IN THE MICHIGAN SUPREME COURT
APPEAL FROM THE COURT OF APPEALS

CITY OF HOLLAND,

Plaintiff – Appellee

v

JENIFER L. FRENCH,

Defendant – Appellant

Supreme Court No. 147492
COA No. 309367
Lower Ct No. 10-0011684-CZ
Ottawa Circuit Court

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BRIEF OF AMICI CURIAE THE MICHIGAN MUNICIPAL LEAGUE AND THE STATE BAR OF MICHIGAN PUBLIC CORPORATION LAW SECTION IN SUPPORT OF THE APPELLEE CITY OF HOLLAND'S RESPONSE ON APPEAL

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STATEMENT OF BASIS OF JURISDICTION

MCR 7.301(A)(2) gives this Court jurisdiction to consider whether to hear the City of Holland's appeal from a decision of the Court of Appeals.

In addition, this Court should hear the appeal because the City of Holland is a political subdivision of the State under MCR 7.302(B)(2); the case involves key principles of Michigan law that govern arbitration, employment law, and disputes between local governments and their leading officials, see MCR 7.302(B)(3); and the Court of Appeals' majority opinion conflicts with decisions of the Supreme Court and the Court of Appeals, MCR 7.302(B)(5). The Court also has the power under MCR 7.302(H) to grant immediate relief through a peremptory order.

STATEMENT OF QUESTIONS PRESENTED

1. The Arbitrator failed to consider whether Holland's City Clerk, Jenifer French, should be fired because she engaged in conduct detrimental to the City of Holland's image when she filed certain false voting and property-tax documents. Throughout the arbitration award, the Arbitrator contravened the four controlling principles of Michigan law that substantially impact municipalities across the state:
   - by default, terms of art in a contract – such as "Just Cause" – take on their legal meaning;
   - just cause simply means a good reason to end someone's employment (i.e., more than the "for no reason at all" standard of at-will employment that applies to most non-union employees), and it does not require proof of intentional misconduct;
   - for government employees (especially leaders), just cause exists if their conduct could diminish the public's trust or give the appearance of impropriety; and
   - for leader-employees, the just-cause standard is more lenient to employers and demanding on employees because employers have a strong interest in choosing their leadership, and leadership requires more than ordinary work – leaders have public-relations and management responsibilities that are harder to satisfy.

   A failure to enforce these legal principles undermines municipalities' confidence in arbitration agreements. In light of the Arbitrator's failure or refusal to apply controlling principles of law, should this Court grant leave and/or peremptory relief on these important state-wide issues?

   Appellant City of Holland answers: Yes.
   Appellee Jenifer French answers: No.
   Trial Court answers: Yes.
   Court of Appeals majority answers: No.
   Court of Appeals dissent answers: Yes.
   Amici Curiae answers: Yes.

2. With the aid of counsel, French opted to defend her property-tax documents in the Michigan Tax Tribunal first. After losing there, she proceeded with arbitration, where she persuaded the Arbitrator to focus on intentional misconduct rather than the appearance of

impropriety. The Arbitrator refused to give preclusive weight to the Tribunal's findings that:

- French never principally resided in Holland before she filled out a false property-tax affidavit (as well as a false voter's registration card) saying that she did; and
- the City of Holland's Assessor had adequate evidence to believe that the property in Holland was not French's principal residence.

The City fired French partly because her conduct could be detrimental to her office and the City's image, but the Arbitrator refused to give preclusive effect to the fact that the records were false. Instead, he focused on whether French thought the records were true – which does not address the potential appearance of impropriety. If the courts refuse to correct this blatant misapplication of collateral estoppel, municipalities will lose confidence that administrative proceedings actually have a factually preclusive effect on related issues later. The result will be more litigation and more expense for governments state-wide. Should this Court grant leave and/or peremptory relief on this important state-wide issue of Michigan law?

Appellant City of Holland answers:	Yes.
Appellee Jenifer French answers:	No.
Trial Court answers:	Yes.
Court of Appeals majority answers:	No.
Court of Appeals dissent answers:	Yes.
Amici Curiae answers:	Yes.

