is engaged in an independently established trade, occupation, profession or business wholly apart from the employing unit. (p. 477)

FEDERAL EXPRESS DRIVERS

Federal Express (FedEx) has created a smart business model for its FedEx Ground division that enables it to be highly competitive in the package delivery industry; FedEx hires its drivers as independent contractors. FedEx's 14,000 drivers receive rights to FedEx routes, drive their own vehicles, are responsible for their own expenses and, according to FedEx, operate as self-employed businesspeople. This business model has been very successful for FedEx. Since acquiring Roadway Package Systems and renaming it FedEx Ground in 2000, sales have increased to $4.7 annually creating profits of $1.4 billion in fiscal 2005. (MacDonald, 2005)

While this business model has been profitable, attorneys for FedEx drivers have filed numerous lawsuits asserting that FedEx improperly hires drivers as independent contractors while treating them as employees. These cases have been brought by individuals and as class actions, and claim relief under various federal and state statutes. In August of 2005 the cases were consolidated into *In Re FedEx Ground Package System, Inc, Employment Practices Litigation* by the Judicial Panel on Multidistrict Litigation and assigned to the U.S District Court in the Northern District of Indiana where pretrial proceedings are currently being resolved.

Whenever a court is asked to determine whether or not a worker is an independent contractor or an employee, the court's examination is quite fact-intensive. And in the FedEx cases, because of the business model employed by FedEx, the factual issues are substantially similar. All drivers conduct their responsibilities according to a standard operating agreement which serves as the basis for their employment relationship with FedEx.

THE OPERATING AGREEMENT

Prior to entering into an operating agreement with a driver, FedEx recruits and trains interested candidates. FedEx advertises that is seeking individuals who want to run their own businesses and who have "entrepreneurial spirit". (FedEx Home Delivery, 2006) Individuals who respond to the ads attend informational meetings that emphasize the independent contractor status of FedEx drivers. If FedEx is satisfied with the candidate's screening, he or she is then required to complete a FedEx Home driver training course, which instructs them on how FedEx wants drivers to make their deliveries. (FedEx Home Delivery, 2006)

Candidates who pass the training course are eligible to receive a route and enter into a Contractor Operating Agreement. The same contract is offered to all potential drivers and it is essentially at "take it or leave it" proposition. The agreement specifically classifies the driver as an independent contractor and states that the driver is not a FedEx employee. (FedEx Home Delivery, 2006)

Under the agreement the drivers are required to purchase or lease a white vehicle approved by FedEx that has a painted FedEx logo or displays a removable magnetic logo. While on their routes, drivers must use the vehicles exclusively for the delivery of FedEx packages, but when drivers are not using the vehicle for FedEx deliveries, it may be used for personal and other commercial uses so long as the FedEx logo has been removed. The drivers are responsible for all the costs associated with the vehicle's operation and maintenance. (FedEx Home Delivery, 2006)

In addition to acquiring a vehicle, the agreement requires the drivers to purchase and wear FedEx uniforms, and to maintain certain standards of personal appearance. While making deliveries, drivers must wear a FedEx identification badge that includes the driver's photograph and the title "contractor". The agreement also requires the drivers maintain their vehicles in a clean, and dent-free condition, without extraneous markings. To ensure vehicle complies with FedEx safety and appearance standards, drivers are required to submit a monthly maintenance form along with receipts for any repair and maintenance. (FedEx Home Delivery, 2006)

The agreement specifically states that FedEx does not control how the driver carries out the responsibilities agreed to under the contract; although, it does require the driver to provide the agreed upon daily delivery services in a manner that identifies the driver as part of the FedEx system. Deliveries must be made Tuesday through Saturday; however, drivers can choose the hours they work, and take breaks and run personal errands at their discretion. The drivers are not required to log their hours; however, FedEx does require them to scan their FedEx badges when they leave the FedEx terminal to make deliveries and after they complete their deliveries in order to track their delivery hours. (FedEx Home Delivery, 2006)

Drivers are compensated weekly according formula that, among other things, takes into account the number of stops made by the driver as well as the number of packages delivered by the driver. Drivers also receive a per-package payment for sorting and loading the packages they are to delivery, and can receive additional bonuses for meeting FedEx performance and service standards. Finally the agreement entitles the driver to receive a van/vehicle availability fee for every day that the driver makes his or her van available to provide services to FedEx. (FedEx Home Delivery, 2006)

Should the driver fail to comply with the terms of the operating agreement, a FedEx manager meets with the driver to try to resolve the issue. If the manager is unable to resolve the issue, FedEx can, under the terms of the agreement, terminate the relationship. The agreement also allows the driver to terminate the relationship if he or she provides 30 days written notice. (FedEx Home Delivery, 2006)

ANALYSIS

The courier industry is very analogous to FedEx's delivery business and many courier services hire couriers using a business model similar to FedEx's. While the exact details will vary from business to business, in most instances couriers are hired as independent contractors and are required to provide their own vehicle or in some cases, bicycle. The couriers use their vehicles to pick up and deliver packages for the customers of the courier service and are generally paid on a per-delivery basis. Because of the similarities between FedEx's delivery business and the courier industry, the case law from alleged courier misclassifications should shed some light on the strength of FedEx's assertion that its drivers are truly independent contractors.

Under any of the worker classification tests, courts consider the extent to which the hiring party controls how the worker performs his or her services a significant factor in determining the worker's classification. In *Stover Delivery v. Div. Employ* the court found sufficient control in the fact that Stover's couriers received a policies and procedures handbook that they were expected to comply with and that they could be disciplined for violating. In addition, drivers were required to carry a Stover beeper so that a Stover dispatcher could tell them of necessary route deviations (*Stover Delivery v. Div. Employ,* 1999). The element of control was also established in *JKH v. Dept. of Indus. Relations* where the court held that "by obtaining the clients in need of the service and providing the workers to conduct it, JKH retained all the necessary control over the operation as a whole." (*JKH v. Dept. of Indus. Relations,* 2006) Finally, in *AFM Messenger Service v. Dept. Employ. Security* the court found evidence of the requisite control in a number of facts. "AFM procured the customers; AFM set the delivery rates; AFM provided the delivery tickets to the customers; AFM made the delivery assignment; AFM billed the customers: AFM set the commission; AFM paid the drivers. AFM also retained the right, under the parties' written agreement which AFM provided, to terminate their relationship at any time." (*AFM Messenger Service v. Dept. Employ. Security,* 2001, p. 402)

Given FedEx's business model it is likely that the requisite control could be established. FedEx's operating agreements structures the employment relationship in such detail that it operates as a de facto policy and procedures handbook. The agreement requires drivers to purchase a FedEx approved vehicle, wear a FedEx uniform and FedEx I.D. badge, carry and use a FedEx beeper and comply with FedEx guidelines for safe driving. Drivers are even required to keep their vehicles in a clean and presentable manner. (FedEx Home Delivery, 2006)

On the other hand, FedEx does not require its drivers to follow a schedule. Drivers can decide when they start work and when they stop work; however, they do not have the discretion to skip deliveries on any given day. The FedEx operating agreement requires them to be available to be available for delivers Tuesday through Saturday. Further control is evidenced the fact that FedEx assigns the drivers' routes while retaining the right to unilaterally reconfigure a route. (FedEx Home Delivery, 2006)

The FedEx agreement clearly evidence FedEx's control over how its drivers perform their service. In addition to the extensive and detailed rules and policies in the agreement, control is evidenced in the actual working relationship between FedEx and its drivers. If a driver's service fails to meet the standards set by FedEx, FedEx managers hold a "business discussion" with the driver to try to remedy the problem. If the problem cannot be resolved, FedEx retains the right to terminate the relationship with 30 days notice. (FedEx Home Delivery, 2006)

Another common factor considered in the courier cases was the whether the service provided by the worker was an integral part of the hiring party's business or was it "outside the usual course of the business for which such service is provided" (*AFM Messenger Service v. Dept. Employ. Security*, 2001, p. 398). In each courier case, and also in FedEx's business, drivers pick up and deliver packages. Given the nature of a courier service's business, it is not surprising that in all three courier cases the courts found that the driver's service was part of the hiring party's courier business. In fact, in *JKH Enterprises* the court found the service "functions as the integral heart of" (p. 1065) the courier business. The court in *Stover* reached a similar conclusion and stated that a courier service's success "depends almost entirely upon the drivers' performance of their duties" (p. 693). The same can certainly be said of FedEx's dependence on its drivers.

The courts in the courier cases also considered whether the service provided by the drivers constituted an independently established business. The court in *Stover* determined this by examining whether the drivers were working for more than one firm at a time and whether they made their services available to the generally public. It concluded that while the drivers were free to work for other firms and to offer their services to the general public, none of them did nor could they reasonably do so given the number of hours they worked for Stover. Similarly the court in *AFM Messenger* concluded that the drivers were dependent on their relationship with AFM and as such "a drivers 'business' was not established "independently' of" the courier service. (p. 402)

Applying these considerations to the relationship FedEx drivers have with FedEx, it is pretty clear that they do not operate independent businesses. While FedEx drivers do own their vehicles and arguably could perform services for another delivery service, realistically their "businesses" could not exist apart from FedEx. As noted by the court in *AFM Messenger* the appropriate question is "whether the driver could have performed the same services independent of a relationship with UDS or another such messenger service" (p. 408). If that standard is applied, FedEx drivers do not operate independent businesses. Should FedEx terminate its relationship with a driver, that driver is essentially unemployed.

Another factor considered in the courier cases was whether the parties maintained a continuous relationship. A continuing relationship is considered evidence of an employer/employee relationship, while temporary or short term relationships generally indicate that a worker has been hired as an independent contractor. FedEx's relationship with a driver is not of a temporary nature. Drivers must complete a training course and are required to purchase a FedEx approved vehicles. This investment of time and money realistically precludes a driver from ending his or her relationship with FedEx precipitously. Both FedEx and the FedEx drivers anticipate an ongoing relationship. After the initial term of the relationship, the operating agreement automatically renews for successive one year terms. (FedEx Home Delivery, 2006)

A final factor almost always considered in classifying a worker is whether the worker's compensation is dependent on his own skill and initiative. The court in *Stover* considered the degree to which the driver's profits or losses were dependent on the driver's skill or efforts. In that case the court rejected the Stover's assertion that its drivers could make more money through their own effort and initiative. The court noted that the drivers were paid according to their routes and not according to the number of deliveries they made. (*Stover Delivery v. Div. Employ, 2006, p. 695)*

FedEx drivers on the other hand do receive a fee for each delivery they make and thus are able to earn more money if they make more deliveries. However, the number of deliveries a driver makes each day is limited by the number of deliveries required by FedEx and as such, a driver can not increase his or her profits by simply working harder or faster.

CONCLUSION

While profitable, the FedEx business model of hiring its drivers as independent contractors is unlikely to survive judicial scrutiny. Regardless of which legal theory a plaintiff might use to challenge the classification or which test a court might apply to review the classification, FedEx drivers will almost certainly be found to be employees rather than contractors. The FedEx operating agreement, which all drivers must commit to, extends FedEx's control over how the drivers perform their service, and the service drivers provide, delivering packages, is an integral part of FedEx's business. In addition, the FedEx compensation formula does not allow drivers to increase their income through their own skill or efforts. Finally the employment relationship between FedEx and its drivers is not temporary in nature. Both parties expect, and it is in both parties' interest, that they create and maintain an ongoing relationship. Based on these facts FedEx drivers should be found to be employees and as such, entitled to all the benefits associated with an employer/employee relationship.

REFERENCES

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FOREIGN FLAGGED CRUISE SHIPS AND THE AMERICANS WITH DISABILITIES ACT

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ABSTRACT

The Americans with Disabilities Act of 1990 (ADA) is applicable to businesses in the United States, and, generally, not applicable to businesses outside of the country. But is the ADA applicable to foreign flagged cruise ships docked at U.S. ports? While general statutes, such as the ADA, are presumed to apply to conduct that takes place aboard a foreign-flag vessel in United States territory if the interests of the United States or its citizens are at stake, if instead interests internal to the ship are at stake, then the "clear statement rule" requires Congress to clearly state that the law is to be applied in such a manner. Absent a clear statement by Congress, a law cannot be applied if it would affect the internal operations of the business, such as those relating to matters of internal order and discipline. In Spector v. Norwegian Cruise Line, LTD the Supreme Court held that Title III of the ADA may apply to foreign flagged cruise ships departing from, and returning to, ports in the United States. The plurality opinion concluded that the ADA lacks a sufficiently clear statement that it applies to the internal affairs of foreign vessels, at least insofar as it could be read to require structural changes that might conflict with international legal obligations or pose a real threat to the safety of the crew or other passengers. However, the plurality determined that the clear statement rule does not render Title III entirely inapplicable to foreign vessels, concluding instead that the statute applies to foreign ships to the extent to which it does not bear on their internal affairs. This paper will discuss the ADA and the cruise industry, and the likely effects of this decision.

INTRODUCTION

Cruising is an extremely popular vacation option today, and represents the fastest growing sector of the travel industry with eleven million passengers cruising each year (Mitchell, 2006). Since 1970 the cruise industry has experienced a phenomenal 1,800 percent growth in the number of passengers cruising annually (Sheehan, 2006). To accommodate that volume of travelers, ships became mega vessels during the 1990s, with Carnival's Destiny being the first passenger ship to break the 100,000 ton barrier (Marsano, 1999). Royal Caribbean's Eagle Project launched three ships during that decade, each of which weigh 142,000 gross registered tons, cost $500 million, accommodate as many as 3,838 passengers, and provide an amazing array of activities, such as an ice skating rink, golf course, regulation size basketball and volleyball courts, a twenty foot high rock-climbing wall and an in-line skating track (Snow, 1999). Carnival Corporation, of which the Cunard Lines is a subsidiary, launched the Queen Mary in 2003 (151,400 gross tons), intended to be the largest trans-Atlantic liner ever, until trumped by Royal Caribbean's Freedom of the Seas and upcoming Liberty of the Seas (160,000 gross tons). In comparison, the Titanic was only 43,239 gross registered tons! Norwegian Cruise Lines (NCL) recently ordered up to three 150,000-ton, 4,200-passenger vessels, which would be the fourth-largest class of ships in the world, behind QM2, Royal Caribbean's two existing vessels, and the additional 220,000-ton ships Royal Caribbean has on order for 2009 (Hannafin, 2006). Over sixty new ships have entered service in the past five years (Readers' Poll, 2006). Five new ships are scheduled for launch in 2007 alone: Costa's Serena, Royal Caribbean's Liberty of the Seas, Cunard's Queen Victoria, and the Emerald Princess and Royal Princess (Mitchell, 2006).

Cruise ships are almost exclusively foreign flagged. American flagged cruise ships are clearly subject to U.S. laws, such as the Americans with Disabilities Act ("ADA") (Deck v. American Hawaii Cruises, Inc., 1999), as are passenger ships traveling exclusively within internal U.S. navigable waters (Symeonides, 2005). In order to be flagged American, the ship's hull must be built domestically, which in effect acts as a deterrent to U.S. registration (Fields, 1998). In general, shipbuilding costs in the United States are twice those in Europe, and compliance with American regulatory laws is expensive, so very few cruise ships fly the American flag. Another deterrent to being American flagged is the potential tax burden. Cruise lines that are registered as foreign corporations and sail foreign-flagged ship pay no federal income tax. Carnival, a Panamanian corporation with headquarters in Miami, earned $2 billion in profits between 1995 and 1998, yet paid less than one percent in income taxes, while Royal Caribbean Cruises reported $657 million over the same period and did not even include a line for income taxes in its financial statements (Frantz, 1999).

On the other hand, an advantage to being American flagged is that the ship may sail from and among American ports, and then return to an American port without first sailing to a foreign port, such as to Canada in the Alaska market. Federal law prohibits ships not built in the United States from sailing between U.S. ports without first calling on a foreign country before returning to a U.S. port (Carothers, 2004); under the Jones Act, only American owned ships may transport goods and people between American ports. An all-American itinerary, however, is particularly attractive in the Hawaiian cruise market, which is why in 1999 American Classic Voyages announced plans for "Project America," a venture designed to build at least two, possibly three, ships in American shipyards. American Hawaiian Cruises, a subsidiary of American Classic Voyages, which had operated 1950s American-built ocean liners in the Hawaiian Islands, planned to sail the newly ordered ships, until the drop in tourism after 9-11 forced the company into bankruptcy. Subsequently, the Omnibus Appropriations Bill passed by Congress in 2003 contained a provision to return the Project America ships to Hawaii for inter-island cruises under an agreement with Norwegian Cruise Lines. NCL purchased the two unfinished Project America hulls, which were built in Mississippi, and completed construction of the ships in Europe. It launched the *Pride of America* in 2004, the first new ocean-going passenger ship to fly the American flag in nearly fifty years. Then in April 2006, NCL christened the *Pride of Hawaii*, the largest U.S. flagged passenger ship ever built, and at least for now, the fastest ocean liner ever built as well (NCL America, 2006). As part the agreement, they were permitted to re-flag another ship, previously sailing as the Norwegian Sky, as the *Pride of Aloha*, providing that all of the ships operate with American crews and be subject to U.S. taxation, environmental, and labor laws, including minimum-wage laws.

Not only is federal law usually controlling for American flagged ships, but federal, not state, courts exercise jurisdiction over lawsuits involving cruise ships, as well. The Constitution provides that the "judicial power shall extend...to all cases of admiralty and maritime jurisdiction" (U.S. Constitution. art. III, § 2). In 1789 the first Congress, in the Judiciary Act, established the exclusivity of federal maritime jurisdiction but "saved to suitors" common law remedies available in state courts, including rights granted subsequently by statutes that were rooted in common law (Robertson, 1970). Under the "saving to suitors" clause (28 U.S.C. § 1333 (2006)), state courts can hear certain maritime claims, but still generally apply federal admiralty law with respect to the substantive issues of the claim (Kermarec v. Compagnie Generale Transatlantique, 1959). States may enforce their substantive laws only to the extent that the application of state remedies would not interfere with the uniformity of admiralty law in international and interstate relations, or materially prejudice the general features of maritime law (Southern Pacific Co. v. Jensen, 1917). For example, since federal admiralty law may not allow for the recovery of punitive damages, those remedies may not be available, even if permitted under state law (Robertson, 1997). Although contract rights and remedies are usually a matter of state law, the contract of passage, which governs the rights and responsibilities of the parties for any cause of action arising out of the voyage (The Moses Taylor, 1886), is a maritime contract, and as such it is to be governed by federal maritime law (Milanovich v. Costa Crociere, S.p.A., 1992). Maritime law, in essence, is judge-made law with its own precedents, and preempts conflicting state law to the same extent as if it had been codified by an act of Congress (Robertson, 1970). This general federal maritime law, in addition statutes passed by Congress, comprises the law of admiralty.

But while American flagged ships and ships on U.S. navigable waters are subject to U.S. law, are foreign flagged ships subject to the same? In the Wildenhus's Case (1887) the Supreme Court stated that even though a seagoing vessel "subjects itself to the law of the place to which it goes," pursuant to generally understood principles of comity among nations "all matters of discipline and all things done on board which affected only the vessel or those belonging to her, and did not involve the peace or dignity of the country, or the tranquillity of the port, should be left by the local government to be dealt with by the authorities of the nation to which the vessel belonged as the laws of that nation or the interests of its commerce should require." In other words, foreign flagged ships are generally subject to American law when in port or territorial waters in so far the welfare of U.S. citizens are implicated, but internal matters are usually governed by the law of the flagged ship, absent a contrary intention by the legislature. Congress, however, may regulate such internal affairs if it clearly states its intent to apply its legislation to foreign ships. For example, the Seamen's Act of 1915, permitted foreign seamen on foreign vessels, as well as American seamen on such vessels, to demand up to half the wages earned at each port at which cargo was loaded or unloaded, notwithstanding stipulations in the employment contract to the contrary. The Supreme Court held that it was Congress's intention, as well as within its authority, to condition the right of foreign vessels to enter and use the ports of the United States upon compliance with the statute (Strathearn Steamship Co. v. Dillon, 1920). Therefore, although Congress has the power to regulate foreign ships in U.S. ports and territorial waters, courts usually defer to the law of the flag, and presume that Congress does not intend to exercise that power, unless there is a clear statement of its intention to do so (Robertson & Sturley, 2006).

In addition to the potential application of federal law, passenger vessels are also subject to both domestic and international regulations. The Coast Guard and National Transportation Safety Board have regulatory jurisdiction in territorial waters. Further, the U.S. Centers for Disease Control and Prevention (CDC), under its Vessel Sanitation Program begun in 1970, bi-annually inspects vessels with a foreign itinerary that carry thirteen or more passengers and call on U.S. ports. CDC then issues a report assigning a numerical sanitation score to each ship; additionally, CDC assists the cruise industry with developing and implementing comprehensive sanitation programs (Centers for Disease Control, 2006). Nevertheless, many regulations of the cruise industry, including those relating to passenger safety and welfare, are international in nature. The United Nations' International Maritime Organization ("IMO") is the primary regulatory body responsible for establishing international standards for cruise ship safety, design and construction, and leaves enforcement of its safety standards to member countries. For example, the IMO established new regulations in 1992 which mandated the installation of sprinkler and smoke detection systems in cabins and public areas, the placement of emergency lighting for escape routes, the enclosing of stairways, and the replacement of combustible materials such as wood. The international convention which administers the new standards, Safety For Life At Sea ("SOLAS") provides that phased implementation of the new regulations should begin in 1994 and be completed by 2010 (Yenckell, 1997). The IMO also worked with the International Council of Cruise Lines ("ICCL"), an association of the sixteen largest passenger cruise lines, to prepare passenger vessel guidelines that address design and operation features for the accommodation of persons with disabilities (Cruise Ship Accessibility for Persons with Disabilities, 2006). While such recommendations guide the development of national regulations and requirements, they are not usually binding on contracting states, nor do the accessibility recommendations by the IMO have the force of treaty provisions.