DESCRIPTION OF AMICI CURIAE

The Michigan Municipal League ("League") speaks for the 524 Michigan cities, villages and townships who are its members. Organized as a Michigan non-profit corporation, the League provides them with legislative and judicial advocacy, educational opportunities for their officials, and assistance for their leaders in administering community services. Most of those same municipalities are also members of the League's Legal Defense Fund ("Defense Fund"). The League established the Defense Fund in 1983 to represent its members and to provide them with litigation support on issues of statewide significance – that is, issues that broadly impact not only the particular municipal party in a case, but also other Michigan municipalities. The League continues to operate the Defense Fund through a Board of Directors, which authorized Amicus Curiae to file this Brief because this case has a significant impact on the majority of Michigan municipalities, well beyond the borders of the City of Holland. The League and the Defense Fund respectfully submit this Brief on behalf of their municipal members pursuant to MCR 7.306(D)(2).

The Public Corporation Law Section of the Michigan State Bar of Michigan ("Section") joins in this Brief. The Section is a membership section, composed of 625 attorneys who represent the interests of government corporations, agencies, departments and boards, including townships,

counties, villages, cities, schools, and charter and special authorities. Although membership in the Public Corporation Section is open to all members of the State Bar, the focus of the Section is centered on the laws and procedures relating to public law and government corporations, agencies, department and boards, including townships, counties, villages, cities, schools and charter or special authorities. The Section is committed to promoting the fair and just administration of public law. In furtherance of this purpose, the Public Corporation Section of the State Bar of Michigan is participating in submitting this Brief in order to address the significant, state-wide issues impacting governmental entities in Michigan.

I. INTRODUCTION AND SUMMARY OF THE ARGUMENT

This is an important arbitration case where the arbitrator refused to follow the terms of the arbitration agreement and the controlling law. As is well understood in our jurisprudence, arbitrators cannot do this, and if they do, the arbitration decision is fatally flawed. The Circuit Judge understood this and set aside the arbitration decision as a result. But in a split decision, the Court of Appeals reversed as they improperly understood the law on these matters. This Court should grant leave on this case because if this decision is left unreversed, it opens the flood gates to capricious, result-driven arbitration awards and compromises the heretofore well understood

expectations of those who use arbitration, that the law and the agreement will control arbitration. If large employers such as municipalities cannot count on arbitrators to be bound by the arbitration agreement and the law, they will not use arbitration. This, Amici believe, is self-evidently consequential to our state. It will greatly increase the burdens on our courts and the parties. This Court should grant leave to sweep away this rogue holding, which promises to produce chaos until it is dispatched.

The arbitrator's profound errors are especially significant here because they dealt with legal issues that have state-wide significance. In particular, the arbitrator mangled key principles of municipal control over high-ranking leaders, who – by virtue of their position – must earn and keep the community's trust. When leaders fail to honor and keep this trust, the controlling law gives municipalities the power to remove them, regardless of whether the matter is subject to arbitration. The issue here is whether Michigan's courts are impotent to do anything when an arbitrator departs from that controlling law and so badly distorts a municipality's arbitration agreement that it reads plain terms out of existence and exposes the municipality to scandal and shame.

Jenifer French was Holland's City Clerk – a high-ranking official in the public eye. She was responsible for core matters of local government,

including registering voters and overseeing elections. At best, French made a significant mistake when she said that Holland was her primary residence. It was not, and the parties stipulated as much for arbitration. Based on her mistake, French improperly registered herself to vote in Holland and claimed an unwarranted property tax exemption. French might not have committed fraud. But governments are entitled to expect more on behalf of their citizens. They are entitled to expect that leaders will not only avoid impropriety, but also the appearance of impropriety.[1] They are entitled to expect that leaders will set the standard for competency in core matters. In short, they are entitled to expect that leaders will lead the way.