THE AMERICANS WITH DISABILITIES ACT

The Americans with Disabilities Act (ADA) was passed by Congress in 1990 in an effort to eliminate discrimination in employment opportunities, the provision of public services and places of public accommodation, as well as in the provision of telecommunication services. Title III of the Americans with Disabilities Act of 1990 (ADA), which concerns places of public accommodation, provides that "no individual shall be discriminated against on the basis of disability in the full and equal enjoyment of ... any place of public accommodation by any person who owns, leases (or leases to), or operates a place of public accommodation" (42 U.S.C. 12182(a) (2006)). Illegal discrimination includes 1) denying disabled individuals the opportunity to participate in or benefit from the goods, services, facilities, privileges, advantages, or accommodations of an entity; 2) affording disabled individuals the opportunity to participate in or benefit from a good, service, facility, privilege, advantage, or accommodation that is not equal to that afforded to other individuals; 3) providing a good, service, facility, privilege, advantage, or accommodation that is different or separate from that provided to other individuals, unless such action is necessary to provide a good, service, facility, privilege, advantage, or accommodation, or other opportunity that is as effective as that provided to others. (42 U.S.C §12182(b)(1)(A) (2006)). The phrase "public accommodation" is defined in terms of twelve extensive categories, which include, for example, places of lodging, establishments serving food or drink, places of exhibition or entertainment, places of public gathering, sales or rental establishments, service establishments, stations used for public transportation, places of public display, places of exercise or recreation, places of education, and social service centers (42 U.S.C. § 12181(7) (2006)).

The Act also prohibits discrimination in "specified public transportation" services, defined as "transportation by bus, rail, or any other conveyance (other than by aircraft) that provides the general public with general or special service (including charter service) on a regular and continuing basis" (42 U.S.C §§ 12184(a) & 12181(10) (2006)). Both provisions require covered entities that provide public accommodations and public transportation to make "reasonable modifications in policies, practices, or procedures" to accommodate disabled individuals (42 U.S.C §§ 12182(b)(2)(A)(ii), 12184(b)(2)(A) (2006)), and require the removal of "architectural barriers, and communication barriers that are structural in nature" where such removal is "readily achievable," defined as being "easily accomplishable and able to be carried out without much difficulty or expense" (42 U.S.C §§ 12181(9), 12182(b)(2)(A)(iv) & 12184(b)(2)(C) (2006)). Title III further requires that any determination with respect to "readily achievable" account for the impact of the removal of the barrier upon the overall operation of the facility (42 U.S.C. § 12181(9) (2006)).

Generally, entities that provide public accommodations or public transportation 1) may not impose "eligibility criteria" that tend to screen out disabled individuals, 2) must make "reasonable modifications in polices, practices, or procedures, when such modifications are necessary" to provide disabled individuals full and equal enjoyment, 3) must provide auxiliary aids and services to disabled individuals, and 4) must remove architectural and structural barriers, or if barrier removal is not readily achievable, must ensure equal access for the disabled through alternative methods (42 U.S.C §§ 12182(b) & 12184 (2006)). However, eligibility criteria that screen out disabled individuals are permitted when necessary for the provision of the services or facilities being offered (42 U.S.C §§ 12182(b)(2)(A)(i), 12184(b)(1) (2006). Moreover, policies, practices, and procedures need not be modified, and auxiliary aids need not be provided, if doing so would "fundamentally alter" the services or accommodations being offered (42 U.S.C §§ 12182(b)(2)(A)(ii)-(iii) (2006)). Furthermore, auxiliary aids are not mandated if they would result in an “undue burden," nor is any accommodation required if, as a result, disabled individuals would pose "a significant risk to the health or safety of others that cannot be eliminated by a modification of policies, practices, or procedures or by the provision of auxiliary aids or services" (42 U.S.C §§ 12182(b)(2)(A)(iii) & 12182(b)(3) (2006)).

It clearly was the policy choice of Congress to require places of public accommodation and transportation providers doing business in the United States not only to cease discriminating against disabled person in the provisions of their services, but also to make an accommodation in some circumstances. This policy choice necessarily implicates an economic allocation of cost to businesses. However commendable and reasonable that decision, it may not be the policy choice of other nations. Notwithstanding that consideration, did Congress intend for the ADA to apply to foreign flagged ships in U.S. ports or territorial waters? That issue was addressed by the Supreme Court last term. The case raised broad questions about the potential reach of U.S. law, “an issue of increasing practical and symbolic importance these days” and whether, as characterized by Justices Ginsburg and Souter respectively during oral argument, the question should be framed in terms of "[T]he U.S. rules the world. No matter what the other ports say, U.S. law is going to govern," or alternatively "U.S. law rules the world unless the world doesn't want to use the U.S. as a port of call" (Kaufman, 831, 2006).

SPECTOR V. NCL

Norwegian Cruise Line (“NCL”) is incorporated in Bermuda, but has its principal place of business in Miami. NCL ships “are essentially floating resorts” that “depart from, and return to, ports in the United States” (Spector v. Norwegian Cruise Line, LTD, 126, 2005). Most passengers are residents of the United States, and pursuant to terms of the contract of passage, disputes between the cruise line and its passengers are subject to the laws of the United States, even though almost all of NCL’s vessels sail under foreign flags. Plaintiffs in the lawsuit were disabled passengers, who alleged violations of the ADA in that, unlike other travelers, they 1) were required to pay higher fares and special surcharges, 2) were required to waive any potential medical liability and travel with a companion, and 3) were subject to NCL’s right to remove a disabled passenger from the ship whose presence posed a danger to the comfort of another passenger. They further alleged that NCL violated the ADA by maintaining evacuation programs and equipment in locations that were not accessible by disabled passengers, and asserted that in general, NCL did not do enough to ensure that disabled passengers had the full enjoyment of the services offered by the cruise line (Spector v. Norwegian Cruise Line, LTD, 2005). The district court held that Title III of the ADA applied to foreign flagged vessels and that the plaintiff's companions associational discrimination claim were valid, but dismissed the claim that the physical barriers needed to be removed because the agencies charged with promulgating architectural and structural guidelines for the ADA had not promulgated such regulations for cruise ships (Spector v. Norwegian Cruise Line, LTD, 2005).

The Court of Appeals for the Fifth Circuit sustained the district court's dismissal of the petitioners' barrier-removal claims on the alternative ground that Title III does not contain a specific provision mandating its application to foreign-flag vessels, and reversed the district court on the remaining Title III claims (Spector v. Norwegian Cruise Line, LTD, 2004). The Fifth Circuit reasoned that, while it is settled law that a ship which voluntarily enters the territorial waters of the United States is subject to its jurisdiction, there is no obligation to exercise that jurisdictional authority. Given that the exercise of jurisdiction is not mandatory, the application of American law to the foreign flagged vessel requires that the law to be applied contain a clearly expressed affirmative intention by Congress (clear statement) to do so. The appeals court reviewed Supreme Court precedent, which concluded that labor and wage laws do not apply to foreign vessels that are temporarily in port and manned entirely by foreign seaman. It further determined that nothing in the statutory text of Title III of the ADA or its legislative history indicated a contrary intent in this case, because Congress did not address the problems of the conflict of foreign laws. The court further opined that Title III barrier removal provisions must be narrowly drawn to avoid conflicts with international rules and conventions governing sea vessels, since those provisions "may govern the finest details of maritime architecture in the quest to render the ships fully accessible to disabled passenger" (Spector v. Norwegian Cruise Line, LTD, 647, 2004). As such, those changes in maritime architecture would be permanent, thus allowing Title III to apply beyond the territorial waters of the U.S.A. and representing possible conflicts with transnational or international law (Spector v. Norwegian Cruise Line, LTD, 2004). In contrast, the Eleventh Circuit, which encompasses Florida's ports, had held that the ADA applied to foreign flagged vessels in U.S ports and territorial waters (Stevens v. Premier Cruises, Inc., 2000). The Supreme Court granted certiorari to resolve the split of authority.

In reversing the Fifth Circuit the Supreme Court held that, while the ADA does not include a specific provision mandating its application to foreign flagged cruise ships in U.S. waters, and while its definitions of "public accommodation" and "specified public transportation" did not mention cruise ships in particularly, "there can be no serious doubt that the NCL cruise ships in question fall within both definitions under conventional principles of interpretation" (Spector v. Norwegian Cruise Line, LTD, 129, 2005). "Cruise ships flying foreign flags of convenience offer public accommodations and transportation services to over 7 million United States residents annually, departing from and returning to ports located in the United States. Large numbers of disabled individuals, many of whom have mobility impairments that make other kinds of vacation travel difficult, take advantage of these cruises or would like to do so. To hold there is no Title III protection for disabled persons who seek to use the amenities of foreign cruise ships would be a harsh and unexpected interpretation of a statute designed to provide broad protection for the disabled" (Spector v. Norwegian Cruise Line, LTD, 132, 2005).

The Court surmised that while a clear statement must be made by Congress as to its intentions in its passage of legislation before the requirements of the statute can interfere with the internal operations of a foreign flagged vessel, "general statutes are presumed to apply to conduct that takes place aboard a foreign-flag vessel in United States territory if the interests of the United States or its citizens, rather than interests internal to the ship, are at stake" (Spector v. Norwegian Cruise Line, LTD, 130, 2005). For example, the National Prohibition Act, which prohibited the sale or consumption of alcohol, was applicable to foreign flagged vessels in the territorial waters of the United States because was no provision in the Act making it inapplicable to such vessels, and the prohibition affected the welfare of American citizens (Cunard S.S. Co. v. Mellon, 1923). The narrow exception of the clear statement rule to the general applicability of U.S. statutory law to foreign flagged vessels in its territorial waters applies only to matters involving "the internal order and discipline of the vessel, rather than the peace of the port" (Spector v. Norwegian Cruise Line, LTD, 130, 2005). The Court deduced that sound principles of statutory construction support both the presumption of not interfering with matters that primarily concern issues to which foreign law applies, as well as the presumption that statutes are intended to apply to all entities, foreign or domestic, that affect U.S. citizens or the peace and tranquility within the jurisdiction of the United States. Thus, only if the duties and requirements of Title III of the ADA interfere with the internal operations of a foreign flagged vessel, will the absence of a clear statement by Congress intending that effect preclude requiring compliance those statutory obligations.

The Court admitted that there is no precise definition of what constitutes internal affairs, but admonished that precision was not necessary: "It suffices to observe that the guiding principles in determining whether the clear statement rule is triggered are the desire for international comity and the presumed lack of interest by the territorial sovereign in matters that bear no substantial relation to the peace and tranquility of the port" (Spector v. Norwegian Cruise Line, LTD, 133, 2005). The Court acknowledged that if the predominant effect of the statutory requirement is on the internal affairs of the vessel, even though the welfare of U.S. citizens are also served, the clear statement rule's deference is triggered. It presumed that the alleged ADA violations regarding physical barriers presented by the structure of the vessel would likely interfere with the vessels internal operations because they could require physical alteration of a ship's design which would be permanent and, in some cases, substantial. In contrast, discriminatory pricing policies and mandatory waivers of liability have nothing to do with a ship's internal affairs.

The Court also hypothesized that the express limitations contained in the statutory provisions of the ADA may make resort to the clear statement rule unnecessary. Since Title III requires barrier removal only if it is "readily achievable," a barrier removal requirement “that would bring a vessel into noncompliance with the International Convention for the Safety of Life at Sea or any other international legal obligation, would create serious difficulties for the vessel and would have a substantial impact on its operation, and thus would not be ‘readily achievable,’" under proper construction of the ADA, without resort to a consideration of the internal operations of the ship (Spector v. Norwegian Cruise Line, LTD, 135-36, 2005). Further, the Court noted that, while the determination of whether or not a barrier modification is readily achievable under Title III should consider the effect of the modification on shipboard safety, Title III by its own language provides that its nondiscrimination and accommodation requirements are not applicable if to comply would pose a significant health or safety risk to others. The court observed that obviously Congress would not have intended to bring a vessel into compliance with the ADA only to cause it to cease its overall operations, nor it would have intended that compliance with a statute, which was designed to accommodate disabled citizens, should result in posing a significant risk to the safety or health of everyone else.

In sum, the Court concluded that Title III of the ADA applies to foreign flagged vessels which are in the territorial waters of the United States “to the same extent that it is applicable to American ships in those waters,” except where it would interfere with the internal operations of the vessel” (Spector v. Norwegian Cruise Line, LTD, 142, 2005). In remanding the case for an application-by-application approach, the court directed that if the lower court finds that Title III’s requirements would interfere with the ship’s internal affairs, for example in affecting a ship’s safety requirements or conflicting with its international obligations, then the clear statement rule must be given effect, and as a result, may preclude structural modification requirements, even those that would be readily achievable. Justice Ginsburg in her concurring opinion asserted that Title III should not be hemmed in where there is only interference with internal operations, and no potential for international discord.

The dissenting justices argued that Title III did not apply to any vessel which would require modifications of the vessel’s structure, whether or not they affected the internal operations of the ship or were readily achievable. The dissent concluded that, because there is no clear statement by Congress that Title III of the ADA should apply to foreign flagged vessels, the presumption is that it does not apply. The justices further contended that any requirement to remove barriers would affect the internal affairs of a vessel, because removing barriers necessarily requires the alteration of the structure of that vessel permanently, continuing to affect the vessel, its crew and its owners beyond the territorial jurisdiction of United States. They also maintained that Title III either applies to foreign flagged vessels or does not, and cannot be interpreted as having prescriptions, some of which apply to the internal affairs of the ship and others which do not, “any more than it is in our power to prescribe that the statute applies to foreign-flag cruise ships 60% of whose passengers are

United States citizens and does not apply to other foreign-flag ships" (Spector v. Norwegian Cruise Line, LTD, 156, 2005). In defending their position, the justices also noted that, while Congress clearly intended the ADA to apply to hotels and other public accommodations, it failed to mention ships of any kind.

RAMIFICATIONS AND POLICY CONSIDERATIONS

The plurality decision in *Spector* suggests cruise ships are subject to Title III of the ADA unless the requirements would affect their internal affairs. The Court recognized that a readily achievable removal of a barrier on a foreign flagged vessel is not required if complying would interfere with internal operations, such as by posing a significant risk to the safety or health of others on the vessel, or rendering the vessel to be out of compliance with some international convention or law necessary for it to operate outside U.S. territorial waters. The parameters articulated in this case for the application of the ADA to the non-internal affairs of ships, however, have not yet been applied by lower courts. In future cases the parameters of those internal affairs will need to be defined because even if minor requirements are to be imposed by Congress on ships of another nation, the clarity of these requirements is imperative (DiPolito, 2006).

However, with respect to the most significant issue, that is, the barrier-removal question, the Court effectively ruled that Title III does not require the owner of a foreign cruise ship to make permanent and significant structural modifications to the ship (Robertson & Sturley, 2006). Thus, the industry will not have to retrofit their ships to comply with Title III of the ADA; instead, temporary ramps and accessible bathrooms could become necessary staples for the industry (Sheehan, 2006). The opinion does leave open several questions regarding the harmonization of international obligations with Title III of the ADA. For example, given that the U.S. was a signatory to the treaty at issue in *Spector*, that is SOLAS, would international obligations defined by a treaty, to which the United States is not a party such as the United Nations Convention on the Law of the Sea, still trump the ADA (Bodansky, 2005)? Another issue concerns the domino effect by which other nations could enact laws, such that compliance with the laws of both ports could be impossible, posing a dilemma for international relations when a resolution must be made as to which law controls (Sheehan, 2006).

Further, on remand to the district court, the Fifth Circuit observed that the Supreme Court did not eliminate its original grounds for denying relief, that is, the government's failure to date to promulgate uniform physical accessibility guidelines for cruise ships, as at least being a factor in the liability determination (Spector. v. Norwegian Cruise Line, LTD, 5th Circuit, 2005). Even though Title III applies to cruise ships, as long as there is no interference with internal operations, its application is limited by its own terms. The ADA only requires *reasonable* modifications in policies, practices, or procedures that would not fundamentally alter the services offered, and requires only the removal of barriers that are *readily achievable*, that is, that can be accomplished easily without much difficulty or expense, taking into account the impact upon the overall operation of the facility. But how are those limitations operable in the context of an ocean-going vessel? The First Circuit Court of Appeals also has questioned how an ADA complaint against a foreign-flagged ship "may proceed despite the absence of a separate category of regulations governing the new construction and alteration of cruise ships" (Disabled Americans for Equal Access, Inc. v. Ferries Del Caribe, Inc., 66, 2005).

Nevertheless, a district court recently denied NCL's motion to dismiss an ADA complaint filed against one of its American flagged ships, on the asserted grounds that the regulations have not been promulgated yet. The court predicted that "[S]ome proposed barrier removals (e.g., moving life boats) may be in such obvious conflict with SOLAS that they can be dismissed from the face of the complaint;" but on the other hand, "[I]t is difficult to fathom what international obligation would conflict with a requirement that the *Pride of Aloha* be fitted with a pool lift" for access to the pool and spa (White v. NCL America, Inc., .*7-*10, 2006). The court suggested that the feasibility of the removal of other barriers might require significant discovery and guidance by experts in technical and engineering elements that can be affected by particular barrier removal methods. Plaintiff had alleged eight other barriers for disabled passengers in violation of the ADA, in addition to the unavailability of lifts and inadequate paths of travel to the pool and spa, including 1) an insufficient number of accessible cabins; 2) an insufficient variety of amenities and pricing of accessible cabins; 3) inflated prices for accessible rooms compared to similar rooms for non-disabled passengers; 4) an insufficient door pressure and reach range to amenities in accessible cabins; 5) an insufficient number of public restrooms in public areas of the ship; 6) an insufficient disabled accessible seating in public areas, including theaters, lounges and bars; (7) inaccessible seating and paths of travel in the ship's Blue Hawaii night club; and 8) inadequate transportation and access to excursions which are offered to non-disabled passengers. The feasibility of such requested accommodations, given both the mandate and the limitations of the ADA, are still without guidance from government regulatory authorities.

Title III directs the Department of Justice and Department of Transportation to promulgate regulations governing accessibility for public accommodations (42 U.S.C. § 12186 (2006)). However, the Department of Justice did not interpret the new construction and alteration provisions of subpart D of the regulations to apply to cruise ships (Resnick v. Magical Cruise Company Ltd., 2001). As a result, the authority for developing regulations specifically applicable to ocean going vessels vests is the United States Access Board, which released a revised draft of guidelines for passenger vessels under the ADA for public comment in July of 2006. The guidelines provide accessibility criteria for various types of vessels, including cruise and gaming ships, ferries, and excursion boats, among others, and incorporate feedback received from the public and special interest groups who responded to a previous draft (Revised Draft, 2006).

Even though ADA plaintiffs may state a cause of action against foreign and American flagged ships for the removal of barriers that are readily achievable, and even though regulations addressing those issues are pending, litigating an ADA case against cruise lines will not be an easy campaign. This premise is true for most passenger plaintiffs, considering that the limited rights and remedies available under admiralty law "are governed by antiquated legal principals which favor cruise lines to the detriment of cruise passengers" (Dickerson, 448, 2004). There are several reasons why litigation by consumers against cruise lines is difficult, costly, and usually less than fruitful. First, ADA plaintiffs will bear the burden of proving that barriers may be removed in a readily achievable manner and that such barrier removal will not conflict with the internal order of the cruise ship (White v. NCL America, Inc., 2006). This might prove a formidable burden involving complex expert testimony regarding shipbuilding and international law.

Second, forum selection clauses, which provide that any controversy arising out of the cruise contract are to be litigated if at all, in a certain jurisdiction to the exclusion of all others, are presumptively valid under maritime law, unless enforcement would be unreasonable and unjust, or the clause was the result of fraud or overreaching (The Bremen v. Zapata Off-Shore Company, 1972). The Supreme Court extended that principle to contracts between passengers and cruise lines by upholding the non-negotiated forum selection clause contained in a cruise contract (Carnival Cruise Lines v. Shute, 1991). As a result, ADA plaintiffs will need to litigate in a potentially distant forum selected by the cruise line, notwithstanding the criticism levied by commentators that a forum selection clause in this context does not serve its economic goals, and in fact transforms forum selection agreements from instruments of freedom to instruments of economic oppression (Purcell, 1992; Borchers, 1992; Goldman, 1992).

Third, there is usually a time limitation for filing suit in the passenger contract, which provides that notice of the intent to file suit must be given, and that claims must be filed within a specified time period. In the absence of contractual provisions to the contrary, admiralty law has a three-year statute of limitation period for personal injury claims arising out of a maritime tort (46 U.S.C. § 30106 (2006)), although a one-year limitation period with a six-month notice requirement to the carrier is permissible under admiralty law if such a limitation is contained in the contract of passage (46 U.S.C. § 30508(b) (2006)). Provisions for even shorter periods are routinely included in passenger contracts and upheld by courts, provided they are reasonably communicated (Keefe v. Bahama Cruise Line, Inc., 1989). A common limitation period of three months for any additional claims not involving personal injury may be applicable to complaints alleging violations of the ADA, which likely would be enforceable under maritime law (Ames v. Celebrity Cruises, Inc., 1998).

Lastly, remedies recoverable by plaintiffs may be limited under maritime law, as well as by the provisions of the ADA itself. As a result of a compromise designed to protect the interests of small businesses, Title III of the ADA covers a broad list of places of public accommodation, but in exchange, provides a limited set of remedies. Private parties bringing suit under that Title are only entitled to injunctive relief, not monetary damages, although the Attorney General may seek civil penalties (42 U.S.C. § 12188 (2006)). Arguably, as a result of its limited avenue for relief, as well as the narrow interpretations by courts of the authority to grant injunctive relief, Title III has been less successful than what was expected (Colker, 2000). Even if the damages issue was reconsidered in the future, it is unlikely that anything other than limited compensatory damages would be permissible since punitive damages are not routinely awarded under maritime law. For example, punitive damages are unavailable in a negligence case arising in admiralty absent allegations of willful or wanton conduct (In re Amtrack "Sunset Ltd." Train Crash in Bayou Canot, 1997). Moreover, federal legislation permits cruise lines to insert a provision in the passenger contract which disclaims liability for emotional distress, mental suffering and psychological injury, except for "liability of a crewmember or the manager, agent master, owner, or operator of a vessel in a case involving sexual harassment, sexual assault, or rape" (46 U.S.C. § 30509 (b)(2) (2006)).

Further, the general admiralty rule is that attorneys' fees are not allowable as damages nor taxable as costs absent a showing of bad faith or oppressive litigation tactics (Southworth Machinery Co. v. F/V Corey Pride, 1993), although the continued viability of this rule has been questioned (Robertson, 1996). The Eleventh Circuit as recently as 2005 observed that generally "attorney fees are not awarded in admiralty cases," (Offshore Marine Towing, Inc. v. MR23, 1256, 2005) absent special circumstances, such as when the losing party acted in bad faith (Alyeska Pipeline Service. Company v. Wilderness Society, 1975). The ADA, on the other hand, provides that "[I]n any action or administrative proceeding commenced pursuant to this Act, the court or agency, in its discretion, may allow the prevailing party, other than the United States, a reasonable attorney's fee, including litigation expenses, and costs..." (42 U.S.C. § 12205 (2006)). If admiralty law trumps this provision of the ADA, making such fees not recoverable, then there is little or no incentive for private lawsuits. The Department of Justice then would be the only avenue for redress in assuring compliance with its promulgated standards.

CONCLUSION

One scholar argues that it may be a stretch to consider such structural modifications as involving the "internal discipline" of the ship or "the rights and duties of the officers and crew towards the vessel, or among themselves" as contemplated by the Wildenhus Court: "The only basis for arguing that the structural modifications might involve the ship's internal affairs is the potential effect of these modifications on the ship's architecture. However, even if this brings these modifications within the general scope of the internal affairs doctrine, there remains the Wildenhus exception for matters that involve "the peace or dignity of the country, or the tranquillity of the port, and "the non-application of the ADA would affect the 'dignity' of the United States to the extent that it would compromise the values embodied in the ADA's non-discrimination principle" (Symeonides, 2006 p.498-99). While the Supreme Court did not seem to embrace this premise, as a practical matter market forces have already inspired cruise lines to outfit their ships to accommodate disabled passengers, who are a significant part of the industry's customers (Kaufman, 2006).

The economic consequences of compliance for foreign flagged vessels with whatever regulations are developed and are also applicable to them is difficult to predict. But given the decision in *Spector*, what also might be looming is the likelihood of increased scrutiny of the cruise industry by Congress. News stories covering the disappearances of loved ones at sea and fires onboard ships, for example, may have already stirred Congress to consider further regulation of the cruise industry. Recently Congress held hearings to examine who has jurisdiction when a crime is committed or an accident occurs at sea, and to explore requirements for reporting crimes to U.S. authorities and maintaining a data base of such statistics for passengers (Cruise Control, 2006). The House Committee on Governmental Reform held hearings in December of 2005 and March of 2006 on maritime security and legal jurisdiction issues related to crimes against U.S. citizens in international waters, including criminal incidents involving U.S. passengers on cruise ships. The overall impact of the potential regulation of such matters, which now seems permissible, could be substantial.

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CONSUMER PERCEPTIONS ON THE CONSUMERISM ISSUES AND ITS INFLUENCE ON THEIR PURCHASING BEHAVIOR: A VIEW FROM MALAYSIAN FOOD INDUSTRY

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ABSTRACT

Despite the growing awareness of the consumerism and social responsibility issues in academia as well as in the industry, the investigation of the influence or effect of these issues on the consumer purchasing behavior especially in terms of both fairness on business practices(micro issues) and environmental consumerism practice(macro issue) is very limited. Though there exist very few prior studies which tend to conceptually show the effect of the consumerist issues/ethical issues on the consumer purchasing behavior, empirical evident are yet to be explored.

Thus, this study had been developed to empirically investigate the factors of business ethics and consumerism that would likely to influence the customer ethical purchasing behavior. The basic objective of this study is to find out the consumers' perceptions on the both consumerism issues such as fairness on trade practices and environmental consumerism practice and their impact on their ethical purchasing behavior in food industry in Malaysia. Data was collected by applying the personal interview method where by the selection of sample respondents was based on the convenience sampling techniques targeted at 400 respondents for 4 states such as Kula Lumpur and Negeri Sembilan (Central region) and Melaka and Johor Bahru(southern region). The investigation was applied to the food products since it is very delicate sector and where there is much concern for the consumerist issues as suggested by Bhushan (2003); Brunk(1973); and Turner (1995). The result revealed that both the micro and macro consumerism issues such as fairness on trade practices and environmental consumerism practice were found to have significant association with the consumer ethical purchasing behavior. It implies that the companies should try to concentrate on the ethical aspects of business in order to build competitive advantage in the market. Furthermore, the companies should also try to reconcile the ethical aspects of the products with the other functional attributes of the products since the findings revealed that the consumers are not ready to sacrifice the other necessary attributes of products such as product quality, brand image, convenience etc only for ethics.

INTRODUCTION

In this modern era of societal marketing concept business ethics and social responsibility is becoming one of the central issues of all the marketing practices. Now the business enterprises cannot consider themselves as sovereign in the marketplace. The modern waves of consumerism have made the consumers vocal in expressing their rights and privileges in the marketplace. However, from the prior studies it can be inferred that a comprehensive study is still required in this area especially in respect of consumer behavioral perspective. The growing concern for ethical issues or consumerist issues among consumers has been well documented in marketing literature. However, despite the attention to the subject and rising concern for 'ethical' issues in society, research has tended to neglect the ethical consumer (Mintel 1999). In recent years, business ethics has drawn increased interest from business and marketing practitioners as well as from academicians. However, much of the research that has been done on business ethics has focused on marketing activities (Ferrell and Gresham, 1985; Ferrell, Gresham and Fraedrich 1989; and Hunt and Vitell; 1986, 1992). Uusitalo and Oksanen(2004) also argued that though business ethics and corporate social responsibility have gained more attention in recent years, the empirical research of consumers perspective on ethics is still minimal.

The overall objective of the study is to explore the consumers' perceptions towards the business practices in term of fairness on trade practices(micro consumerism issues) and environmental consumerism practice(macro consumerism issue) in the marketplace; the extent of the consumers' purchasing behavior regarding the consumerist issues and the relationship between the fairness on trade practices and environmental consumerism practice with the consumers purchasing behavior regarding the consumerist issues in the food industry in a newly developed country like Malaysia. Apart from this the prior supports regarding the specific research objectives have been discussed below:

There was a slight degree of skepticism among consumers about quality of products in the market, there is obvious mistrust of the communications manufacturers use to attract buyers to those products (French, Barksdale and Perreault, 1982). There is questionable among the consumers regarding the current food labeling issues (Brunk, 1973). Barksdale and Darden (1972) found that majority of the respondents agreed that from the consumers' standpoint, manufacturers' procedures for handling complaints and settling grievances were not satisfactory. French et.al. (1982) and Lisa, (2004) found that majority of the respondents believe that price charged by the companies is excessive and unfair. Mingquan (2003); Paugh and Fletcher (2002); and Youfu (2002) revealed that the organizations have growing concerns towards the environmental consumerism.

Uusitalo and Oksanen (2004) found that while the majority of the respondents regard business ethics as important, this attitude does not translate into their choice behavior. Boulstridge and Carrigan (2000); and Carrigan and Attalla (2001) argued that the consumers are concerned regarding the ethical purchasing but the other purchase criteria such as price, value, quality and brand are often important choice criteria than ethics. Memery, Megicks and Williams (2005) notified that the consumer's skepticism about the fairness of advertising often discouraged them to buy products according to the ethical consideration. Shaw, Grehan, Shiu, Hassan and Thompson (2005) notified that honesty in labeling can influence the consumer pro ethical or pro consumerist purchasing behavior.

Memery et.al. (2005) mentioned customer care as an important factor that can likely influence the consumer purchasing behavior. Uusitalo and Oksanen(2004) argued that fairness with pricing is an important consideration among the consumers in involving in the pro-ethical or pro-consumerist purchasing. Charter (1992); Moisander(2001); and Uusitalo (1986) argued that the consumer pro-environmental purchasing behavior is positively influenced by the availability of the ethical and social responsible firms that offer environmental friendly or sound products .

From the above discussions the following research objectives have been constructed:

1. To determine the consumers' perceptions towards the business practices in terms of fairness in the marketplace and environmental consumerism practice in food industry in Malaysia.
2. To ascertain the extent of the consumer purchasing behavior regarding the consumerist aspects in food industry in Malaysia.
3. To derive the relationship between the fairness on trade practices (micro consumerist issues) and environmental consumerism practice (macro issues) and the consumer ethical purchasing behavior.

LITERATURE REVIEW

Consumerism is defined as social force to protect consumer interests in the marketplace by organizing consumer pressures on business. In fact, consumerism is a protest of consumers against unfair business practices and business injustices. It aims to remove those injustices, and eliminate those unfair marketing practices, e.g. misbranding, spurious products, unsafe products, planned obsolescence, adulteration, fictitious pricing, price collusion, deceptive packaging, false and misleading advertisements, deceptive warranties, hoarding, profiteering, black marketing, short weighs and measures, etc. Consumerism is the public demand both for refinement in marketing practices to make them more informative, more responsive, more sincere, more truthful and more efficient, and for a new concern with factors other than privately consumed goods and services that determine the quality of life (Sherlaker, 1999). According to Kaynak (1985) and Quazi (2002) the consumerism is concerned with both the micro and macro consumerist issues. The micro consumerist issues include the issues like misbranding practice, misleading advertisement, deceptive packaging, unfair pricing etc. While on the other hand, the macro consumerist issues are mainly concerned with the broader contexts like environmental pollution, health care system, antinuclear issues etc. The micro issues of the consumerism are also known as the fairness on trade practices or fairness on business practices. In this research, four well known and widely discussed micro consumerist issues such as misleading advertisement, deceptive packaging, customer care and unfair pricing as well as one macro issue (environmental consumerism practice) have been taken into consideration in order to find out their effect on the consumer purchasing behavior.

CONSUMER PURCHASING BEHAVIOR

Consumer Purchasing Behavior is the dependent construct of the study. Assael (2004); Aaker and Keller (1990); and Berkman and Gilson (1978) have indicated the customer purchasing behavior as an important facet of the consumer behavioral perspective. McKenzie (2000) has also denoted the customer purchasing behaviour as the significant behavioral aspect of consumer behavior. Al-Mazarooei, Chomo and Omezzine (2003) focused the consumer behavioral perspective in the ethical perspective in terms of the purchasing behavior. As a result this study considered the consumer purchasing behavior as an important dimension of consumer behavioral perspective to find the impact of the micro and macro consumerism issues on it.

Consumer Purchasing Behavior is the decision processes and acts of people involved in buying and using products. Consumer Purchasing Behavior refers to the buying behavior of the ultimate consumer (Assael, 2004; and Berkman and Gilson, 1978). Berkman and Gilson (1978) argued that a purchasing behavior is the sequential activity from buying intention to actual purchasing behavior.

In this study the purchasing behavior is linked and has been defined in terms of ethical or consumerist aspects. On the basis of the prior studies by Irving, Harrison and Rayner (2002); Simon (1995); Uusitalo and Oksanen(2004); Uusitalo (1986); and Zadek, Lingayah and Forstater (1998); the consumer purchasing behavior exhibits the consumers' expressed behavior regarding the consumerist or ethical issues while purchasing their products. In other words, on the basis of the prior studies in this area the consumer purchasing behavior can be defined as the consumer concerns and attitudes regarding the consumerist issues while purchasing their products.

Boulstridge and Carrigan (2000); and Carrigan and Attalla (2001) notified about the consumers less inclination towards ethical purchasing where they mainly focused that the main barrier of the consumers not to be involved in the ethical purchasing is the consumers skepticism regarding the ethical practices in the marketplace as well as the existence of the ethical firms in the marketplace. They also argued that another reason for which the consumers do not involved in the ethical purchasing is that many consumers perceive the other choice criteria such as product, price, brand etc as more important than ethics. Uusitalo and Oksanen (2004) found that majority of the consumers are concerned regarding business ethics but it is not usually executed by them in any purchasing situation.

In the conclusion it can be said that in order to find out the influence of the different consumerism issues on the consumer behavioral perspective it is important and also suitable to first find out its impact on the consumer ethical purchasing behavior since the term consumerism is very much related to the consumer. From the prior studies it has been derived that the consumers are not usually engaged in the ethical purchasing behavior where the main reason is that they are uncertain regarding which firms follow the ethical rules and which do not and retain an unhealthy skepticism that there is little to choose from between the companies. Moreover, there also exist some consumers who usually give more preference to the other criteria of the products such as product, price, brand preference etc rather than ethics.

FAIRNESS ON TRADE PRACTICES (MICRO ISSUES)

In aspect of fair trade, AIM-the European Brands Association (2002) prepared a paper on the fairness of trade in order to meet the consumers' current and future needs and by its of consumer rights and interests. According to AIM there are several categories of unfairness which are as misleading practices, failure to provide material information to the consumers, undue influence and complaint handling and after sales service.

According to Kaynak(1985); Quazi(2002) and Sherlaker (1999), the fairness on trade practices construct which are also termed as the micro issues of consumerism consider various exploitative business practices among which the mostly discussed issues are misleading advertising, deceptive packaging, unfair pricing, customer care, product adulteration, black marketing, misbranding practice etc.

Misleading advertising

Misleading advertisement refers to the advertising that, although, not strictly untrue, leads consumers to less than accurate conclusions. Intentionally misleading consumers is an extreme form of misleading advertising and is against the advertising standards code of conduct (Oxford Dictionary of Business, 2005). Koslow(2000); and Maronick(1991) argued that deceptive or misleading advertising should be legally defined as: the standard that has generally relied on what a reasonable consumer would take away from an advertisement under the circumstances. Attas (1999) argued that an advertisement will be deemed misleading or deceptive only if it is reasonable to expect that persons exposed to it, or those targeted by it, would come to hold false beliefs as a result of exposure to it. He further added that a misleading advertisement is one that causes a distorted perception and for which the advertiser is considered responsible. It might be thought that the consumer mislead by an advertisement will be tempted to buy the advertised product and in that way either getting less than he thought he would or paying more than he should.

Knauer (1973) mentioned about the National Business Council's advertising reporting on the following issues:

> "Advertising should avoid the use of claims whose validity depends upon fine interpretation of meaning. Furthermore it also stated that advertising shall not claim nor promise by implication any product performance or characteristic which is not fully supported by test or research data or other similar factual information and the test of whether anything is permissible in advertising under the policy is to ask whether it is true, believable and good taste".

Deceptive packaging

Faruque (2003); and Mann and Thornton (1978) defined deceptive packaging as one sort of unscrupulous practice done by the marketers whereby the faulty product information or misinformation is provided in order to deceive consumers.

Mason, Rath, Husted and Lynch (1995) mentioned about the Fair Packaging and Labeling Act of U.S.A. (1966) where it was stated that the information given on a package should tell the consumer exactly what the package contains. Consumers can then compare the product with those of other manufacturers. The Fair Packaging and Labeling Act (1966) require that the label state the package's contents and weight, and the name of the manufacturer or distributor. Furthermore, since 1990 several states and the federal government have banned deceptive environmental claims in ads and on product labels. Mann and Thornton (1978) also mentioned that the amount and type of information available to the customer through the product label and package on any particular product is the function of three factors such as government regulation, independent labeling institute and business policy.

In the Business Week (1958) it has been stated that marking, advertising and labeling practices have improved enormously but the complexity of purchasing decisions has also increased, so that informational needs still seem unsatisfied.

Unfair pricing

Unfair pricing is also a burning consumerist issue since pricing is the most sensitive issue to the consumers. French et.al. (1982); Kaynak (1985); Lisa (2004); and Sherlaker (1999) indicated that unfair pricing which the consumers believe is charging of either excessive price from the consumers than its original price or to charge fictitious pricing.

Mason et.al. (1995) mentioned that the various type of fictitious pricing include price fixing, price discrimination, resale price maintenance and deceptive pricing. These are all various types of fictitious pricing.

Customer care

Customer care is a very important issue for any business in satisfying their customers because proper customer care can create an image to the customers as the ethical and social responsible firm. Berkman and Gilson (1978); and French et.al. (1982) defined customer care as the companies' engagement in complaint handling and after sales service to the customers.

Sherlaker (1999) mentioned that as a practical solution for establishing better rapport with the consumer, it is suggested that every manufacturer, especially for consumer goods, establish a consumer affairs cell (CAC). The main objectives of this cell would be to become more responsive to the valid grievances of consumers with resolving customer complaints promptly. Furthermore they should also act promptly in disseminating consumer information; advising management on consumer issues; dealing with/providing liaison to outside consumer interest groups and also to educate consumers about their rights and responsibilities.

ENVIRONMENTAL CONSUMERISM PRACTICE (MACRO ISSUE)

Environmental consumerism practice refers to the green marketing practice which can be defined as follows:

1. "The marketing or promotion of a product based on its environmental performance or an improvement thereof" (Charter and Polonsky, 1999).
2. "The holistic and responsible strategic management process that identifies, anticipates, satisfies and fulfils stakeholder needs, for a reasonable award, that does not adversely affect human or natural environmental well-being."(Charter, 1992).

HYPOTHESIS DEVELOPMENT

From the previous studies it has been found that there almost exists no prior study that explains the influence of the separate and specific consumerist issues regarding the fairness on trade practices on the consumer purchasing behavior. There is also lack of prior empirical studies that discussed both micro and macro consumerism issues on the consumer behavioral perspective. However there exists very limited number of studies that merely qualitatively or conceptually explain the influence of the ethical/consumerist issues on the consumer purchasing behavior.

Memery et.al. (2005) notified that the consumer's confusion about the fairness of advertising often discouraged them to buy products according to the ethical consideration. Boulstridge and Carrigan (2000); and Uusitalo and Oksanen (2004) also mentioned that the truth in advertising claim likely to have significant effect on the customer pro-ethical purchasing behavior. So from the above discussion the following hypothesis can be developed:

H1: There is a significant influence of misleading advertisement on consumer purchasing behavior.

Shaw et.al. (2005) notified that honesty in labeling can influence the consumer pro ethical or pro consumerist purchasing behavior. Dickson and Wilkie(1985); Dickson and Sawyer (1990) also argued that honesty and informative labeling may have significant effect on the consumers pro-ethical purchasing behavior. So from the above discussion the following hypothesis has been developed:

H2: Deceptive packaging has a significant impact on the consumer purchasing behavior.

Memery et.al. (2005); Mason et.al. (1995) mentioned about the customer care and the business responsibility as the vital ethical aspects that are likely to influence the consumer pro-ethical purchasing behavior. So from the above discussion the following hypothesis can be developed:

H3: There is a relationship between customer care and consumer purchasing behavior.

Uusitalo and Oksanen(2004) argued that fairness with pricing is an important consideration among the consumers in involving in the pro-ethical or pro- consumerist purchasing. Memery et.al. (2005) also argued that fairness with pricing has a significant effect on the consumer pro-ethical or pro-consumerist behavior.

H4: There is a relationship between unfair pricing and consumer purchasing behavior.

Ellen, Wiener and Cobb-Walgren (1991); McKenzie-Mohr (2000); and Shrum, McCarty and Lowrey (1995) argued that consumers' skepticism regarding the environmental consumerism practice discourage them to be involved in ethical and pro-environmental purchasing. Chase (1991); and Chase and Smith (1992) argued that the consumers are skeptical regarding the environmental claims and the environmental consumerism practices which discouraged them to be engaged in the environmental purchasing. Charter (1992); Moisander(2001); and Uusitalo (1986) argued that the consumers pro-environmental purchasing behavior is positively influenced by the availability of the ethical and social responsible firms that offer environmental friendly or sound products . So from the above discussions the following hypothesis can be developed:

H5: There is an effect of environmental consumerism practice on consumer purchasing behavior.

In the conclusion it can be argued that the consumer ethical purchasing behavior is significantly influenced by the ethical business practices in the marketplace where the reason is that the consumers usually feel discouraged to be involved in ethical purchasing behavior if they perceive that more or less all the firms are unethical in some way.

METHODOLOGY

The target population of this study is the end consumers who have at least STPM or Pre-university degree due to the sophistication and complexity of the research area. In this research sampling was used because it would incur too cost to perform a census Furthermore, there is also a time constraint to collect huge amounts of data from the census and to analyze them for interpreting the result. Non probability sampling of convenience sampling was used where the samples are drawn at the selected convenience location in which the possibility to get the targeted respondents is greater. Samples are targeted from 4 states i.e. central region (Kuala Lumpur and Negeri Sembilan), and southern region (Melaka and Johor Bahru). Out of 400 sample respondents 313 could be gathered at a response rate of 78.25% where some of the respondents refused to actively participate in the survey. Face to face interview was conducted with the sample respondents since it is considered as the more flexible form of data collection and also since the rate of refusal under this method is low (Sherlaker ,1999). Questionnaire was used as the survey instrument. The questionnaire consisted of three sections: demographic profile of the respondents, consumers' perceptions or attitudes towards the companies' level of fairness on business or trade practices and environmental consumerism practice in the marketplace and the consumer purchasing behavior regarding the consumerist/ethical issues. All the questions were structured using the six point Likert scale from 1= strongly disagree to 6= strongly agree. No "middle" or "neutral" column was included because the respondents were forced to make a choice. This forced- choice decision was made for two reasons. First the instrument was intended to measure definite attitudes; respondents given a middle choice might use it simply because of laziness or fatigue. Secondly, six-point scaling is consistent with the majority of psychological research concerning the formation and permanence of attitudes (Kiesler, Collins and Miller 1969; and Klein, 1982). The questionnaire of this study has been developed by considering the issues fully or partially from the studies done by Barksdale and Darden (1972); Berkman and Gilson (1978); French et.al. (1982); Jain and Kaur (2004); and Klein (1982).