Like other officials who fall flat in key areas, French created an unreasonable risk of scandal and disrepute, and her conduct warranted her dismissal. Like other employers, Holland reserved its power in an arbitration agreement to recognize her failure as just cause to terminate her. Like other

[1] See *Matter of Bennett*, 403 Mich 178, 192 n7; 267 NW2d 914, 919 n7 (1978) (quoting Canon 4 of the Canons of Judicial Ethics: "A judge's official conduct should be free from impropriety and the appearance of impropriety; he should avoid infractions of law; and his personal behavior, not only upon the bench and in the performance of judicial duties, but also in his everyday life, should be beyond reproach."; "Judge Bennett's public use of profane, obscene and abusive language and abusive manner demonstrates a gross lack of judicial temperament"). See also *Westinghouse Elec Corp v Grand River Dam Auth*, 720 P2d 713, 717-18 (Okla 1986) ("Government officials and employees must exercise great care to avoid even the appearance of impropriety in their duties; for they, like Caesar's wife, must be above reproach."), and *In re Marriage of Miller*, 239 Mont 12, 19; 778 P2d 888, 892 (1989) ("A] judge's official conduct is to be free from even the appearance of impropriety and . . . his personal behavior should be beyond reproach as set forth in Canon IV, Canons of Judicial Ethics.").

employers, Holland also used its agreement to identify higher-than-normal professional and ethical standards, which serve a fiduciary purpose for the public.[2] Like other employers, the City of Holland probably simply wanted a fair day in front of the arbitrator, with each of its grounds for terminating French heard, considered and addressed. But *unlike* other arbitrators, one here refused to honor the arbitration agreement's terms, picking and choosing among them as a means to an end. Most important, rather than considering – under the agreement's terms – whether French did something that could tarnish the City's reputation, the Arbitrator went his own direction and focused on the standards of intentional fraud. That refusal violated fundamental principles of arbitration and law. Courts must have the power to correct the problem, and municipalities need the reassurance that courts are willing to do so.

Correcting the error need not change the courts' great deference to arbitration decisions. Arbitration is a vital alternative to the burdens of litigation – especially for municipalities, where garden-variety lawsuits easily turn into salacious, expensive front-page litigation. For arbitration to work, however, arbitration agreements must count for something. When arbitrators

[2] See also *People ex rel Plugger v Overyssel Twp Bd*, 11 Mich 222, at *2 (1863). ("All public officers are agents, and their official powers are fiduciary. They are trusted with public functions for the good of the public; to protect, advance and promote its interests, and not their own.").

run roughshod over the agreement's terms and the controlling law, courts must and *do* have the power to rein them in.

Here, the arbitrator refused or utterly failed to consider one of the City's material and determinative grounds for termination; namely, whether the City Clerk's personal filing of false property-tax and voter documents could tarnish the City's reputation or her public office. That is an issue with broad implications for municipalities across the state, and the City did not receive a hearing on it or an answer to it. The Circuit Court recognized the error and issued a sound 7-page decision vacating the award and sending the matter back to arbitration for a full and complete resolution of the issues. (Pl-Appellant's Appl Ex 1.) In a split 2-1 decision, however, the Court of Appeals reversed and effectively reinstated the original award. (Pl-Appellant's Appl Ex 5.) That decision cannot stand without signaling to municipalities across the state that arbitration is a waste of time where the law holds no sway.

The League, the Defense Fund and the Section respectfully ask the Supreme Court to grant leave, reinstate the circuit court's order vacating the arbitration award, and further hold that as a matter of law municipalities have just cause to fire a leading official for conduct that jeopardizes the public employer's reputation or affects the official's ability to lead in a public role.

Alternatively, Amici ask the Court to grant peremptory relief to the same effect.

II. BACKGROUND

The mission of every Michigan municipality should include "serv[ing] with honesty and integrity." (Pl-Appellant's Ex 25 at "Mission Statement".) The City of Holland expressly identified this as one of its key missions. (*Id.*) Its appointed employees agree to a Belief Statement promising to "perform each responsibility with . . . integrity." (*Id.* at "Employee's Belief Statement".) That is not too much for a municipality to ask of any employee, especially its high-ranking and leading officials.