RESULTS AND DISCUSSION

Two types of analysis had been conducted such as descriptive analysis and hypothesis testing. The descriptive analysis have been conducted which aimed to answer the first two objectives of the study. Besides, hypothesis testing has been conducted in order to answer the main objective of the study i.e. the relationship between the micro and macro consumerism issues and the consumer purchasing behavior in terms of the ethical issues.

Demographic profile of the respondents

The first portion of the analysis demonstrates the demographic profile of the respondents who are the consumers with at least STPM or pre university level degree. A brief discussion regarding this profile has been illustrated below:

Age

In this research the age of the respondents has been categorized into below and 20, 21-30, 31-40 and 40 above. Among these categories the 21-30 aged consumer group represents the highest percentage which is 68.10 % while the lowest one is below and 20 aged group which represents 7.3%.

Gender

Both male and female respondents have been considered which represents 52.9% and 47% respectively.

Race

All three races have been considered such as Malay, Chinese and Indian. Moreover the other category has been also considered which includes the expatriates or the international students. In this category Malay represents 55.6% while the others category represents the lowest percentage which is 10.2%.

Educational qualification

In this criterion, the educational qualification of the respondents has been divided into STPM/pre university level, diploma, bachelor degree and post graduate degree holders. Bachelor degree holders represent the highest percentage which is 46% while the post graduate degree holders represent the lowest percent i.e. 9.3%.

Descriptive analysis

The descriptive analysis has been used in this research to ascertaining the consumers' perceptions on the fairness on trade practices and environmental consumerism practice in the market and to derive the extent of the consumer purchasing behavior regarding the consumerist issues in food industry in Malaysia. It also serves as basic foundation of determining the association between the independent and dependent variables of the study.

Table: 1 Descriptive analysis

Descriptive analysis	Mean Score
True picture of advertisements (MA1)	2.79
Genuine claims of advertisement (MA2)	2.78
Proper information of package or label (DP1)	2.86
Expire date on label or package (DP2)	2.97
Fair price on label or package (DP3)	2.93
Company's procedures for handling complaints (CC1)	2.95
Company's procedures for settling grievances (CC2)	3.02
Excessive price of products (UP1)	4.25
Fictitious pricing of products (UP2)	4.21
Caring about the impact of products on environment (EC1)	3.09
Offering products in biodegradable package (EC2)	3.03
Offering products in recyclable package (EC3)	3.00
Offering products which cause less pollution (EC4)	2.92
Offering environmentally certified products (EC5)	2.94
Buying products from socially responsible companies (PB1)	3.09
considering ethical or consumerist issues (PB2)	3.08
Switching products for ethical reason (PB3)	3.17

Table 1 illustrates the mean scores of each statement of the consumers' perception towards the companies' level of fairness on trade practices and environmental consumerism practice in order to meet the first objective of the study and the extent of the consumer purchasing behavior regarding the consumerist issues to derive the answer of the second objective of the study. In other words, here in this analysis the mean scores have been derived for the independent variables such as misleading advertising(MA), deceptive packaging(DP), customer care (CC) and unfair pricing (UP) in order to find out the respondents' opinion towards the consumerism issues(independent variables) to answer the first objective of the study. The analysis also revealed the respondents' attitudes towards the ethical purchasing behavior (PB), the dependent variable of the study in order to answer the second objective of the study.

Here from the above table it has been found that the sample respondents moderately disagree regarding the fairness on advertising and packaging which implies that the sample respondents believe that the companies are engaged in the misleading advertising and deceptive packaging practices. The above table also demonstrates that the sample respondents moderately disagree regarding the companies efficiency towards the complaint handling and settling grievances. Moreover the sample respondents moderately agree regarding the companies' unfair pricing practices. The sample respondents also moderately disagree regarding the companies consciousness towards the environmental consumerism practice. So from the above table it can be observed that almost in all the cases the consumers perceive that the companies are not engaged in ethical and socially responsible business practices in the food industry in the market place. This result is aligned with the prior studies done by Anon (2003); Barksdale and Darden (1972); Bhushan (2003); Brunk (1973); French et.al. (1982); Koslow (2000); and Lisa (2004) where it has been found that majority of the consumers perceive that the companies do not practice business ethics and they are not socially responsible.

While on the other hand it can be derived that the mean scores represent that the consumers expressed their less inclination to be involved in ethical purchasing behavior or considering the consumerist issues while purchasing the food products. The result is aligned with the prior studies by Carrigan and Attalla (2001); Roberts (1996); Simon (1995); and Uusitalo and Oksanen (2004) where it has been found that the consumers did not exhibit any inclination towards the ethical or consumerist issues while purchasing their products.

Reliability analysis

The reliability concept tells how accurate, on the average, the estimate, of the true score of the inter items internal consistency of the variables to be measured. In this study, Cronbach Alpha will be utilized to test the internal consistency for all items under their respective variables.

The outcome derived that all the factors in the variables form a single, strongly consistent and conceptual construct. The value recorded for alpha for all 6 factors are also above the acceptable range of $\alpha = 0.7$ (Nunnally 1978).

However, it can be found that the alpha values here in most of the cases are extremely high. This may be due to the less number of factors in each issue which is by nature very selective.

Furthermore, the respondents also view these issues more or less in very similar way which also stopped any further variation.

For the similar research it has been found that almost majority of the consumers perceived these issues in very similar way such as Barksdale and Darden (1972); Carrigan and Attalla (2001); French et.al. (1982); and Uusitalo and Oksanen (2004) etc.

Table: 2 Reliability analysis

Variable	Cronbach Alpha (α)
Misleading Advertising	0.916
Deceptive Packaging	0.90
Customer Care	0.765
Unfair Pricing	0.887
Environmental consumerism practice	0.912
Purchasing Behavior	0.914

Hypothesis testing

In this study correlations between the independent and dependent variables have been conducted in order to find out whether there is any relationship between them. The hypotheses are being tested in order to find out whether the fairness on trade practices(micro issues) in respect of the misleading advertisement and deceptive packaging, customer care and unfair pricing as well as the environmental consumerism practice (macro issue) do have any relationship with the consumer purchasing behavior.

Table: 3 Correlation coefficients (for hypothesis testing)

Variable	Purchasing behavior	Sig. value
Misleading Advertising	.116*	(.041)
Deceptive Packaging	.238**	(.000)
Customer Care	.180**	(.001)
Unfair Pricing	.165**	(.003)
Environmental consumerism practice	.357**	(.000)

*Correlation is significant at the 0.05 level (2-tailed)
**Correlation is significant at the 0.01 level (2-tailed)

Table 3 shows the association between the sub-independent variable i.e. the issues of fairness on trade practices in terms and the consumer purchasing behavior towards the consumerist issues. In testing the hypothesis the Pearson Correlation had been performed to assess the relationship between the independent and dependent variables.

The table shows that the ρ value for each of the sub-independent variables of the fairness on trade practices is less than 0.05. So it can be said that they are significantly associated. Another independent variable i.e. environmental consumerism practice is also significantly associated with the dependent variable such as customer ethical purchasing behavior. However, the correlation coefficients of each sub-independent variable denote that there is a weak association between the variables. Among these variables the statements of the unfair pricing denoted unfavorable meaning since the issue and its statements are by nature represents unfavorable mode (which has been also derived from the prior studies) where it was expected to have negative association between this variable and the consumer purchasing behavior. But in this case also there found to have positive association between the variables.

So among these variables, misleading advertising, deceptive packaging and customer care are found to have positive association with the consumer purchasing behavior which indicates that the consumer ethical purchasing is positively influenced by the firms' fairness practices in terms of these issues. Only in case of unfair pricing there is inverse impact of this issue on the consumer ethical purchasing behavior where the reason may be that for this particular aspect or issue where the statement represents unethical meaning the consumers get more vigilant if they can be aware of the unethical business practices especially in respect of unfair pricing. This identification or the perception towards the particular unethical or unfair practice make them more alert in making a pro-ethical purchasing. This result has proved the arguments of few prior conceptual studies by Geath and Heath, (1987); Koslow (2000); and Mohr, Eroglu and Ellen (1998) where it has been mentioned that in certain cases consumers' skepticism may influence them to be involved in ethical purchasing.

The strength of association between the variables is weak where the reason may be that still there are some consumers who are not aware of the ethical or the consumerist issues while purchasing their products and also there are some consumers who are mainly concerned with the other aspects of products such as price, product quality, brand preference etc than ethics. Apart from this it can be said that the hypotheses are supported since prior studies have found that the consumerism issues do have influence on the consumer ethical purchasing behavior (Carrigan and Attalla, 2001; and Memery et.al. 2005).

Moreover, in order to view a clearer scenario a correlation test has been conducted between the overall fairness on trade practices (micro issues) and the environmental consumerism practice (macro issue) with the consumer pro-ethical or pro-consumerist purchasing behavior where it was found a correlation coefficient of +.280 for the relationship between the overall fairness on trade practices and consumer ethical purchasing behavior which indicates a weak association between the variables. While the correlation coefficient between the environmental consumerism practice and consumer ethical purchasing behavior is weak but tends towards moderate association with the correlation coefficient of +.357. Thus, on the overall it can be inferred that the environmental consumerism practice has more impact on the consumer ethical purchasing behavior in comparison to the fairness on trade practices. However, it can be also observed that both the consumerism issues such as micro and macro issues have significant influence on the consumer ethical purchasing behavior (since the p value for both the issues is 0.000). The direction of association for both of the cases is positive. From this analysis it can be inferred that the more the consumers will perceive that there exists adequate ethical firms and ethical practices in the market the more likely they are to be involved in the ethical purchasing behavior.

Table: 4 Correlation coefficients (Comparison between overall micro and macro issues)

Variable	Purchasing behavior	Sig. value
Overall fairness on trade practices (micro)	.280**	(.000)
Environmental consumerism practice(macro)	.357**	(.000)
**Correlation is significant at the 0.01 level (2-tailed)		

The prior conceptual studies also argued that the availability of the ethical firms as well as the existence of the ethical business practices likely to have influence on the consumer ethical purchasing behavior where these studies mentioned that the most important barrier of the consumers not to be involved in the ethical consumption is the lack of availability of the ethical firms and the ethical practices.

In a prior study Uusitalo and Oksanen (2004) argued that the reason why the consumers are not involved in pro-ethical purchasing is that the consumers are uncertain about which products and firms follow the ethical rules and which do not. Uusitalo and Oksanen also mentioned that the most important obstacles to ethical consumption were difficulties in obtaining information problems in product availability. Carrigan and Attalla (2001) argued that other issues of products such as price, value, quality and brand are often important choice criteria than ethics. They also mentioned that the consumers do seem to be aware of unethical behavior, but they appear to be confused about who is guilty and who is not and retain an unhealthy skepticism there is little to choose from between companies. Moreover, they have also expressed skepticism about the genuineness of the firms' ethical claims.

The regression analysis has been conducted in order to find out the impact as well as predictors among the two independent variables i.e. overall fairness on trade practices and the environmental consumerism practice on the consumer purchasing behavior in order to strengthen the proposition.

Table: 5 Multiple Regression Analysis					
Model	B	Std.Error	t	Sig.	Collinearity Statistics(VIF)
(Constant)	.197	.420	.468	.640	
EC	.451	.078	5.790	.000	1.058
FP	.483	.124	3.905	.000	1.058
Adjusted R Square= 0.163 for model F value of ANOVA= 31.401 ρ value< 0.05					

From the table above the collinearity statistics table indicates that there is no multicollinearity problem since the VIF is less than 5 (Malhotra, 1999). The value of adjusted R Square shows that 16% of the variability in purchasing behavior (PB) is explained by both fairness on trade practices (FP) and the environmental consumerism practice (EC). The model also shows that F value of the ANOVA table is 31.401 ($p<0.05$) which indicates that both the variables such as FP and EC are associated with the PB. From the regression analysis it can be derived that both the FP and the EC have significant influence on the PB. Thus it can be inferred that both the variables should be taken into consideration in order to influence the customer ethical purchasing behavior.

From the regression table the estimated regression equation can be summarized as:

$$PB = .197 + 0.451\ EC + 0.483\ FP$$

In conclusion, generally the study found that all the variables have a positive coefficient which indicates that the predicted value of the dependent variable (PB) increases when the value of independent variables increases (FP and EC). The regression equation has the constant value of .197 if no initiatives are taken to increase the level of the independent variables FP and EC. However, the effort must be concentrated on the EC since it shows the higher relative importance to the identified model of t=5.790 when compared to FP (t=3.905). The result thus indicates that environmental consumerism practice is more important determinant of the customer ethical purchasing behavior.

MANAGERIAL IMPLICATION

This study has found that both the fairness on trade practices (micro issues) and environmental consumerism practice (macro issue) have some impact on the consumer ethical purchasing behavior. Thus it is better for the firms to conduct business according to ethics at least to ensure benefit to the consumers, business and the country as a whole. Furthermore by being ethical and by being concerned regarding the consumerist issues a firm can get a competitive advantage in the market. Many reputed companies in the world have been able to attain consumer confidence by putting “ethical claims” in their business slogans.

However, it is also important to note that it is not possible in reality that the consumers will sacrifice brand, quality, price, value, convenience etc for only ethics. The ethical aspects of the products should be bundled with these necessary features of the products. As a matter of fact in order to become successful as the ethical and socially responsible business a firm should try to promote its ethical practices to the consumers in such a way that it will not confuse or alienate consumers. The firms’ ethical practices should be able to convince the consumers since it has been found that the consumers usually get confused regarding the ethical claims of the products which often discourage them in getting involved in the ethical purchasing. From the prior studies by Memery et.al. (2005); and Shaw et.al. (2005) as well as from the present study it can be observed that the consumers get discouraged to be involved in ethical purchasing if they perceive that more or less all the companies are engaged in unethical practices in some way. However, the study revealed that in certain rare cases some fairness issues might have inverse impact on the consumer ethical purchasing behavior such as unfair pricing for this study, even in those cases also it can be believed that the overall fair and ethical business practices can ultimately remove any skepticism among the consumers and will convince them regarding the existence of the adequate ethical firms in the market which will ultimately involve them in the ethical purchasing behavior.

In this situation, it largely depends on the firms to make the consumers encouraged in ethical purchasing by convincing them that there are enough ethical product alternatives in the market and their ethical claims are true and genuine. Furthermore they should also demonstrate that their ethical attributes are bundled with the other functional criteria of products such as brand, quality, value, price, convenience etc.

SUGGESTION TO GOVERNMENT AND THE SOCIAL FORUMS

In order to make the consumers aware and concerned towards the consumerist issues in a country the government should take the most important and crucial role. In fact the government should provide a good shelter to the aggrieved consumers.

In Malaysia, the government and the department of the Ministry of Domestic Trade and Consumers Affairs have made a dramatic and effective attempt to protect the consumers. However, some more strategic effective actions should be taken by the government and its respective department in order to make the majority consumers aware of the consumerist issues. More over the business firm should be strictly imposed to abide by the ethical code of conduct. If the consumers can be made aware and concerned regarding the consumerist issues then the consumers will equally give importance to the ethical aspects of products with the other functional aspect of the products.

Furthermore, different social forum and the consumer association can considerably help to make the consumer aware regarding the consumerist issues as well as to protect the consumers.

In Malaysia there are various consumer associations who are trying to act effectively in spreading the consumerist issues. The consumer associations should play a pro vital role in making the average consumers aware regarding the consumerist issues from the grass root levels and should promote the ethical aspect of business as well as provide publicity about the unethical firms and their products which would eventually turn them as ethical consumers. They can also try to make the necessary information available to consumers from which the consumers can make a pro ethical choice.

LIMITATION AND FURTHER STUDY

As with most research, this study also has some limitations despite its contribution to some major findings. Firstly the sample size is comparatively small due to the time and cost constraints with 313 respondents where it is difficult to draw the generelisabilty of this research. Moreover the respondents were selected from some geographical areas. The other regions of the country may demonstrate different result regarding the consumers' perceptions towards consumerism issues.

Another limitation is that in this research only one product category was considered i.e. food product. So, the result might differ across the product category. Moreover, this research only highlighted some major fairness issues (micro issues) and one well known macro issue such as environmental consumerism practice. The other issues might represent different results. In addition to these, though the survey has been conducted with great care and best effort, some of the respondents might not found to be honest and sincere in answering the questionnaire on which the researcher does not have any control.

Despite these limitations, the study makes a significant contribution at least to view a general scenario of the consumers' perceptions towards the consumerism issues and its impact on the consumer purchasing behavior in food industry in Malaysia.

From the prior studies it has been found that consumers' exposure on ethics is very limited. This study emphasizes on the major specific fairness issues (micro issues) of consumerism and one macro issue such as environmental consumerism practice; consumers' perceptions on these issues and the effect of these issues on the consumer purchasing behavior where it has been found that both the issues (micro and macro) found to have association with the consumer ethical purchasing behavior. However, further research can be conducted on the other micro consumerism issues such as product quality, product safety, product adulteration, misbranding practice or with the macro issues like health care, tax system, antinuclear issues etc on the consumer behavioral perspective. Moreover, similar study can be conducted in different geographic segment of Malaysia. Furthermore, another comprehensive study can be conducted by covering more disperse population from all 14 states in Malaysia or any other parts of the world.

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ETHICS OF U.S. GOVERNMENT ACTION AND INACTION: IS LOUISIANA BEING TREATED LIKE A COLONY OF THE UNITED STATES?

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ABSTRACT

The entire story of Louisiana in the post-Hurricane Katrina era is not yet written, as the facts and events and ethical issues are still unfolding. At first, it may seem to some that this article is premature, because the whole story of New Orleans and the post-Katrina recovery is years away. Certainly new findings by engineers, economists and investigators are to emerge in coming years which may support or refute some of the conclusions that are considered to be at the forefront of contemporary discussion about who or what lies at fault for the tragedy at New Orleans in 2005.

In this article, three key events are identified which lay outside of the control and influence of the people of New Orleans; these events started New Orleans on an economic death-spiral. These events were the result of direct actions of the U.S. Government. While the breaking-point for New Orleans may be Hurricane Katrina, New Orleans has suffered an ever-increasing burden that the United States Government, by its actions, put upon the city. These three include the Cuba Embargo, Louisiana's share of offshore oil and gas revenues, and U.S. Government-controlled failures associated with Hurricane Katrina.

INTRODUCTION

In the wake of Hurricane Katrina, for many reasons, some in Louisiana wonder if they are somehow something less than a full partner in the United States; in what it is to be part of the United States. A year after the hurricane flooded 80% of the City of New Orleans, despite the U.S. Government approving billions of dollars of aid, the money has by and large not made it to the people. Apathy, Katrina-fatigue, and detachment from the crisis have caused some in the country to turn their collective noses up in the air and ignore the ongoing cries for assistance. Moreover, the politically-connected, no-bid contracts that surfaced in the news seem ripe with at least the air of abuse of some of the funds that have made it to Louisiana. Given the failure of the money to trickle-down to the citizens, they wonder what the U.S. Government's response would have been, had a disaster of the magnitude of Hurricane Katrina befallen Washington D.C., San Francisco, CA, or Boston, MA.

Why should the U.S. Government bear the lion's share of the costs for the Katrina damages? News reports of engineering tests conducted on failed levees *clearly* show the hand of the U.S. Government was in the levees that failed. They hear that the specifications, the design, the mistakes, *were all activities that were totally controlled by the U.S. Army Corps of Engineers*. They ask, from their FEMA travel trailers, from their tents, from their moldy, damaged and crumbling homes, if they are being treated fairly.

The ethical question: *Is Louisiana being treated like a partner, equal to the other 49 states of the United States, or is it being treated as nothing more than a third-world colony; a colony that has served its purpose and is now being abandoned?*

Several key events started New Orleans on an economic death-spiral. These events were outside of the control and influence of the people of New Orleans; they were events spurred by direct actions of the U.S. Government. The breaking-point for New Orleans may be Hurricane Katrina, due to an ever-increasing burden that the Federal Government, by its actions, put upon the city.

- First, we review the Cuba Embargo and its impact upon New Orleans.
- Second, we review Louisiana's share of offshore oil and gas revenues.
- Third, we look at the U.S. Government's failures associated with Hurricane Katrina.
- Finally, we explore the ethical treatment of Louisiana as a state.

THE CUBA EMBARGO

New Orleans has had long and historic ties to Cuba. In his online history of the Archdiocese of New Orleans, Nolan (2001) wrote, "Louisiana became a Spanish colony in the 1760s. Church jurisdiction was transferred to the Diocese of Santiago de Cuba and later Havana." (Para. 1). In 1771 Louisiana became part of the Diocese of Santiago de Cuba. In 1785, Cirilo de Barcelona was consecrated Auxiliary Bishop of Santiago de Cuba with his residence in New Orleans, with his responsibility, Louisiana and the Floridas. In 1787, the Diocese of San Cristobal of Havana is established; Louisiana and the Floridas become part of the new diocese." (Para. 8)

Louisiana's Governor Kathleen Blanco is attempting to reestablish some of the historic trade relationships with Cuba. Varney (2005) summarized the trade, social and economic ties that are part of our shared histories. "At the beginning of the 19th century," Varney wrote, "trade, primarily in coffee, sugar and slaves, meant heavy travel between Cuba and Louisiana. There were periodic exoduses from one place or another, part of a churning of populations between Haiti, Cuba and New Orleans," citing a statement by Ariana Hall, "the executive director of CubaNola, an arts organization that seeks to expand cultural ties between the island and the city"(Para. 4).