In 2000, Jenifer French was promoted to serve as Holland's City Clerk. That meant two things. First, she was a high-profile and leading official, bound to serve Holland's mission of integrity. Second, she was bound by Holland's handbook.

In the handbook, the City of Holland took the lead among municipalities in offering officials some key ground rules. The handbook contains the kind of extensive and fair arbitration provision that is common to many Michigan employers. It states:

> Grievances are defined as any disputes between the employer and employee regarding the meaning, interpretation, or alleged violation of the terms of this handbook.

* * *

4. **Cases involving the termination of employment may be submitted to binding arbitration** if the response from the head of management is unacceptable to the employee.

* * *

The arbitrator will be selected by mutual agreement of the employee and the Employer. . . . The designated arbitrator will decide the time and place for a hearing, which will be conducted according to AAA rules. At the arbitration hearing, the employee will have the opportunity to rebut the evidence presented by the Employer and the employee may present witnesses and evidence in support of their case. **The arbitrator will decide, in writing, whether the employee was discharged for just cause.** The arbitrator will also rule on any tort or civil rights claims made by the employee. If the arbitrator decides that the discharge was not for just cause, or otherwise violated the employee's rights, the arbitrator may decide upon an appropriate remedy, which may include reinstatement and/or back pay and/or back benefits. **The arbitrator may not add or delete anything in this procedure. In deciding whether or not the discharge was for just cause or was otherwise improper, the definition of "just cause" and the other rules and policies set forth in the Employee Handbook, and all other relevant policies and procedures, will be observed. In addition, the arbitrator shall be guided by prior decisions of other arbitrators and the meaning of "just cause" in such prior decisions.** [*Id.* at 19-21, "Fair Treatment Procedure" (emphasis added).]

Holland's "Discipline" policy defines what "just cause" means, and it is consistent with Michigan law:

**Examples of employee actions that could be[3] just cause . . . are: * * *

- Insubordination . . .
- **Conduct detrimental to the image of the employer or other employees.**
- **Willfully . . . stealing . . . property or other dishonesty.**
- Violation of the Alcohol and Drug Abuse Policy.
- Violation of the Harassment Policy.
- Safety violations.
- **Other forms of misconduct.** [*Id.* at 11-12, "Discipline" (emphasis added).][4]

This definition is contractual, but it fits with how municipalities across the state understand the law of "just cause" for visible public officials who do things that reflect badly upon the city or the office. Nothing about these policies is particularly remarkable. Especially when a leader is concerned, just cause for termination can include – among other things – engaging in dishonest behavior, creating an unstable work environment, violating ordinary rules, or simply behaving in a way that tarnishes a city's reputation.

[3] In an apparent effort to avoid limiting its definition to the categories of conduct expressly enumerated here, see John E. Sanchez & Robert D. Klausner, *State & Local Govt Employment Liability*, Employment Status-Civil Serv: For Cause § 14:5 (West 2012), the City of Holland stated that just cause "could" include the enumerated things, but could also include other causes. In other words, just cause includes but is not limited to the conduct listed here.

[4] In Holland's "Termination" policy, the handbook states: "At times it may be necessary for the employer to take the initiative and action in the termination of an employee. Examples of such situations are summarized in the discipline section of this handbook." (*Id.* at 43, "Termination".)

Although the City of Holland gave French more protection than most non-union employees across the State – who are at-will – receive from their employers, French still managed to do something that led to her dismissal. After serving as the City Clerk for roughly five years, French filled out voter registration and property-tax filings in 2005, saying that she was a Holland resident, even though Holland was not her primary residence. (*See* Pl-Appellant's Appl Ex 9: Voter Reg Card; *id.* Ex 11: Principal Residence Aff.) About a year later, the issue came to Holland officials' attention, and a question arose whether she had acted properly. City officials – including its chief executive, City Manager Soren Wolff – recognized quickly that the conduct reflected badly on the City and its administration, and they were unhappy with it. They even might have been strongly inclined to fire her. But they conducted an internal review, spoke with French and gave her an opportunity to respond. Based on the evidence and information developed in the review, the City believed that French had not acted properly. The City Council ultimately heard the matter and ended French's employment.