The Port of New Orleans enjoyed prominence in previous years as either the no. 1 or no. 2 port in the United States, competing for that honor with the Port of New York. "Ever since the end of World War II, commerce through the Port of New Orleans has steadily increased," per the *New Orleans Port Record* (1960, p.4). New Orleans competed well with most U.S. ports, and the Gulf and South Atlantic ports especially. The Port of New Orleans' ties to Latin American trade were of tremendous importance. "In calendar 1960, the three traditional and leading export commodities of Latin America – coffee, sugar and bananas continued their dominant role, and together accounted for …80% of the total value of Latin American imports to the Port of New Orleans. These also "represented 45% of the total value of all imports at the Port of New Orleans." (Toledano, 1962, p. 11)

The June 1961 (p. 5) issue of the New Orleans Port Record, featured the address of Carlos Todd to a recent Mississippi Valley World Trade Conference. Todd, a native of Cuba. was the former political editor of the *Times of Havana*. He described the events away from New Orleans that changed the dynamic of its Port and the posture of the U.S. in Latin America. His prophetic warnings included perceptions by Latin Americans of U.S. policies toward challenges in the hemisphere.

Policies from Washington D.C., and the Cuba Embargo changed the Port of New Orleans. Trade flourished between Louisiana and Cuba until the Cuban Revolution in 1959. Robins & Trujillo (1999) of Tulane University's Cuban Studies Institute wrote:

> Prior to the revolution in 1959, Cuba had close trading ties with the U.S. Trade was very important to Cuba's economy, accounting for 57 percent of the GNP. The U.S. was Cuba's principal trading partner. In 1958, approximately one third of all goods passing through the Port of New Orleans were destined for Cuba. In 1958, Cuba was Louisiana's number one trading partner in imports and number seven (7) in exports. Imports amounted to 1,232,000 tons consisting of: sugar (988,000); molasses (234,000); vegetable fiber (2,000); fruit (900); and pigment paints and varnishes (900). Exports amounted to 269,000 tons consisting of: flour (51,000); chemicals (36,000); grain (35,000); vegetables (27,000); animal feed (22,000); and lumber (20,000). As Louisiana's largest single trading partner, over 6,000 Louisianians were employed in Cuba-related commerce. During this time, in the service sector, approximately 85% of Cuba's business was done with the U.S., most notably in the areas of banking and insurance. Likewise, 85% of foreign tourists visiting Cuba were United States citizens. (Paragraph 8)

Past issues of the New Orleans Port Record, a monthly journal of the *Port of New Orleans*, provide insight to its operations. Examination of past issues illustrates changes were taking place timed to the problems with Cuba. In the June 1961 issue (p. 64), the Monthly Report, Port of New Orleans showed that from May 1960 to May 1961, Total Cargo was down 23%; Inbound cargo was down 23% and outbound was down 25%. The schedule of sailings from the Port of New Orleans, January 15 through February 28, 1961, (New Orleans Port Record, March 1961, p. 58) showed a ship of the Cubamar Line sailing every Friday. The February 15 through March 31, 1961 schedule of sailings (New Orleans Port Record, April 1961, p. 58) and those thereafter do not show that listing again.

It appears that the loss of Louisiana's no. 1 trading partner, and the loss of the no. 3 destination of the Port of New Orleans, created a ripple effect. Table 1, featuring data from the U.S. Census Bureau, shows population trends of the State of Louisiana, and the parishes of East Baton Rouge, Jefferson, and Orleans. From 1900 – 2000, the State of Louisiana and East Baton Rouge show continuous growth. From 1900 – 1960, all four indicators showed growth. However, after 1960, Orleans Parish showed continuous losses in population per decade, while neighboring Jefferson Parish showed only one decade of loss, but an overall gain in population for the period.

Table 1: Population of Counties by Decennial Census: 1900 to 2000

	State Of Louisiana	Louisiana Gain or Loss *	Parish of East Baton Rouge	East B.R. Gain or Loss *	Parish Of Jefferson	Jefferson Gain or Loss *	Parish Of Orleans	Orleans Gain or Loss *
1900	1,381,625	n/a	31,153	n/a	15,321	n/a	287,104	n/a
1910	1,656,388	274,763	34,580	3,427	18,247	2,926	339,075	51,971
1920	1,798,509	142,121	44,513	9,933	21,563	3,316	387,219	48,144
1930	2,101,593	303,084	68,208	23,695	40,032	18,469	458,762	71,543
1940	2,363,880	262,287	88,415	30,207	50,427	10,395	494,537	35,775
1950	2,683,516	319,636	158,236	69,821	103,873	53,446	570,445	75,908
1960	3,257,022	576,506	230,058	71,822	208,769	104,896	627,525	57,080
1970	3,641,306	384,284	285,167	55,109	337,568	128,799	593,471	<34,054>
1980	4,205,900	564594	366,191	81,024	454,592	117,024	557,515	<35,956>
1990	4,219,973	14,073	380,105	13,914	448,306	<6,2986>	496,938	<60,577>
2000	4,468,976	249,003	412,852	32,747	455,466	7,160	484,674	<12,264>

1900-1990 data from: "Population of Counties by Decennial Census: 1900 to 1990", located: http://www.census.gov/population/cencounts/la190090.txt
2002 data from: U.S. Census Bureau State & County Quickfacts, located: http://quickfacts.census.gov/qfd/states
* Losses indicated with "< >"

Prior to U.S. government policy changes toward Latin America in the 1960's and the Cuba Embargo, the Port of New Orleans was set for continued growth and expansion. The Mississippi River-Gulf Outlet (MRGO), known the Mister Go in New Orleans, opened on Thursday, July 25 1963. It was touted as New Orleans' second "Gateway to the Sea" and was seen as a "shorter route between the Gulf of Mexico and the heart of the nation's busiest port," (New Orleans Port Record, August 1963, p. 4).

The Cuba embargo since its inception proved to be a mixed-bag of success and failure. It has shown to be an inconsistent policy. Tyree (1997, p. A17) "…we're doing business like gangbusters with Communist China, which still has the same party and system of government in power that it had in the …1950's," while not doing business with our Communist neighbor 90 miles to the south.

Until the Cuba embargo by the U.S. government, New Orleans enjoyed an ongoing commercial and cultural tie to Cuba. This Cuba-New Orleans relationship was important not only to the city itself but to the entire state of Louisiana. Thus, an ethical issue*: If U.S. foreign policies in Latin America in general, and toward Cuba in particular, are at the root of the depopulation and economic downturn of New Orleans, is there an ethical responsibility on the part of the United States to repair the damage? Is this part of a trend of inequitable treatment of New Orleans and the state of Louisiana?*

LOUISIANA'S SHARE OF OFFSHORE OIL AND GAS REVENUES

On August 13, 2005, Scott Angelle, Secretary of the Louisiana Department of Natural Resources testified before the U.S. House of Representatives' Committee on Resources. In his testimony, he said:

> Louisiana has a long and distinguished history of oil and gas production, both on and offshore. Currently, approximately 34% of the nation's natural gas supply and almost 30% of the nation's crude oil supply is either produced in Louisiana, produced offshore Louisiana, or moves through the state and its coastal wetlands…Together with the infrastructure in the rest of the state, this production is connected to nearly 50% of the total refining capacity in the United States.
>
> The offshore area beyond 3 miles from Louisiana's coast is federal territory. Other than in a 3-mile transition zone, the federal government receives all of the mineral revenue from production in the Outer Continental Shelf (OCS).

Based upon 2004 data, OCS production off Louisiana's coast constitutes 91% of oil and 75% of natural gas production from all U.S. OCS areas combined. Louisiana OCS territory has produced 88.8% of the 14.9 billion barrels of crude and condensate and 82.3% of the 150 trillion cubic feet of natural gas ever extracted from all federal OCS territories since the beginning of time.

Little did anyone know on August 13, 2005 that merely a couple of weeks later, Hurricane Katrina (August 29, 2006) would be the worst natural disaster to hit the Gulf Coast and the state of Louisiana. Tidal surges, now had unfettered access to populated areas, because of the disappearance of hundreds of square miles of coastal marshes and barrier islands. Much of this disappearance stems from saltwater intrusion of fresh-water marshes thanks to canals dug to serve the oil and gas industry. Hurricane Katrina flooded vast areas of south Louisiana, including in particular the City of New Orleans and the parishes of St. Bernard, Plaquemines, Jefferson and St. Tammany.

On September 7, 2005, Scott Angelle was again in Washington, D.C., appearing before the U.S. House of Representatives Committee on Energy and Commerce hearing on Hurricane Katrina's effect on gasoline supply and prices. He raised the issues of the disparity when landlocked states like Wyoming, New Mexico and Colorado host drilling on federal lands onshore, they receive 50% of the revenues in direct payments, thus receiving revenues to support the drilling infrastructure. In contrast, coastal states provide the infrastructure for OCS drilling on federal lands, but they receive little compensation to fund their support. Angelle testified, "…for example in 2001, of the $7.5 BILLION in revenues produced in the federal OCS area, only a fraction of one percent came back to those coastal states." He further testified that, "Production off Louisiana shores alone contributes an average of $5 BILLION dollars a year to the federal treasury, its second largest source of revenue."

Louisiana and other Gulf Coast states bear the cost for infrastructure but do not receive the same revenue sharing as other states hosting drilling on federal lands. Thus, an ethical issue*: If Louisiana bears the costs for hosting the oil and gas industry on federal lands, should it receive the same revenue share as other states which provide this hosting – but on federal lands of a different composition? Is this part of a trend of inequitable treatment of New Orleans and the state of Louisiana?*

U.S. GOVERNMENT FAILURES ASSOCIATED WITH HURRICANE KATRINA

U.S. Army Corps. Of Engineers

This information is still being determined and discussed. In short, levee systems designed and supervised by the federal government, along with federal wetlands policies left Louisiana and especially the City of New Orleans vulnerable. Bodies floated in the streets. Homes and businesses flooded. A year after the hurricane, much of New Orleans looks like it did after the storm waters receded.

The failure of the United States Army Corps of Engineers to properly design and build levees which were in their care and custody caused the loss of thousands of lives, and billions of dollars in damage. Warrick & Grunewald (2005), at a point eight weeks after Katrina stuck New Orleans identified that the three major levee breeches looked, "Less like acts of God and more like failures of engineering that could have been anticipated and very likely prevented" (p. A01). Stromberg (2006) identifies the (U.S. Army) Corps as having supervised the design and construction of the failed levee system in the 1960's (p.2). Vartabedian (2006) describes an unheeded report from the

1980's that the US Army Corps. of Engineers in the 1980's conducted tests and knew at that time that levees in New Orleans would fail, citing a study by the National Science Foundation that pointed to an unheeded study by the Corps. of their own work. In the tests by the Corps., a sample wall tilted and opened a gap when put under hurricane-type forces, much like the failures of the actual levees in New Orleans (p.4). According to U.S. Congressman Bill Jefferson, "The Army Corps of Engineers has acknowledged that they failed the people of New Orleans and the Gulf Coast who trusted that the levees the corps built would keep us safe. Unfortunately, the designs were flawed, leaving us vulnerable to the high winds and high tides of Hurricane Katrina," (Alpert, 2006 p. 9). Congressman Jefferson has filed a bill titled, "Federal Engineering Accountability Act of 2006, which would waive immunity from lawsuits enjoyed by the U. S. Army Corps of Engineers since 1928 (p.9). The United States Senate passed a bill requiring independent oversight of the U.S. Army Corps. of Engineers in the aftermath of the failures of the New Orleans area levees during Katrina (Alpert 2006 p.1) In addition to potential litigation against the U.S. Government if the barriers to litigation are lifted, contractors are concerned about their own exposure to lawsuits. Landers (2006) states, "many public officials and government agencies enjoy sovereign immunity," but expressed concerns of contractors who, "might be held liable for work it conducts at the behest of government entities" (p. 2). *If Louisiana was told to rely upon Federal levees, and if evidence shows that the Corps. knew years in advance that the levees would fail, is there an ethical responsibility of the U.S. Government to make those entities which experienced losses whole again? Is this part of a trend of inequitable treatment of New Orleans and the state of Louisiana?*

Federal Aid

Despite bearing the brunt of houses damaged, Mississippi is getting more money for housing from the Federal government than Louisiana. Post-Katrina Federal grant money for housing shows a huge disparity: Louisiana has received \$6.2 Billion with 204,737 homes with major or severe damage while Mississippi has received \$5.3 billion with 61,386 homes with similar damage (Russell, 2006, p. 1). These concerns about the distribution of Federal funds have been attributed to the relative political strengths of the states receiving aid, but also reflects a growing nation-wide sentiment that Louisiana's politicians have handled their responsibilities poorly. Indeed, large amounts of Federal Aid seems wasted. Nevertheless, a disparity of aid and treatment does exist. *Is it fair that the distribution of Federal disaster relief funds flows disproportionately between and among states? Is this part of a trend of inequitable treatment of New Orleans and the state of Louisiana?*

CONCLUSION

This paper presents several reasons to ask if New Orleans and the State of Louisiana have been treated equitably. The impact to Louisiana of the Cuban Embargo, Louisiana's disproportionate share of oil and gas revenues hosted on Federal lands (that happen to be OCS lands), and the failed levees and wetlands policies have us ask: Is Louisiana being treated as an equal state to the other 49 states in the Union, or is Louisiana in fact or in essence a colony – a resource to enrich the Federal treasury? If a disaster of the scale of Hurricane Katrina had hit Texas or Massachusetts or New York, given the failures of Federal systems and levees and the massive losses of life and property, would the Federal response have been different?

The disproportionate hardships imposed upon Louisiana by the United States via the Cuban Embargo when the Port of New Orleans lost a major shipping destination; the expectation of Louisiana to bear the burden of hosting offshore oil exploration efforts without sharing in the royalties from those efforts, and most recently, the catastrophe of the levee failures and the aid after Hurricane Katrina all indicate that Louisiana is not receiving ethical, fair treatment by the U.S. government. The census figures illustrate that New Orleans has not kept pace in population with the rest of Louisiana, with its neighboring Jefferson Parish, nor with its rival in size, Baton Rouge. The downward spiral is traced to the era of the Cuba Embargo, which started the process. Katrina in 2005 may be the *coup de gras*.

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GOVERNMENT REGULATION OF ACCOUNTANTS: THE PCAOB ENFORCEMENT PROCESS

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ABSTRACT

In 2002 the federal government altered the landscape of the accounting profession by creating, for the first time, a federal regulatory agency for this profession: the Public Company Accounting Oversight Board (PCAOB). Congress responded to the massive corporate failures of Enron, Tyco and others by enacting the Sarbanes-Oxley Act (SOA), to improve corporate governance and the reliability of financial information. Sarbanes-Oxley created the PCAOB to oversee the work of public accountants, the creators of corporate financial information.

The purpose of this paper is to provide insight and understanding into the PCAOB's enforcement process. This is important to public accounting students and practitioners. By gaining insight into how and why the PCAOB regulates as it does, needless conflict can be avoided and a constructive, mutually beneficial relationship will likely ensue.

This paper begins with an overview of government regulation, in order to show how the PCAOB fits into the general context of regulation. Then we review the Sarbanes-Oxley Act, which created the PCAOB. Next we consider the PCAOB, noting its unique features. The paper then describes and analyzes the PCAOB's enforcement mechanisms. Finally we conclude with recommendations as to how accountants can most constructively interact with the PCAOB.

INTRODUCTION

When President Bush signed the Sarbanes-Oxley Act (SOA)[1] in 2002 he stated that it created "the most far-reaching reforms of American business practices since the time of Franklin Delano Roosevelt"[2]. The SOA was a federal response to the massive corporate failures of Enron, Tyco and others. These failures were caused, in part, by accounting failures that had misrepresented the financial condition of some corporations. When the truth came out these corporations collapsed, causing losses to investors estimated at between $300 billion[3] and $500 billion[4]. Investor confidence in our capitol markets was shaken. In order to restore that confidence, and to make financial information more reliable, Congress passed the SOA by an overwhelming majority: 423 to 3 in the House of Representatives, and 99 to 0 in the Senate[5].

Accounting failures contributed to the recent crisis in investor confidence, but they were not the only cause of it. Some corporate managers contributed by "cooking the books" in order to increase stock prices so that they could collect inflated performance-based bonuses and profit from their stock options. Some securities analysts contributed by touting questionable securities because their broker-employers were selling them. And some public accounting firms contributed by performing substandard audits because they were not sufficiently independent and because they did not want to lose profitable non-audit business[6]. Add to this mix the bursting of the tech stock bubble, and a perfect storm of shaken investor confidence ensued.

Sarbanes-Oxley attempts to correct the various causes of this post-Enron crisis in confidence. To improve corporate governance, new independence requirements were established for corporate board audit committees; new internal control systems were mandated; corporate loans to management were prohibited; new attestation statements and signatures[7] by Chief Executive Officers (CEO)s and Chief Financial Officers (CFO)s were required for reports to the Securities Exchange Commission (SEC); and penalties for fraud were increased. Securities analysts' conflicts of interest were addressed by requiring a wall of separation between the sales staff of a brokerage firm and its analysts, and by prohibiting a brokerage firm from punishing an analyst who issued a negative report on a security. Analysts were also required to disclose their own holdings of the securities they were reporting on.

But the most sweeping changes wrought by Sarbanes-Oxley were reserved for public accountants. This profession performs the essential function of certifying that the financial information issued by public companies is accurate. Investors in our capitol markets rely on this financial information to make decisions. Without this reliance and trust our capitol markets could not function effectively. Our economy, which depends upon the health of our capital markets, would be significantly impaired.

In order to restore investor confidence by assuring more reliable certification of financial information, the SOA did two things: Title I of the Act created the Public Company Accounting Oversight Board (PCAOB or Board), a new government regulatory agency to oversee the work of public accountants; Title II enacted new auditor independence requirements to prevent conflicts of interest and undue influence by management in the auditors' work.

The PCAOB was a radical departure from past practice. Until the SOA, the accounting profession had been largely self-regulating[8]. The profession's national organization, the American Institute of Certified Public Accountants (AICPA) administered numerous self-regulatory organizations such as the Public Oversight Board (POB), whose task was to oversee the work of public accountants. But self-regulation by the profession was not entirely successful. The POB had no authority to sanction auditors for deficiencies or incompetence. In 2002 the POB voted unanimously to dissolve itself[9], feeling that it was unable to fulfill its mission with its limited authority[10]. Among other problems, the POB had been unable to get support for its plan to review the Big 5 accounting firms' compliance with auditor independence standards.

This paper focuses on Title I of Sarbanes-Oxley, the PCAOB, and more specifically on its enforcement process. As will be more fully described below, regulatory agencies operate by first promulgating rules or regulations and then by enforcing those rules. It is very useful for those being regulated to understand this regulatory process. Every public accountant will eventually come into contact with the PCAOB and its staff. With understanding, needless conflicts can be avoided and a smooth, mutually beneficial relationship can be maintained.

Unfortunately, as the business education publication BizEd[11] pointed out in August 2005, there is a shortage of useful educational material on the PCAOB and its enforcement process. The purpose of this paper is to help fill that need.

We begin with an overview of government regulation, in order to show how the PCAOB fits into this context. Then we review the Sarbanes-Oxley Act, which created the PCAOB. Next we consider the PCAOB, noting its unique features. The paper then describes and analyzes the Board's inspection process, probably its most important enforcement mechanism. Separate sections follow, describing and analyzing the Board's investigative process and its disciplinary process. The legal rights of parties appearing before the Board are noted. Finally, conclusions are drawn regarding how accountants can best to interact with the PCAOB.

OVERVIEW OF GOVERNMENT REGULATION

The PCAOB is one of many regulatory agencies in the U.S. All agencies share a great many common features, so an understanding of regulation in general will help to understand the PCAOB in particular. Government regulation comes about as a legislative response to the electorate's demand that the government "fix" a serious public problem. For example, in 1929 the stock market crashed. The Dow Jones Industrial Average dropped from 381 in 1929 to 41 in 1932, losing 89% of its value[12]. Fortunes were lost and the crash ushered in the Great Depression. The stock market crash was caused in part by fraud and manipulation of securities. The federal government wanted to correct these problems, and to be seen as actively addressing the causes of the terrible economic depression gripping the nation.

Congress' response was to pass the Securities Acts of 1933[13] and 1934[14], which imposed new financial reporting and disclosure requirements and prohibited certain practices such as insider trading. But administering the provisions of these securities acts required collecting a vast amount of financial information from thousands of companies, reviewing it, and sometimes bringing enforcement actions in federal court. This work required a great deal of time and also the expertise of lawyers, accountants, securities professionals and administrators. Congress had neither the capacity nor the inclination to do this work itself, so it created an administrative agency to do it, the Securities Exchange Commission (SEC). This new agency first needed to take the general language of the securities acts and translate it into specific regulations that could be administered. Then it hired enforcement staff to ensure compliance with those regulations.

This is the pattern of all federal and state regulation: the public perceives a problem (sometimes a crisis); the legislature passes a new statute to remedy the problem and it also creates an agency to administer the remedial statute; the agency then translates the general provisions of the statute into specific rules or regulations and then enforces them. The agency is central and essential to regulation.

New government regulation is often controversial because it interferes with previously unrestricted private conduct. The antitrust laws might prevent a merger, or the Environmental Protection Agency (EPA) might require expensive waste water treatment. There is also a political aspect to people's response to regulation. Political conservatives generally disfavor regulation, at least in the economic or business sector. They point to compliance costs and diversion of management attention from central business issues. Conservatives prefer market solutions. Political liberals typically favor regulation, believing that improving society is a proper role of government. Liberals focus on the benefits of regulation and they have less confidence in market solutions.