The City of Holland's rationale for terminating French appears in a series of letters that City Manager Wolff sent to French. On May 23, 2006, Wolff sent French a letter giving her notice of the initial charges against her, as

well as a chance to respond. (Pl-Appellant's Appl Ex 17: 05/23/2006 Ltr.) It listed four problems relating to her conduct:

1. **Falsification of City Records and Documents** [discussing the improper voter registration and tax documents];

2. **Improper Voter Registration** . . . you registered to vote as a City of Holland voter stating your home address [in] Holland, Michigan . . . [but y]ou were not living at that address then, or now, by your own admission. **As City Clerk for the City of Holland, you are responsible [to] insure that all voter registration is done properly and in conformance to the law.**

3. **Improper Property Tax Registration** . . . you completed an application for [favorable tax treatment] on property you own in the City of Holland, which **is not your principal residence, as required by State Tax Law**. As a result, you stand to personally derive substantial financial benefit, in violation of the law.

4. **Conduct Detrimental to the Image of the Employer (City of Holland)** . . . As a result of [this] **misconduct . . . in a leadership position with the City, you have set a detrimental example** for your colleagues and subordinates. **You have violated the public trust placed in you by the citizens of Holland, and will potentially subject the City of Holland to a negative image** in the media and, as a result, negatively impact the City's image and credibility with the general public.

The City considers your misconduct to be extremely serious. Any one of the violations described above, standing alone, justifies termination of your employment. . . . [Y]ou have been given an opportunity to respond in our meeting . . . . * * * Before we make a final decision as to your employment with the City of Holland, we will give you one more opportunity to respond, in writing, to the charges. [*Id.* (emphasis added).]

About a week later, French responded to the charges through her lawyer, denying any "sinister act or ill motive." (Pl-Appellant's Appl Ex 18 at 3:

05/30/2006 Ltr.) She said she and her husband each had separate residences, and the Holland house was "her principal residency" and, therefore, the voter registration card and tax affidavit were accurate. (*Id.* at 4.) Rather than directly addressing the appearance of impropriety or its potential impact on the City of Holland's image, French emphasized that she did nothing wrong and expressed concern that the charges might embarrass her family. (*Id.* at 5.) French's counsel invoked the just-cause terms of the handbook and argued that French should be reinstated.

A week later, City Manager Wolff wrote French a follow-up letter:

> In addition to the areas of misconduct previously discussed with you, the statements you have made through your attorney regarding the amount of time you spent at the South Shore Drive home during the period in question cause us great concern. **We believe you have not been completely truthful with the City. This is incompatible with your position and contrary to City policy.** [Pl-Appellant's Appl Ex 19: 06/06/2006 Ltr (emphasis added).]

In the letter, Wolff proposed to present the City Council with a resolution to fire her based on these various charges during an upcoming Council meeting on June 14. [*Id.*] Apparently, the City Council approved that resolution.

French disputed the decision. In accordance with the handbook, she submitted the matter to arbitration. Meanwhile, she and her counsel also pressed the dispute over her tax filings in an administrative proceeding before the Michigan Tax Tribunal. French chose to proceed with the tax proceedings

first. In 2007, she and her husband attended the Tribunal's hearing. They chose not to testify, while leading city officials testified in support of their decision. (Pl-Appellant's Appl Ex 7 at 2-3: Proposed Opinion.) The hearing resulted in a 35-page proposed opinion and judgment in October 2007, (*see id.*), and a final 11-page opinion in August 2008 responding to certain, mostly procedural objections, (*see* Pl-Appellant's Appl Ex 8: Final Opinion).