This pattern of conservative opposition or liberal support for regulation was particularly evident in the 1930s with Franklin Delano Roosevelt's New Deal. At that time an alphabet soup of new federal regulatory agencies emerged to combat the great depression: the Securities Exchange Commission (SEC), Works Progress Administration (WPA), Tennessee Valley Authority (TVA), Social Security Administration (SSA) and many others. With the proliferation of these agencies in the 1930s many became concerned that regulatory agencies had become a "fourth branch of government". This new branch was thought by some to have excessive unchecked power and was therefore a threat to our system of limited government. U.S. Supreme Court Justice Robert Jackson stated, in the case of FTC v. Ruberoid[15], that agencies "have become a veritable fourth branch of government, which has deranged our three-branch legal theories".

This criticism is not without some basis. Our American constitutional system, which has admirably preserved our essential freedom for over 200 years, is based in part on the principle of separation of powers. This principle holds that if the executive authority of government is separate from the legislative authority, and the judicial authority is also separate, then each power of government will check and balance the others, preventing the emergence of a tyrant[16]. James Madison, one of the authors of our Constitution, makes this case in Federalist Number 47.

However, regulatory agencies combine the three powers of government. They violate the separation of powers principle. When regulatory agencies promulgate rules that have the force of law, they are performing what is essentially a legislative function. When regulatory agencies enforce their rules or regulations, they are performing what is essentially an executive function. And when they hold hearings and decide cases to determine whether their rules have been violated, agencies are performing what is essentially a judicial function.

This conflation of the powers of government by regulatory agencies has been troubling from the beginning. There is certainly the potential for abuse. Concern increased during the 1930s, with the proliferation of agencies under the New Deal.

By 1946 it became apparent that there was a need to limit the powers of agencies. Congress responded by passing the federal Administrative Procedure Act[17] of 1946. This Act discourages agency abuse by requiring them to follow certain procedures. For example, when making a new rule, the agency must first publish the proposed rule in the Federal Register and then wait during a comment period for public response. Hearings within an agency must provide a modicum of due process (although far less than in a civil or criminal trial). This includes providing a decision-maker called an administrative law judge who is kept separate from the prosecutorial arm of the agency. Appeals to the federal courts are provided for, but only after "final agency action" (APA Section 704). This allows the agency an opportunity to correct its mistakes before it is taken to court. All federal agencies must comply with the Administrative Procedures Act's requirements, just as private parties must comply with the agencies' rules.

In addition to the APA's curbs on agency abuse there is oversight by the three traditional branches of government. The President can remove directors of some agencies at his or her pleasure; Congress can enact new legislation that curbs the budget or authority of "rogue" agencies or it can even eliminate them entirely. The courts can overturn agency decisions that are arbitrary, that exceed statutory authority, or that violate proper procedure. Between oversight by the three traditional branches of government and the procedural guarantees of the APA, it is generally agreed[18] that abuse of power by regulatory agencies has been largely avoided. Nevertheless, and particularly with the emergence of a controversial new regulatory agency, the old criticisms and concerns sometimes re-emerge.

THE SARBANES-OXLEY ACT (SOA)

The SOA fits squarely into the pattern of government regulation described above. It was a legislative response to a crisis in public confidence that threatened to undermine our capital markets and our economy. The public demanded reform, and Sarbanes-Oxley was enacted with almost unanimous support from Congress. This Act contains nine Titles. Title I established the Public Company Accounting Oversight Board (PCAOB or Board). This will be described in greater detail in the next section. Title II strengthens auditor independence, prohibiting acts that may lead to conflicts of interest, for example simultaneously performing audits and lucrative non-audit work such as consulting. SOA Section 201 provides a list of prohibited activities including bookkeeping, appraisal, management of human resources, legal services and "any other service that the Board determines, by regulation, is impermissible". SOA Section 203 requires that the lead audit partner can not remain in that position for more than five years, for fear of a too-close relationship developing between the lead auditor and corporate management.

Title III seeks to improve corporate management responsibility. SOA Section 301 requires that corporate boards of directors establish audit committees composed of independent directors – those not otherwise connected to the corporation or who receive fees from the corporation. SOA Section 302 requires that corporate chief executive officers (CEO)s and chief financial officers (CFO)s sign their companies' annual and quarterly reports to the SEC. They must certify that they have reviewed the report and that, "…based on the officer's knowledge, the report does not contain any untrue statement of a material fact…"

Title IV continues to strive to improve management responsibility. To avoid conflicts of interest between executive officers or directors and the corporation, SOA Section 402 prohibits personal loans from the corporation to those individuals. SOA Section 404 requires that each annual report required by the Securities Exchange Act of 1934 must include an internal control report. This is a new requirement, and has probably attracted more criticism and complaint than any other single section of the SOA. This may be because Section 404 causes companies to incur significant additional compliance costs[19].

Title V addresses securities analyst conflicts of interest. SOA Section 501 requires that analysts disclose their own investments in corporations they are reporting on. This Section also requires brokerage firms to "establish structural and institutional safeguards" to separate their securities dealers from their analysts. Brokerage firms are prohibited from retaliating against an analyst who issues "an adverse, negative, or otherwise unfavorable research report" on securities the firm is selling.

Title VIII increases the penalties for corporate fraud. SOA Section 802 makes intentional destruction or falsification of records a federal felony when done "with the intent to impede, obstruct, or influence the investigation or proper administration of any matter within the jurisdiction of any department or agency of the United States…". The maximum penalty is imprisonment for 20 years. SOA Section 806 provides whistleblower protection. SOA Section 1107, in Title IX, makes retaliation against whistleblowers a federal felony, punishable by imprisonment for up to 10 years.

THE PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD (PCAOB)

As PCAOB Board Member Daniel Goelzer stated[20] "the Sarbanes-Oxley Act ended the profession's long tradition of self-regulation and peer review. In its place, the Sarbanes-Oxley Act created the Public Company Accounting Oversight Board." The Board consists of a Chair and four other Board Members, selected by the Securities Exchange Commission. This new regulatory agency was created to administer the accounting provisions of the SOA. The PCAOB follows the general pattern of agency action described earlier: hiring experts, promulgating rules, and setting up an enforcement mechanism for those rules.

Several features of the PCAOB are note-worthy. It is an "independent" agency, in that its board members are appointed for fixed terms as opposed to serving at the pleasure of the President. SOA Section 101(e) provides that the five Board members shall be selected by the SEC in consultation with the "Chairman of the Board of Governors of the Federal Reserve System and the Secretary of the Treasury". PCAOB Board Members may not be removed before the expiration of their terms except for "good cause shown".

The PCAOB is more independent than most other independent agencies in that its funding comes from an independent source and not from Congress. SOA Section 109 provides that the funding of the Board shall come from "annual accounting support fees" levied on corporate issuers in proportion to their "equity market capitalization". We observed earlier in the section titled "An Overview of Government Regulation" that oversight by Congress is one traditional means of controlling agencies and preventing abuse. Congress controls the purse-strings, and sets the budget of each agency annually. If an agency has aroused the ire of Congress, it can cut back that agency's budget. Agencies, being bureaucracies, strenuously try to avoid this. However, if an agency has independent funding, it is immune from such cutbacks. Very few agencies enjoy this privileged status, but the PCAOB is one that does. Greater independence makes the agency less responsive to political pressures.

Another note-worthy feature of the PCAOB is that its status is somewhat unclear. SOA Section 101(b) provides that the Board shall be a private "non-profit corporation" not "an agency or establishment of the United States Government". This is not a mere academic distinction. The Administrative Procedure Act (APA), which requires that agencies follow procedures that assure certain rights of affected parties, only applies to federal government agencies. If the PCAOB is not such an agency, then the APA does not apply. In addition, the Constitutional protections of the Fourth Amendment, which prohibit unreasonable searches and seizures, apply to government agencies but not to private corporations. This could be important in future litigation.

In deciding whether the PCAOB is an agency within the contemplation of federal law we may examine its authority and operation. If it looks like an agency and acts like an agency, then a federal court will likely rule that it is an agency. It is beyond dispute that the PCAOB was established by the federal government, specifically by the Sarbanes-Oxley Act. Moreover, the Board is controlled by and reports to the SEC, indisputably a federal agency. Its members are appointed by the SEC, with consultation from other federal agencies. SOA Section 104(a) authorized the Board to establish rules for inspections and to "conduct a continuing program of inspections" to assure compliance with the Act. SOA Section 105 authorizes the Board to establish rules for investigations and to conduct investigations. This Section also provides that the Board may request issuance of a subpoena from the SEC. SOA Section 105(c)4 gives the PCAOB authority to "impose such disciplinary or remedial sanctions as it determines appropriate", including suspension or revocation of registration, without which a public accounting firm can not do public company audit work. Sanctions can also include fines of up to $15 million. SOA Section 107 provides for SEC review of disciplinary action taken by the Board. In effect the PCAOB reports to the SEC. The decisions of the SEC with regard to Board actions constitute final agency action from which an adversely affected party can appeal to federal court.

Even though Sarbanes-Oxley describes the PCAOB as a private "non-profit corporation", we see that it was created by the federal government and it has the same authority, and behaves in the same manner as does a typical government regulatory agency. It is therefore reasonable to conclude that a future federal court will probably regard it as such, and require that it comply with the provisions of the Administrative Procedure Act and other federal law.

PCAOB ENFORCEMENT

As noted earlier, the PCAOB uses three separate enforcement mechanisms: inspections, investigations and disciplinary actions. Inspections are usually routine and do not indicate the presence of any problem. However, if irregularities are discovered by the inspection, then the next mechanism, an investigation, will ensue. The investigation will focus on perceived problem areas, and may include requesting or subpoenaing witnesses or documents. If the investigation leads the PCAOB to conclude that a violation has occurred, and the accounting firm has not corrected or undertaken a plan to correct the violation, then the next mechanism, disciplinary action, follows. Disciplinary action takes the form of a hearing followed by the possible imposition of sanctions which can include suspension or revocation of the accounting firm's registration and substantial fines.

The PCAOB appears to be mindful of its ground-breaking role as the first federal government agency to regulate the accounting profession. It has adopted a "soft" approach to enforcement, preferring to guide public accounting firms and to assist them towards compliance rather than by wielding its sanctions in an aggressive manner. This was described as a "supervisory approach" in the PCAOB Release of March 21, 2006. This releases states[21]:

> The Board takes a supervisory approach to oversight and seeks through constructive dialogue to encourage firms to improve their practices and procedures.

The Release goes on to state "Overall, both the effectiveness and efficiency of the Board's programs are enhanced when firms opt for constructive engagement rather than an adversarial approach." The PCAOB Annual Report for 2005, released August 2006 confirms[22] this approach.

This "soft" supervisory approach to regulation was more fully described by PCAOB Board Member Daniel Goelzer in a speech on December 12, 2005. He stated[23]:

> That brings me to the fundamental point I would like to make regarding our enforcement program. The Board's enforcement philosophy is modeled on what we have called the "supervisory approach" to regulatory oversight. As long as we believe that an auditing firm is acting in good faith and is capable of and willing to conduct audits in accordance with the PCAOB's standards, we will generally use our authority to make non-public recommendations, rather than our authority to bring disciplinary actions.

The supervisory approach taken by the Board is remarkably conciliatory and non-confrontational. Time and again, as will be seen below, accountants are given a second chance, even a third chance to avoid sanctions or even public criticism by indicating a good-faith effort to comply. Sometimes merely undertaking additional training or education is all that the Board requires.

This soft approach by the PCAOB might be due to several factors. First, the Board is regulating members of a learned profession, one that has a proud history. The Accounting profession understands its key role in American society. This is evidenced by the remarks of former Chairman of the AICPA Board of Directors Bob Bunting, who stated in his acceptance speech[24] in October 2004:

> Fundamentally, great professions play a vital role in the health of our economy and society. Each of you—whether you work in academia or government, for a corporation or in a public accounting firm—is involved in the process of providing understandable, reliable and transparent information for decision-makers. This role is vital to our society and its economy. It is in our interest as a profession to ensure this function's integrity, fairness and relevance.

Another reason for the soft enforcement approach taken by the PCAOB may be that it appreciates the drastic nature of the step taken by Sarbanes-Oxley in instituting, for the first time, federal government regulation of a profession that had, until then, been largely self-regulating. It is natural to expect push-back from some accountants who resent the federal intrusion. For the PCAOB to be successful it needs the cooperation of the profession. Likewise, for the profession to be successful and to regain public confidence following the Enron debacle, it is helpful to be seen as partnering with a federal agency closely associated with the Securities Exchange Commission. There is every reason to view the relationship as symbiotic. Let us now take a closer look at the PCAOB's enforcement mechanisms. Inspections, investigations and disciplinary actions are described and discussed in separate sections.

THE PCAOB INSPECTION PROCESS

Of the PCAOB's three enforcement mechanisms, inspections are probably the most important. All public accounting firms will be inspected, once each year for larger firms and at least once every three years for smaller firms. The Board recognizes the importance of its inspection program. PCAOB Board Member Charles Niemeier stated[25] in 2006 that "our inspection program is the core of our supervision of registered firms". Board Member Daniel Goelzer stated[26] in 2006 that "the Board is fundamentally an inspection body". The largest single group of employees of the PCAOB is in the inspections division[27]. In 2005 the Board conducted inspections of 281 registered accounting firms[28].

Before discussing the specific provisions of Sarbanes-Oxley and the PCAOB's Rules promulgated to administer those provisions, it is useful to consider the general approach taken by the PCAOB in its inspection process. An inspection of a public accounting firm usually starts with an assessment of that firm's "tone at the top".

Tone at the top refers to top management's attitudes and behavior regarding regulatory compliance and ethics. It would be hard to overestimate the importance the PCAOB inspectors place on positive tone at the top. If the inspection team determines that the tone at the top is positive, it will feel a reduced need to make in-depth inspections of specific audits.

The accounting profession recognized the importance of determining tone at the top long before passage of the Sarbanes-Oxley Act[29]. In 1987, the National Commission on Fraudulent Financial Reporting (the Treadway Commission) issued a report that concluded that the tone set by top management was critically important in creating a healthy financial reporting environment[30].

In a 2004 speech[31] given by Director of the Division of Enforcement of the SEC Stephen Cutler, he emphasized the importance of a healthy tone at the top. He suggested several ways in which top management could act to provide it. These include complying with the "letter and spirit of the rules", taking "good moral character" into account when hiring new employees and making "integrity, ethics and compliance part of the promotion, compensation and evaluation process". Mr. Cutler pointed out that

> It speaks volumes when a company fires or suspends a rainmaker or other important employee for an ethical breach; and just as importantly, it speaks volumes when a company doesn't.

Mr. Cutler also gave useful examples of firms which had failed to provide healthy tone at the top. He reported that at Enron, senior managers conducted a skit in which one of the themes was deceiving the SEC. At Hollinger, CEO Conrad Black wrote an email in which he referred to his company's shareholders as "a bunch of self-righteous hypocrites and ingrates."

Another aspect of the PCAOB's general approach is that inspectors conduct what has been described as a "risk-based" inspection. Inspectors do not focus their attention equally on all areas of a public accounting firm's work. They focus on those areas which seem to carry the most risk. As the PCAOB Annual Report for 2005[32] explains:

> The PCAOB uses a risk-based approach to performing its oversight programs. For example, the PCAOB's inspections teams identify audits for review based on an evaluation of the risks of misstatements or omissions in financial reporting, and they further maximize the effectiveness of their reviews by selecting the portions of those audits that are likely to pose the most challenging audit issues.

Using this risk-based approach, inspectors would not randomly select audits to review. Instead they would look for high-risk audits. An example of a high-risk audit might be an audit of a company that had a troubled history of SEC compliance. Another example might be an audit of a company that other public accounting firms had declined to work for.

We now turn to specific provisions of the Sarbanes-Oxley Act and the PCAOB Rules. Section 104 of the SOA authorizes the PCAOB to conduct inspections and describes the Board's inspection procedures. As noted earlier, regulatory agencies take the general language of a statute and translate it into specific rules or regulations that can be administered. The PCAOB has accordingly promulgated PCAOB Rules 4000-4012 to define and apply the provisions of SOA Sec. 104. The SOA statutory provisions and PCAOB Rules are conveniently available online at the PCAOB's website, www.pcaobus.org.

SOA Sections 104(a) and 104(b), and PCAOB Rules 4000-4004 describe "regular inspections" and "special inspections" by the Division of Registration and Inspections of the PCAOB. Regular inspections are routine inspections required of all registered accounting firms doing audits of public companies regulated by the Securities Exchange Commission (SEC or Commission). Large accounting firms, auditing "more than 100 issuers" (corporations that issue securities) must be inspected annually, while smaller accounting firms need only be inspected at least once every three years. However, in addition to the Rule 4001"regular inspections", the Board may also conduct Rule 4002 "special inspections". SOA Section 104(b)2 states that the PCAOB may conduct these special investigations "at the request of the Commission or upon its own motion". The Rules do not elaborate on what the proper basis for a special inspection should be. Rule 4002 does emphasize however that "the Board may authorize a special inspection on its own initiative". An appropriate basis for a special inspection might be a "tip" that an auditor is in violation of a PCAOB rule or standard. The Board has actively sought such tips by setting up a tip hotline[33] with which informants can transmit information anonymously if they wish. They can email the Board at tips@pcaobus.org or telephone the confidential tip line at (800) 741-3158.

SOA Sections 104(c) and 104(d) and PCAOB Rule 4004 describe the procedure to be followed during a PCAOB inspection. Inspectors are given exceptional latitude to inspect for "any act or practice or omission … that may be in violation of this Act, the rules of the Board, the rules of the Commission, the firm's own quality control policies, or professional standards". Note that an accounting firm's own policies, as expressed in a handbook or manual, could be used against an accountant working for that firm, even if the violation or omission is not prohibited by Generally Accepted Accounting Principles (GAAP) or Generally Accepted Auditing Standards (GAAS). Moreover, the Board can enforce "professional standards" which also might not be specifically addressed by GAAP or GAAS. However, as noted above, the Board has taken a "soft" approach and is unlikely to use this broad discretionary authority in an aggressive manner.

A problem arises however, because PCAOB Rule 4006 titled "Duty to Cooperate With Inspectors" requires registered public accounting firms and "every associated person of a registered public accounting firm" to cooperate with the inspection. This cooperation includes providing "information by oral interviews, written responses, or otherwise" and also providing access to any records in the "possession, custody or control" of the firm or person. Non-cooperation can result in suspension or revocation of the firm's registration.

This is not a small matter, and it raises a Constitutional issue[34]. What if a PCAOB inspection reveals evidence of criminal activity, such as embezzlement or bribery, to which the accountant has been a party? Does the Constitutional privilege against self-incrimination, contained in the Fifth Amendment, protect an accountant who refuses to give self-incriminating testimony? The Board has anticipated this problem, and addressed it in its September 29, 2003 Release[35]:

> We note, however, that we do not intend to invade the province of any legitimately asserted privilege … including valid assertions of the privilege against self-incrimination under the Fifth Amendment to the United States Constitution. We fully intend, however, that assertions of the Fifth Amendment privilege may be used as … the basis for evidentiary inferences against the person asserting the privilege.

An accountant who believes that her testimony could implicate her in a crime can therefore refuse to provide that testimony, but the Board can then use her refusal to infer that a Sarbanes-Oxley violation has occurred. This places the accountant in a difficult position, especially considering the broad sanction powers of the Board. The Courts will have to define the exact outlines of the Fifth Amendment's protection in these situations.

After the inspection is complete, the PCAOB investigating team prepares a report. This report is described in SOA Sections 104(f) and 104(g), and also PCAOB Rules 4007-4009. Here we see the first of several remarkable provisions evidencing the "soft" approach of the Board. First a "draft inspection report" is prepared and shared with the accounting firm that has been inspected. That firm has 30 days to submit a written response to the draft report. The Board may provide an extension of that time.

The firm can submit its response, which might disagree with the inspectors' findings. The firm can also request "confidential treatment" for any portion of the firm's response, but the firm must "supply any supporting authority or other justification for according confidential treatment to the information". Justification might take the form of evidence that certain information is a trade secret or that it is protected by the attorney-client privilege. If the PCAOB agrees with the firm's response it could modify its draft inspection report, or it could merely attach the firm's response to its draft report. Note that these confidentiality provisions are different from the confidentiality provisions regarding the final inspection report, discussed below.

PCAOB Rules 4008 and 4009 deal with the Board's "final inspection report". The Board will review the draft inspection report and may respond to it by modifying it, or perhaps by sending inspectors back to collect more information. The Board will then issue a final inspection report.

The Board will share the final report with the accounting firm, which can attach its letter or comments to that final report. If the Board thinks it appropriate, it can also attach a letter or comment by the inspectors. This final inspection report, with attached letters and comments, is then transmitted to the SEC.

PCAOB Rule 4009 and SOA Sec. 104(g)2 provide additional evidence of the "soft" approach taken by the Board and by the SOA. The final inspection report will be made public, but in almost all cases the accounting firm will be spared the embarrassment of criticisms or exposure of defects in its quality control systems. Those criticisms and defects will *not* be disclosed to the public for twelve months following the Board's issuance of its final inspection report. During that time the firm may submit evidence that it has addressed the defects. Rule 4009 provides that if the accounting firm merely *addresses* (not cures) the defects, then the criticisms contained in the final inspection report will remain confidential. The SEC and other agencies that received a copy of the original report will then be notified that "the firm has satisfactorily addressed the criticisms or defects in the quality control system." PCAOB Rule 4009 infers that if an accounting firm falls short and receives a negative inspection report but that firm shows good faith in attempting to deal with its shortcomings, no sanctions or public criticism will follow.

In taking this "soft" supervisory approach, the Board is mindful of the need to maintain the viability of existing public accounting firms. With the demise of Arthur Anderson, the "Big 5" public accounting firms shrank to the "Big 4". If another major public accounting firm were to succumb we would be down to the "Big 3". With three or fewer large public accounting firms it would be extremely difficult for large companies to satisfy their accounting needs. The accountant independence provisions of Sarbanes-Oxley prohibit an accounting firm that is already providing other services to public companies from also undertaking audit work. This limits the potential universe of public accounting firms available to those large companies. A large multinational corporation such as General Electric has such vast accounting needs that only one of the "Big 4" can satisfy those needs. It is logical that the PCAOB will seek to preserve and rehabilitate a firm with shortcomings rather than contribute to its demise. All the PCAOB asks is a good faith effort to improve, and evidence that the firm is capable of work that meets PCAOB standards.

PCAOB INVESTIGATIONS

In most cases PCAOB enforcement will end with the final inspection report issued by the Board. However, if evidence of a violation is discovered during the inspection (or otherwise, for example by an informant) then the Board can initiate the next mechanism in the enforcement process, an investigation. The PCAOB's authority to conduct investigations is found in SOA Sections 105(a) and 105 (b), and in PCAOB Rules 5000-5113.

When the Board undertakes an investigation, the process shifts gears. The Board, in its Release of March 21, 2006[36], stated that "unlike the Board's inspection process, the Board's disciplinary process is adversarial in nature". The matter shifts to a new department within the PCAOB, the Department of Enforcement and Investigations. It is to be expected that the investigators of this department will have a more prosecutorial attitude than the inspectors who performed routine inspections.

In order to engage in a formal investigation, the Director of Enforcement must first obtain an "Order of Formal Investigation" from the Board. The Board will issue that order "when it appears that an act or practice, or omission to act … may violate any provision of the Act." It therefore appears that a formal investigation should not be ordered unless the Director of Enforcement first has evidence of a questionable act or omission. Presumably this is to discourage "fishing expeditions" in which over-eager regulators go hunting for evidence of non-compliance. Such conduct is highly unlikely today, with the PCAOB understaffed and barely able to keep up with its workload.

SOA Sec. 105(b)2 and PCAOB Rules 5102-5109 and 5111 deal with the important issue of the powers of the Board to collect or compel the production of evidence from accountants and accounting firms being investigated. The Board may require the testimony of any registered public accounting firm or "person associated with a registered public accounting firm, with respect to any matter that the Board considers relevant or material to an investigation." Testimony is to be given under oath, with a reporter preparing a transcript, in a non-public proceeding. This again raises the issue of the Constitution's Fifth Amendment privilege against self-incrimination, discussed earlier. SOA Section 105(b)5 and PCAOB Rule 5108 deal with the important issue of the confidentiality of investigative records. SOA Section 105(b)5 states that all "documents and information" prepared or received by the Board are "confidential and privileged as an evidentiary matter (and shall not be subject to civil discovery or other legal process)". Moreover, this privileged information is not subject to discovery under the Freedom of Information Act[37]. These provisions provide effective confidentiality protection with respect to civil liability and civil litigation.

PCAOB DISCIPLINARY PROCEEDINGS

Unlike its predecessor the Public Oversight Board (POB), which was a self-regulatory organization under the supervision of the American Institute of Certified Public Accountants (AICPA), the PCAOB has very potent sanctions at its disposal. SOA Section 105(b)4 gives the Board the authority to impose "disciplinary or remedial sanctions" including temporary suspension or permanent revocation of an accounting firm's registration. Without registration a firm may not audit public companies. Revocation of registration would probably lead to the demise of a public accounting firm. The Board can also temporarily suspend or permanently bar an individual accountant from association with any registered public accounting firm. The Board has authority to impose heavy fines on violators. For unintentional (probably negligent) acts, the Board can impose a fine of up to $100,000 for an individual, and up to $2,000,000 for a firm. These limits increase substantially if an intentional act is involved. The limits then go to $750,000 and $15,000,000. Intentional acts include reckless conduct and even "repeated instances of negligent conduct" that violate the SOA. Other sections of the SOA authorize the imposition of jail sentences for failure to maintain required records or willful destruction of records.

Perhaps the most interesting sanction available to the PCAOB is described in SOA Section 105(b)4(F). This section authorizes the Board to require "additional professional education or training." Once again we see the "soft" side of PCAOB enforcement. If a situation seems salvageable, the Board will probably act to preserve the public accounting firm.

As with most regulatory agencies, there is an opportunity for a party charged with a violation to challenge it. These challenges are decided in administrative hearings within the agency. As noted earlier, regulatory agencies were criticized because they combine the three powers of government: they act in an executive capacity, investigating and enforcing; they act in a legislative capacity, promulgating rules that have the force of law; and they act in a judicial capacity by hearing and deciding cases which contest allegations of regulatory violations. In the case of the PCAOB, regulatory violations can result in significant sanctions, as just noted.

Agency hearings are efficient because agency personnel having the necessary expertise are already on hand as salaried employees. The decision-maker is not a judge from the judicial branch of government, but rather another employee of the agency who serves as the hearing officer. Due process at agency hearings typically is reduced so that less time is spent on each hearing. These factors enable the agency to resolve disputes with greater efficiency; they are all present in the specific case of PCAOB hearings. In order to avoid abuse, parties are accorded procedural rights including several opportunities for appeal.

The SOA's description of the hearing process within the PCAOB is remarkably brief: only a few paragraphs contained in Section 105(c). From this brief statement of authority the Board had promulgated 49 rules that occupy 44 pages of text. This is a good example of how agencies take general statutory language and then promulgate many specific rules necessary to implement the intent of the legislation. Many of these rules are purely procedural and of interest only to lawyers engaged in administrative hearings. For example, Rule 5408 limits page lengths of briefs. Rule 5463 limits the time for oral argument before the Board. However, other rules define substantive rights of parties appearing before the Board and are of interest to practitioners and students. These more significant rules are discussed below.

One of the early complaints about abuse by agencies was that the quasi-judicial officer deciding cases within the agency was an employee of the agency and therefore biased in favor of it. The first requirement of anyone deciding cases is an open, unbiased mind. In order to meet this objective, the federal Administrative Procedure Act (APA) requires that this function be performed by an "administrative law judge" who may be an employee of the agency but who is insulated by a high wall of separation from the enforcement or policy arms of the agency[38]. PCAOB Rule 5200 conforms to this requirement. The decision-maker is called a "hearing officer" who "may not be responsible to or subject to the supervision or direction of an employee or agent engaged in the performance of investigative or prosecuting functions for the Board". As a result, the hearing officer does not have to fear career retaliation for decisions adverse to the agency. Any employee or agent of the Board engaged in investigative or prosecutorial functions may not "participate or advise in the decision … except as a witness or counsel".

In order to preserve impartiality (and equally important, the appearance of impartiality) it is important that agency personnel not influence the hearing officer through informal, private contacts. PCAOB Rule 5403(b) therefore prohibits ex parte (one party only) communications. Enforcement personnel may not "communicate with the person presiding over an evidentiary hearing on a fact in issue, unless on notice and with opportunity for all parties to participate."

Hearings before the Board are generally private. Rule 5203 provides that the Board has the power to hold public hearings but only "for good cause shown and with the consent of the parties". The burden of proof is on the Board to prove the alleged violation "by a preponderance of the evidence". This is the same burden of proof in the ordinary civil trial (Rule 5204). Alleged violators may represent themselves or be represented by an attorney (Rule 5401). If an alleged violator reasonably believes that a particular hearing officer is biased against her, she can challenge that hearing officer by making a motion for withdrawal (Rule 5402). However, that motion is made directly to the challenged hearing officer, who must decide if he or she is biased. If the hearing officer decides that he or she is biased, a replacement will be appointed. But if the hearing officer decides that he or she is not biased, then that hearing officer "shall continue to preside over the proceeding." There is no provision in the rules for an interlocutory appeal from a hearing officer's decision not to withdraw. One possible improvement to these rules would be to provide alleged violators with one peremptory challenge to a hearing officer. This would enhance confidence in the fairness of the proceedings.

At the hearing before the PCAOB, either party may request a PCAOB demand for testimony or production of documents. The Board has discretion to seek an SEC subpoena that would compel testimony or production of documents from "any person, including any client of a registered public accounting firm" (Rule 5424).

PCAOB Rule 5441 deals with the admissibility of evidence. Here we see the typical contraction of due process in the interests of administrative efficiency. This rule provides that "the hearing officer may receive *relevant* evidence and shall exclude all evidence that is irrelevant, immaterial or unduly repetitious." This standard of "relevance" is a liberalization of the far more restrictive rules of admissibility that exist in a civil or criminal trial. For example, hearsay evidence is normally excluded at trial, but it could be admissible under the relevance standard of Rule 5441. By adopting a less formal standard of evidence admissibility, technical wrangling over specific admissibility rules is avoided and the hearing officer can focus on the basic merits of the agency's allegations. This is a common trade-off found in agency hearings.

If the hearing officer's decision is adverse to the accountant, he or she can appeal that decision to the Board (Rule 5460). The Board has wide discretion to affirm, reverse or modify the hearing officer's decision, or the Board can send the matter back to the hearing officer for additional proceedings. The accountant can file briefs with the Board (Rule 5462) and seek oral argument before the Board (Rule 5463).

If an accounting firms meets with an adverse decision by the Board, the firm can appeal to the Securities Exchange Commission (Rule 5467). The SEC's decision is the final one within the regulatory agency system. At this point the firm can bring a legal challenge against the PCAOB in federal court.

When challenging agency action before the federal courts it is useful to remember that courts typically give great deference to agency expertise.[39] If an appellant accounting firm is arguing, for example, that the financial information it provided to the SEC is correct using accounting method A, but the PCAOB or the SEC insist that accounting method B must be used to provide accurate financial information, it is highly unlikely that the court will overturn the agency's finding. Judicial review is most likely to succeed if a procedural requirement has been violated, or perhaps upon a convincing showing that the agency has exceeded the authority granted to it by the legislature.

CONCLUSION

The Public Company Accounting Oversight Board is the first federal regulatory agency for the accounting profession. It has substantial sanction powers, including revocation of a public accounting firm's registration, which would probably result in the demise of that firm. The Board has strong inspection and investigation authority, including subpoena power for testimony or documents. These powers are exercised by an agency that is extremely independent. PCAOB independence comes from the fact that Board Members are appointed for fixed terms and can only be removed for good cause. The Board is largely independent of political pressure because the Board's funding comes from a fee levied on regulated companies.

Even though the PCAOB is an extremely powerful government regulatory agency it has chosen to exercise its power with great restraint. It has adopted a soft, "supervisory approach" to enforcement. Criticisms of accounting firms contained in final inspection reports remain confidential for twelve months. If during that time the accounting firm addresses its shortcomings, these criticisms will never become public. The Board will try to work with an accounting firm to improve that firm's performance, so long as the firm demonstrates good faith and a capacity to perform audit work that meets the Board's standards.

Parties coming before the Board have important procedural rights. If the PCAOB charges an accounting firm with a violation, the firm can challenge that in an administrative hearing held within the PCAOB. The hearing officer will be a PCAOB staff member who is kept separate from the enforcement staff of the Board. There are opportunities for appeal from an adverse hearing decision, first to the Board, then to the Securities Exchange Commission and finally to the federal courts.

While parties coming before the PCAOB can assert their legal rights in the enforcement process, they should be mindful that the Board's "supervisory approach" affords them an opportunity to work constructively with the Board. The Board much prefers to preserve public accounting firms rather than to see them fail. In almost all cases a firm will be better off taking advantage of the Board's supervisory approach rather than by aggressively contesting the Board's determinations. After all, both the Board and the profession share the common goal of providing the best possible financial information to decision-makers.

By working constructively with the PCAOB, public accounting firms can best serve their clients and themselves and attain the high standards to which their profession aspires.

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MAKING MORE INFORMED HIRING DECISIONS: POLICY AND PRACTICE ISSUES FOR EMPLOYERS

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ABSTRACT

Making an accurate hiring decision is extremely important for most employers. The cost associated with making a poor hiring decision from a productivity, customer service, and liability prospective have been widely studied and has been estimated to be three times the annual salary of the individual involved. Also, in recent years numerous studies have reported that applicants for employment have grown increasingly willing to misrepresent their credentials in the application process. This growing phenomenon has further complicated the hiring decision for employers attempting to hire the right individual for a position. The purpose of this paper is to examine the problems created by this increased willingness of job applicants to misrepresent their credentials, and to present policy and practice suggestions that employers can utilize in order to reduce their legal liability and the cost associated with making poor hiring decisions.

COSTS ASSOCIATED WITH MAKING A POOR HIRING DECISION

The cost associated with making a poor hiring decision have been widely studied. A 2004 studied conducted by SHL and the Future foundation concluded that "the hidden cost of selecting the wrong candidate for a position equals an annual sum of $105 billion in the United States" (BIZCOMMUNITY.com, 2007). This estimate, derived from an analysis of managerial earnings and the time spent managing poor performance only captures part of the cost of making a poor hiring decision. Often the eventual remedy utilized to correct a poor hiring decision is either voluntary or involuntary termination. In those situations, the most obvious costs the firm will incur are those associated with filling the vacated position. Severance payments, cost associated with re-advertising the job, recruitment, assessment, selection process cost, and training a new hire are incurred again and possibly again if the organization repeats the same mistakes it made the first time. Poor hires can also lead to lost production, sales, and customer satisfaction in addition to poor morale as competent and productive employees develop resentment at "being on the same team with losers" (Burke, 2007).

In those situations where involuntary termination occurs, the potential for wrongful discharge allegations is usually greater (Dinse, Knapp & McAndrew, 2006). The potential legal cost associated with wrongful discharge allegations can add up very quickly in today's litigation happy society. With the wide array of protected class status options available to unhappy former employees, the possibility of having to defend an allegation of some type of discrimination and or retaliation is very real. On the Job Solutions, citing research conducted by the Jury Verdict Research Series, reported the following average compensatory losses:

Table 1	
Wrongful termination	$532,016
Sexual harassment	120,702
Work-related gender	501,622

Table 2	
Defense Hard Costs	
Attorney Fees if the case goes to trial	$250,000
Attorney Fees if the case settles prior to trial	95,000
Manager time expended in the claim process	40 hours
Employee time expended in the claim process	40 hours
Employee time spent investigating the claim	60 hours
Employee time spent preparing for trial	60 hours
Range of settlement costs or jury awards	$150,000 to $250,000
Defense Soft Costs	
Impact on the work group in terms of distraction and reduce morale.	
Impact on the cost of insurance if company is covered and experiences losses.	
Impact on stock price and reputation if there is publicity around the claim.	
Potential of copycat lawsuits or other claims due to internal and external publicity.	
Impact on attracting the best employees given potential negative publicity of a claim.	
(ELT and Littler Mendelson, 2002).	

According to On the Job Solutions, "these amounts do not include legal fees which historically have ranged from $200,000 to $1 million per claim. Plus the cost of managements' time, which can be expensive" (On the Job Solutions, 2007). Another often cited study by ELT and Littler Mendelson, identified both the hard and soft costs and their average dollar and time amounts incurred by an organization to defend itself against a single claim in the employment law area:

One of the more expensive hiring mistakes that a company can make is associated with applicants that lie. If an untruthful applicant is eventually connected to a negligent-hiring lawsuit, "settling or losing such a suit can cost an employer $1 million or more" (Babcock, 2003).

CHALLENGES TO MAKING MORE INFORMED HIRING DECISIONS

> *In today's workplace, an employer is confronted with a host of human resources-related issues, not the least of which is effecting hiring decisions that are appropriate for the organization and compliant with the plethora of employment laws and regulations. An additional, and often unexpected, challenge for the employer in this regard is awareness of and managing applicant misrepresentations about education, work experience, and the like (Matejkovic and Matejkovic, 2006).*

In concluding that applicant misrepresentation of academic and work experience is a growing challenge for employers, Matejkovic and Matejkovic cited numerous studies. In one, a 2002 Hiring Index study by ADP's Screening and Selection Services reported that 40% of individuals' resumes showed discrepancies in employment and education history. In a 2002 Federal Bureau of Investigation (FBI) study they cited, the FBI estimated that approximately 500,000 people falsely claimed to have a college degree (Matejkovic and Matejkovic, 2006). Another study cited by Ron Aumann, estimated that more than one million fraudulent degrees had been purchased in the past decade and that one provider of false degrees had sold more than 200,000 diplomas (Aumann, 2006). Aumann reported on some recent high profile individuals that had been exposed for overstating their academic credentials including David Edmondson, who stepped down as CEO of RadioShack Corporation, Laura Callahan, a senior director in the U.S. Homeland Security Department ousted in 2004, and Sandra Baldwin, of the U.S. Olympic Committee in 2002. An October 12, 2006 Associated Press story reporting on a federal wire and mail fraud case involving an online diploma mill, noted that a White House staff member and National Security Agency employees were among 6,000 individuals who purchased online college degrees from the company. Many of the degrees were sold to foreign residents seeking entry into the United States, raising national security concerns (Associated Press, 2006). The New York Times reported that 14 New York Fire Department employees "had used, or tried to use, bogus diplomas to be promoted or hired" purchased from the same diploma mill currently facing federal wire and mail fraud charges (Buckley, 2007). Another troubling set of statistics reported by Matejkovic and Matejkovic was on a study of college students that reported that 95% of the students in the survey stated that they would lie to get a job and that 41% reported that they had already done so (Matejkovic and Matejkovic, 2006).

LEGAL ISSUES

> *Typically, a negligent-hiring suit stems from the actions of an employee whose background was checked inadequately if at all during the hiring process and whose villainous history was not discovered until the person had done further harm (Babcock, p. 50, 2003)*

It has been widely held that employers have a duty to exercise "reasonable care" in their hiring decisions and in decisions related to retaining employees (Danaher, 2007). The common law doctrine of "respondeat superior" generally makes employers responsible for harm their employees cause others to suffer if the employees were acting within the scope of their employment.

> *Employees are deemed to be acting within the scope of their employment when their actions relate to the kind of work that they were hired to perform, take place substantially within the workplace and during work hours, and serve, at least partially, the interests of the employer. For example, if a stock clerk drops an item and injures a shopper while stocking the shelves, the employer is clearly liable for the customer's injury (Walsh, p. 126., 2007).*

Negligent hiring is an extension of an employer's responsibility for harm caused by their employees acting within the scope of their employment, to include harm caused by their employees outside the scope of their employment "but for which the careless hiring of an unfit employee set the stage" (Walsh, p. 127, 2007). To establish that negligent hiring has occurred, a plaintiff must establish the following:

1. *A standard of conduct or duty to others exists with respect to an employer taking reasonable steps to avoid hiring unfit employees. The extent of any such duty is based on:*
    a. *foreseeability of harm to others if an unfit person is hired for a particular job.*
    b. *knowledge of unfitness that the employer had or should have had if proper hiring procedures were used.*
    c. *public policy.*

2. *The employer fails to exercise the proper degree of care and hires an unfit employee.*

3. *A coworker or other third part is harmed by an unfit employee.*

4. *The employer's failure to exercise the proper degree of care in hiring is the proximate cause of the harm or injury that occurred (Walsh, p. 127, 2007).*

With respect to avoiding the hiring of an unfit employee, there is no exact standard that is applicable in all cases as to "how careful an employer's background check must be, or whether a background check must be conducted at all" (Walsh, p. 130, 2007). Walsh goes on to note that certain industries and occupations do have statutory requirements with respect to conducting background checks, most notably childcare facilities subject to the National Child Protection Act of 1993 (Walsh, 2007). Health care is another industry that is under intense pressure from the "court of public opinion" to do more to prevent individuals like Charles Cullen from employment (Snitzer, 2005). Charles Cullen worked as a nurse at 10 different hospitals over 16 years who confessed to killing as many as 40 patients. Cullen had been under investigation, suspended, and fired or forced to resign numerous times over the 16 year period, yet none of the institutions where he worked gave him a bad reference (Snitzer, 2005, and Socolof and Jordan, 2006). The negligence claims that evolved from the Cullen situation highlights the importance of reviewing a persons work history. Nursing homes that had at least done reference checks on Cullen have seen claims dropped because those checks did not reveal any past firings or suspensions (Socolof and Jordan, 2006).

The foreseeability of harm to others is often the most important factor influencing the degree of care that an employer must exercise in hiring. Employers...

> *are not expected to be omniscient in anticipating bad things that employees might do. Instead, the question is whether a "reasonable person" of average intelligence would be able to foresee that hiring an unfit person for this particular position would render injury or harm to others likely. Foreseeability thus stems primarily from the nature of the position into which an employee is being hired. The more "sensitive" the position and the greater foreseeability of harm, the more extensive is the background check that should occur(Walsh, p. 130, 2007).*

Some of the more obvious situations where greater foreseeability of harm might dictate a more extensive background check would be jobs

> *"involving contact with children, older persons, the mentally ill, and other vulnerable segments of the public; jobs involving personal care and medical treatment; relatively unsupervised work; positions entailing responsibility for security and/or the use of firearms; transportation work; and jobs affording*

substantial access to the homes and personal possessions of others" (Walsh, p. 131, 2007).

While employers in health and child care have some obvious rational for doing more extensive background checks, a number of other service related occupational situations can present risks that many employers in those situations do not immediately grasp. For example, the Kansa City, Kansas plumbing company that hired Wesley Purkey as a service technician in September of 1998. Purkey was a violent felon who had served the better part of his life in prison for a variety of violent felonies, including aggravated robbery, burglary, assault and kidnapping. Purkey was on parole when he applied for the service technician job, and in the eighteen months prior had worked at six or seven different construction jobs "often working less than one week before he was fired" (Shamburg, 2000). Some of his previous employers and the references he provided had knowledge of his criminal background. In completing his application for employment, Purkey indicated that he had not been convicted of a crime or served time in prison. The company did not conduct a criminal background check even though his job would call for him to be sent into customers' homes unsupervised. After one such service call to an 80-year old widow named Mary Ruth Bales, Purkey returned to Ms. Bales home, robbed her and beat her to death (Shamburg, 2000). The resulting negligent hiring lawsuit was settled for $500,000

In Blair v. Defender Services Inc., the 4th Circuit Court of Appeals allowed Kristin Blair, a 19 year old Virginia Polytechnic Institute and State University ("Virginia Tech") student to pursue her claims of negligent hiring and retention against a janitorial staffing service after allegedly being attacked by an employee of that service (Blair v. Defender Services Inc., 2004). Defender Services was under contract with Virginia Tech to perform custodial work at the university and the contract required Defender to perform criminal background checks on all Defender personnel assigned to the Virginia Tech campus. The employee in question (James L. Harris) had been employed on three different occasions leading up to the alleged incident involving Blair. Defender never conducted a criminal background check on the employee. Eleven months prior to the attack on Ms. Blair, a protective order had been issued against Harris as a result of a criminal complaint having been filed by a woman who had been physically assaulted by Harris. Expert testimony offered in opposition to Defender's motion for summary judgment characterized Defender's pre-employment screening of Harris as inadequate. Further, the appeals court noted evidence that Defender would have discovered that Harris was subject to the protective order if a background investigation had been conducted as required. Further, if Virginia Tech had known of Harris' propensity for violence they would not have allowed him to perform janitorial services at the university (Blair v. Defender Services Inc., 2004).

The Cullen incident highlights another complication for employers looking to make an informed hiring decision. That is, the "see no evil, speak no evil" policy practiced by many employers in and outside of the health care industry. Under this policy, employers will not reveal any negative information about former employees fearing claims of defamation and slander (Socolof and Jordan, 2006). Also often referred to as "name, rank, and serial number" reference policies, these widely practiced approaches that limit the sharing of information between employers are a substantial impediment to making more informed hiring decisions and can often lead to allegations of negligence.

The number of legal issues associated with references have been increasing in recent years and the giving of bad or neutral, and even a good reference may lead to allegations of discrimination associated with inquiries related to arrest and conviction records, retaliation for filing a claim under anti-discrimination laws, and negligent misrepresentation when an employer provides one-sided references despite being aware of negative facts about the former employee (Sayko, Joshua D., 2004). In Kadlec Medical Center v. Lakeview Anesthesia Associations (LAA), et. al., a jury awarded Kadlec $4.1 million in a case where glowing letters of recommendations given by colleagues of Dr. Robert Berry, the anesthesiologist hired by Kadlec, omitted his previous know drug problem. Berry was subsequently involved in a malpractice case that Kadlec had settled for $8.5 million (seattlepi.com, 2006). In the malpractice case, Berry was the anesthesiologist in a tubal ligation procedure that left a mother of three small children with brain damage and unable to care for herself (Smith, 2003). Berry's alleged gross negligence and "the fact that he was impaired by drugs during the surgery" were key elements in the case (Knutson, 2006). Dr. Berry was employed by LAA and had hospital privileges at Lakeview Regional Medical Center (LRMC). In 2000, LRMC conducted an audit of Dr. Berry's medication records and found irregularities in his documentation of withdrawals of Demerol. In 2001, after failing to respond to hospital pages, hospital staff "allegedly" found Dr. Berry asleep and that he "appeared to be sedated" (Knutson, 2006). Dr. Berry was subsequently terminated by LAA, and LRMC allowed his privileges to expire. After relocating to Richland, Washington, Dr. Berry applied for privileges at Kadlec Medical Center. Kadlec then sent letters to LRMC and LAA requesting information about Dr. Berry (Knutson, 2006). Kadlec requested evidence of Dr. Berry's competence and a "candid evaluation of his training, continuing clinical performance, skill and judgment, interpersonal skills and ability to perform the privileges requested" (Knutson, 2006). Two LAA physicians provided reference letters and, LMRC in responding to Kadlec's request, claimed it could only provided limited information "due to the large volume of inquiries received in the office" (Knutson, 2006). While both LAA and LRMC had knowledge of Dr. Berry's problems with drugs, neither informed Kadlec of those problems (Knutson, 2006).

POLICY AND PRACTICE ISSUES FOR EMPLOYERS

> *In the past, applicant screening simply involved assessing an applicant's qualifications to ensure that only the most qualified we hired. Today, however, applicant screening must serve the combined purposes of ensuring that skilled*

individuals are hired, eliminating the ever-increasing costs of "counterproductive behavior" by employees, and aiding the employer in avoiding liability down the road (Bettac, 2003).

Whether hiring in health care, child care, or any other service related occupation, employers that are truly interested in making an informed hiring decision, must include a criminal background check as part of the applicant screening process. Socolof and Jordan believe that especially in health care related situations, "criminal background checks are the single most important component of a thorough screening process"(Socolof and Jordan, p. 9, 2006). Their rational is supported by the widely held view that "prior behavior is often the best indicator for future behavior", and that "criminal records are the first records searched by litigant attorneys and the press after an accusation is made against an employee"(Socolof and Jordan, p. 9, 2006). In conducting criminal background checks, employers must be aware of federal and state laws that govern most background information on applicants and employees. The most important federal regulations in this area are associated with the Fair Credit Reporting Act (FCRA). State laws can very with none being more imposing for employers than the regulation in California. California statutes include the California Consumer Credit Reporting Agencies Act and the California Investigative Consumer Credit Reporting Agencies Act (Stivarius, 2006). FCRA provisions have been broadly applied to both "consumer reports" and "investigative consumer reposts". As defined under FCRA, investigative consumer reports are ...

a subset of consumer reports in which information on an applicant's or employee's character, general reputation, personal characteristics, or mode of living is obtained through personal interviews with the applicant's or employee's friends, neighbors, or business associates. Common examples of investigative consumer reports are employment verifications and interviews with former employers and co-workers, where these are performed by a consumer reporting agency (Stivarius, 2006).

Employers utilizing third-party background screening companies must be aware that these companies are defined as consumer reporting agencies under FCRA and that the reports they prepare are defined as "consumer reports" (Zeidner, 2006). When employers use a third party to perform a background check or investigation, there are four basic steps to basic compliance that should be followed:

Step One-disclosure and Authorization: You must give the individual investigated a special notice in writing that you will request an investigative report, and obtain his or her signed consent. You must also provide a summary of rights under federal law.

If the individual investigated wants a copy of the report then he or she must affirmatively request a copy by "checking the box."

Step Two—Certification: You must certify to the background check or investigation company that you will comply with federal and state laws by signing a form that they typically provide to you. (Your background check or investigation company should provide this form.)

Steps Three and Four—Providing Copies and Notice of Adverse Action: You must provide a copy of the report with a letter to the person investigated if (1) the individual has requested a copy; (2) an employer in California obtains consumer information that is a matter of public record; or (3) adverse action is taken based on information in the report. With the letter you also will provide a summary of federal rights. If adverse action is anticipated, the letter also will describe the action to be taken (e.g., withdrawing offer, denying promotion, termination, etc.) and indicate a reasonable amount of time before it will become effective, so that the individual has time to correct any inaccurate information in the report (Stivarius, 2006).

Employers should also be careful to evaluate any third party vendor they utilize to conduct background screening for them. Vendors that promise instant results, tell you that their nationwide criminal conviction search is FCRA compliant and that they have access to the FBI's National Crime Information Center (NCIC) system are very obvious red flags (Socolof and Jordan, 2006). The NCIC system in particular, may only be utilized by law enforcement agencies and it is "illegal for a private individual or company to obtain information from the NCIC" (Socolof and Jordan, p. 8, 2006).

Another widely cited effective element in any applicant screening process is the use of a standard application (Babcock, 2003). In developing the application form, employers must remember that these forms are subject to federal and state antidiscrimination laws and that any inquiry must be job-related and nondiscriminatory in nature (Bettac, 2003). Basic information application forms should require applicants to provide is their name and other names they have used, their social security number, address and phone numbers. An employment history section that goes back at least 10 years with addresses and phone numbers of the previous employers should also be obtained (Bettac, 2003). If certain degrees, certifications, or licenses are required applicants should also be required to provide that information as well. The address information will be critical if the employer is to do a criminal record search (Babcock, 2003). Applicants should also be asked if they have ever been convicted of a crime but employers should be cautioned against inquiring about arrest records. The Equal Employment Opportunity Commission (EEOC) has generally viewed arrest records as irrelevant and the potential for utilizing them may cause an adverse impact on protected class individuals in some parts of the country (Twomey, 2005). Finally, applicants should also be required to sign the application forms, attesting to the truthfulness and accuracy of the information provided, and that providing false, inaccurate, or incomplete information may be grounds for being denied employment or dismissed (Babcock, 2003, Bettac, 2003). The application form should also contain the "employment-at-will" disclaimer and, if applicable, that the employer will be requiring a drug test (Bettac, 2003).

Collecting relevant job related information is important in making an accurate hiring decision, but unless the organization is willing to extend resources to verify the information provided by the applicant, making an informed hiring decision will be difficult. Individuals charged with verifying information must be trained to employ objective methods in verifying information. Without physical evidence, spotting lies based on feelings and observation of how individuals respond in interviews is a very risky approach. "In fact, many experts say it can be a delusion for an interviewer to think lying can be detected in a person's mannerisms" (Babcock, p. 48, 2003). Babcock reporting on studies by Paul Ekman, a psychology professor at the University of California Medical School, noted that studies "have repeatedly shown that people are poor intuitive judges of truth and deception" and that while "most people cannot tell from demeanor whether someone is lying or telling the truth... most people think they can" (Babcock, p. 48, 2003). An employer attempting to verify information supplied on an application form faces a formidable task if they are not going to outsource the process. Tracking down previous employers, and then getting useable information from them can be difficult and frustrating. Verifying degrees, certificates, and licenses, while potentially much easier utilizing the internet, can still be time consuming and thus expensive. One often cited source for verifying degrees is the National Student Clearinghouse at http://www.studentclearinghouse.org/ (Aumann, 2006). This service organization allows employers to verify information on degrees earned "often more quickly than requesting it directly from the school" (Aumann, 2006). Organizations looking to avoid the public embarrassment associated with the publicity that often surrounds press coverage when individuals in high places are identified as having bogus degrees, let alone the potential legal fallout, should verify employee and applicant claims in this area.

Other tell-tale signs that experienced evaluators of application form information recommend include looking for time gaps between employment, incomplete information, and failing to sign the application, "which could shield the candidate from being accused of falsification, or not consenting to background screening" (Babcock, p. 52, 2003).

SUMMARY AND CONCLUSIONS

The cost associated with making more informed hiring decisions can be high and time consuming. Employers looking to hire and promote the most qualified applicants though, should remember the downside cost of not making every necessary effort to make more informed hiring decisions. While press releases would seem to support the idea that the biggest downside costs are associated with negligent hiring, employers should also calculate the "hidden cost" of selecting the wrong candidate for a position identified in the SHL and the Future Foundation study and the "soft cost" detailed in the ELT and Littler Mendelson study. It would appear that the propensity of applicants to lie when applying for both entry level and upper level positions in all kinds of organizations is a rampant and growing problem in our society. This cultural phenomenon will require employers intent on avoiding the hiring of individuals like Charles Cullen, James L. Harris, Dr. Robert Berry, and Wesley Purkey to allocate even more resources in the future to make more informed hiring decisions.

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A DESCRIPTIVE STUDY OF THE ETHICAL PRACTICES OF STUDENTS IN BOTH TRADITIONAL AND ONLINE ENVIRONMENTS AT A UNIVERSITY IN MISSOURI

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ABSTRACT

The study explores the ethical practices of students in both traditional and online technology environments at a university located in Missouri. The purpose of this study is to determine if the university's students practice ethical behaviors while attending and completing college level courses. The study group consisted of 300 students. Random students were sent a 12 question technology online ethical survey that they completed electronically and sent anonymously back to the information office located on campus at the university.

The study concludes that while there are minimal exceptions of ethical behavior, most students attending the university practice ethical behavior while attending and completing coursework.

INTRODUCTION

With the evolution of education the possibilities for learning at the collegiate level are greater than ever. Technology allows researching tactics, distance learning and tutoring capabilities to be utilized by almost all students willing to seek them out. Unfortunately as the possibilities for expanding learning increase, there are also students who use these technologies to try to gain an unfair advantage over their peers by doing such things as faking online sources in their reference lists, sharing completed papers on websites, and cheating on tests. These scenarios, while historically present in brick and mortar classes, have now infiltrated online education. Practicing questionable ethics in higher education is not a new phenomenon for students. Such practices have been occurring for years and unethical practices range from the cliché of "copying off a neighbor's paper," to today's complex Internet paper mills and search engines.

We surveyed a sample of a Missouri university's students to determine their thoughts and actions with regards to ethical practices in their education experience varied contrasting to their traditional classrooms settings with their online classroom scenarios. The purpose of this paper is to study the results of this ethics survey and evaluate the students' personal ethical practices in their coursework at the university.

The proposed research questions to be evaluated are:

RQ1) Overall what is the percentage of students who have committed questionable ethics practices at this university?

RQ2) What is the percentage of students who have committed questionable ethics practices in the online classroom?

RQ3) What is the percentage of students who have committed questionable ethics practices in the traditional classroom?

The null hypothesis to be tested is:

H1) There is a difference in the percentage of students who have committed questionable ethics practices in online vs. traditional classrooms.

REVIEW OF LITERATURE

There have been many publications made available on the subject of human ethics. There are workplace ethics publications and family values ethics publications, but perhaps nowhere are ethics more important, especially with such a large reflection in the number of publications listed under an "ethics search," than in educational settings. Each passing school year, students have access to more advanced methods of academic deception via the Internet.

Online learning is undoubtedly one of the fastest growing segment in the educational marketplace. According to a July 2003 U.S. Department of Education report, more than three million people were enrolled in online classes in 2001, and six million are projected for 2006. (Conhaim, 2003) With this rapid growth there is nearly no alternative but for instructors to expand their skills and at least be partially involved with online applications of teaching methods. In technology terms, online education is still in its high growth phase; which may be unsustainable in the long run.

Online teaching and learning presents new challenges for faculty, students, and administrators in colleges and universities. They must be assured that the use of technology will enhance the teaching and learning experience. Certainly, faculty members require additional support and time to develop new online learning experiences and to ensure that significant learning takes place. This includes methodologies to identify and prevent questionable ethics practices by students. Students, as well, need time to develop the necessary computer skills and content knowledges to produce quality work. Nevertheless, teaching and learning in online courses should, theoretically, compare equivocally with campus-based courses. (Christopher, 2004) Usually, such courses use Web pages that only registered students may access, and that contain objectives, goals, and course work. These pages may be supplemented by a traditional textbook or e-book, but often all required materials are available online. These include online lectures that can be downloaded; the possibility for real time chat sessions; and if an instructor is concerned about liability, a downloadable ethics statement that students can "digitally sign" before returning it to the instructor. Some courses require attendance of an initial face-to-face session with the rest of the class where university standards regarding ethical practices by students can once again be reinforced. "Other online classes have no residency requirements, requiring you to do all of the work online using your browser and an e-mail program. These courses usually have formal start and end dates." (Dervan, 2002)

The advantages of these classes are many. Students don't have to commute to class and can fit in course activities during their free time, either at home or at work. Because of the low cost of delivery, such courses are often cheaper than traditional classes.

Online courses also have some disadvantages, as well. Students must be self-motivated and able to work without direct personal contact with the instructor. Depending on a student's self discipline, situations like this could be a leading indicator of the use of questionable ethical practice. There can be, and more likely is, additional work than in a traditional class. If a student is an inexperienced Internet user, technical problems may be a challenge and sometimes become overwhelming. Another potential problem with online courses, just as with conventional classes, is the quality of the course itself. All online courses are not created equal. Finally, and perhaps the foremost problem that online courses present, is the potential for online ethical violations on the part of the student. If a student struggles with schedule organization, they may seek an alternative to save time such as creating false sources for bibliographies, or worse yet plagiarizing another's work. This unfair practice gives some students an advantage over those who seek to truly learn online via the World Wide Web.

Although there are always a few students who choose to abuse the freedom that is associated with an online class, there are many success stories that can be attributed to these education scenarios. Economics professors Carl Liedholm and Byron Brown found that students in a virtual economics learning program fared better on examinations than their counterparts who took the same course in live classrooms. (O'Connell, 2002) Given such demonstrated successes in certain online education programs the demand for more instructors with Internet knowledge will likely continue growing.

The term ethics, when speaking of education can cover a wide variety of topics. More often than not non-ethical behavior on the part of a student can usually be associated with some variation of plagiarizing.

The easiest way for a student to plagiarize is to copy and paste information directly from the Internet, and this appears to be among the most common ethics violations. Thanks to the wealth of information available on the Internet regarding most any topic, students assume that it is nearly impossible to track such activity. The challenge for educators today is finding a good balance between encouraging Internet use while deterring Internet plagiarism. There are several different ways a student can use the Internet to cheat and or plagiarize. “The most common way for a student to plagiarize material from the Internet involves copying material from a variety of independent websites and compiling them into an ‘original’ document” (Bartlett, 2001). Some students do not consider this a form of plagiarism because they have research or collected the information. Of course, it is possible to use sources from the Internet as long as they are listed under a reference or bibliography section of a research paper and are cited notably throughout a piece.

Another and more contemporary form of Internet plagiarism is using something called a paper mill. A paper mill is a site online, whether it is a file sharing service or other website, where you can purchase a completed research paper. Paper mills were originally started to serve as a place of peer review and research. Now however, it has grown into a place where students can profit monetarily off each other’s work. From an instructional perspective, more recently, papers bought from paper mills are usually of poor quality. “An investigative report conducted by U.S. News and World Report evaluated the quality of four papers purchased from Internet mills. University professors evaluated each of the papers and judged their quality to be mediocre at best.” (Bartlett, 2001) There are methods that instructors can use to deter such activity.

There are some very basic ways an educator can ensure that their students complete their own work. Some examples would include “incremental paper assignments,” such as paper outlines, rough drafts and statements of purpose. “Instructors can create assignments that cannot be completed solely on the Internet, such as research papers that incorporate personal interviews.” (Bartlett, 2001) A prominent problem for the faculty member is that this method of filing and tracking student work can be very time consuming. Most instructors would agree that it is much easier trying to match up a student’s work with the ability they have demonstrated during class times. Instructor “gut instinct” can be very useful as a potential plagiarism detection tool.

Other ways to prevent Internet plagiarism is to use companies or software designed to catch phrases that have been plagiarized. Turnitin.com is an example of a company that compares papers not only to Internet material but also to other papers in a database and other literary sources. Although many educators find such services cumbersome, they do serve a great purpose. “It tells students we are watching, and we have a tool to catch plagiarism.” (Bartlett, 2001) Perhaps the best things that educators can do to stop plagiarism is to invest time in their students, prepatory work, create challenging assignments, and educate students on plagiarism, and to set firm and understandable guidelines.

When an individual opens a search engine and enters “free term papers” in the search box, a large number of websites appear. In a quick, broad search conducted on Google alone, there were four million two hundred and fifty thousand websites found. These, of course, are ranked by number of times a website has been accessed and not by its relevance to a search item; however the results listing prominence of the possibilities is shocking in itself.

In Weiler's article he noted five potential ways that an instructor can deter plagiarism:

- ♦ On the first day of class have the students write on a topic, and then use this to evaluate their writing on future essays.
- ♦ Very clearly explain what plagiarism is, otherwise they can figure out ways to evade them.
- ♦ Do not explain the methods used to check for plagiarism, otherwise they can figure out ways to evade them.
- ♦ Ask a librarian for help if you suspect plagiarism.
- ♦ Follow-up on papers. Do not let plagiarism slip by just because you don't have time. (Weiler, 2004).

RESEARCH AND FINDINGS

In our view, none of these suggestions requires an inordinate amount of time and each could be instrumental in deterring plagiarism and questionable ethical practices. Ultimately eliminating plagiarism in the classroom, online or traditional, is best accomplished by ensuring students understand what is considered plagiarism. Additionally, students should know the consequences for cheating. An ongoing worry that one will be caught may possibly linger on the student's mind and act as a deterrent.

We used a single group descriptive study research design to collect data for this project. The study consisted of twelve "yes and no" questions in an online survey format. The survey submissions were anonymous, and the results will be used to benchmark against future results.

Due to the survey methodology the demographic information available was limited with regards to the details of the participants in this study group. What is known is that the random participants attend a university in Missouri and are college level, ranging from freshmen to seniors. This study excluded any participants of graduate or higher levels of education.

Our first key finding indicates the percentage of the total students surveyed that have committed questionable ethics practices. This particular question did not differentiate between online and traditional classroom settings. 17% of students surveyed self-reported ethics violations, while 83% did not.

Second, our research indicates the percentage of students who have committed questionable ethics practices in a strictly online class environment. A remarkably consistent 18% of those students surveyed admitted anonymously to committing some form of questionable ethics practice. This line of questioning covered the use of books or other materials during online exams, and using sources such as peers or utilizing the help of small groups on quizzes and tests in violation of course policy.

Third, our research shows the results of the percentage of students at the university who have committed questionable ethics practices in a traditional classroom setting. The questions posed included subject topics like copying off of a "neighbor's" paper during exams, or sharing test questions with peers after a test has been taken. A total of 16% of the students surveyed claimed they engaged in such unethical behavior in traditional classroom situations. A total of 84% of surveyed students claim to practice good ethics and academic integrity in classes, which is a promising result for instructors.

The null hypothesis in this particular study can easily be rejected. There is no substantial difference in the percentage of students who have committed questionable ethics practices in online vs. traditional classrooms.

CONCLUSION

University students at this Missouri school self-report to be an ethical group. The absence of further detailed questioning in the survey, with regards to the traditional vs. online classroom environments, is reassuring that ethics violations appear no more likely to occur in either setting. Additional questions could be asked in the future that may lead to further enlightenment on this somewhat surprising result. An improved design would be beneficial if it was possible to better stratify the root causes of this result. Demographic data could also be helpful to help determine specific variables that could contribute to a student's engagement in non-ethical behavior. As this appears to be the first survey instrument of its kind, additional follow up studies could be performed in a wide variety of ethics areas.

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