The Tribunal's opinions included numerous findings of fact and conclusions of law on the issue of whether French actually lived in Holland when she filled out forms saying that she did. Those findings were relevant to the later arbitration proceedings, which went forward in 2010. Arbitrator David Barbour ("the Arbitrator") acknowledged, "The parties have agreed that the findings of fact and conclusions of law contained in the Final Opinion and Judgment and the Proposed Opinion and Judgment from the Michigan Tax Tribunal . . . are binding on these proceedings." (Pl-Appellant's Appl Ex 2 at 7: Arbitration Award.) One-and-a-half pages of the Arbitrator's single-spaced opinion summarized the Tribunal's findings, including that:

- **The Holland City Assessor had adequate evidence to support a belief that the South Shore Drive property was not Ms. French's principal residence.** * * *
- **Ms. French lived at the Saugatuck Township property [i.e., not in Holland] prior to March 17, 2005 [i.e., the date of her voter registration card]**. . . . The Saugatuck property was the Petitioner's "true, fixed and permanent home" for all relevant

purposes, at least until March 17, 2005. . . . Ms. French had the burden for the purposes of the [Principal Residence Exemption] to prove that the Saugatuck Township home had ceased to be her "true, fixed and permanent home" as of April 25, 2005 [i.e., the date she signed her Principal Residence Exemption Affidavit], and that the South Shore Drive property in Holland had become her [permanent home]. * * *

- [T]he evidence that Ms. French established residence at the South Shore Drive property as of May 1, 2005 is lacking and **the evidence affirmatively proved that the South Shore Drive property was not her "true, fixed and permanent" residence as of May 1, 2005.** [*Id.* at 7-8 (emphasis added).]

The Arbitrator also acknowledged that the Tribunal found that in 2005 and 2006, "Ms. French did **not** occupy the Holland property as her principal residence" and was **not** entitled to receive a Principal Residence Exemption for the property. (*Id.* at 8 (emphasis added).) These findings did not require the Tribunal to go so far as to find fraud, and the Tribunal made "no conclusion of law as to whether Petitioner believed that she was entitled to the PRE in 2005 when she filed the Affidavit." (*Id.*)

The Arbitrator was aware that the City offered several bases for the dismissal. Although the Arbitrator completely missed the one that Wolff identified in the second letter – namely, French's perceived failure to be completely honest during the internal review – he at least acknowledged the other four that Wolff cited in the City's first letter: falsification of documents, improper voter documents, improper tax documents, and conduct detrimental

to the City's image. (*Id.* at 1-2.) The Arbitrator also recognized that both "[d]ishonesty and conduct detrimental to the image of the Employer are dischargeable offenses." (*Id.* at 2; *see also id.* at 5 ("Dishonesty related to one's employment is an offense so serious that it can warrant immediate discharge.").) But that was the last time the Arbitrator addressed conduct detrimental to the City's image.

From then on, the arbitration award focused on willful dishonesty stating, "the principal allegation of misconduct is dishonesty." (*Id.* at 1.) In a result-oriented fashion, the Arbitrator treated the case as if the sole issue were "whether an employer has proven falsification," (*id.* at 2), rather than whether the City of Holland had just cause of any kind to fire French. As a result, he focused on whether the Tribunal's judgment "necessarily demonstrate[d] that a taxpayer was dishonest," and whether "Ms. French falsified her Voters Registration form and her PRE Affidavit in order to derive a financial windfall." (*Id.* at 7.) He concluded that "there is nothing in th[e Tribunal's] findings that proves by a preponderance of the evidence that Ms. French was dishonest in filing her PRE Application or that the alleged dishonesty affected her performance as City Clerk." (*Id.* at 9.) Without regard to the City Clerk's core duties on voting and election issues, he also found that "[t]he alleged dishonesty was totally unrelated to job performance." (*Id.* at 6.)

From this slanted approach, the Arbitrator wrongly concluded:

> The element of the alleged offense that makes it dischargeable is the dishonest intent to deceive. *Carbide Corp*, 100 LA 763, 766 (Felice, 1993). If that element is lacking by having made a mistake or an error, the offense is not so seriously regarded. **In the absence of an intent to deceive, the element of trust is not destroyed and it is not unreasonable to continue the employment relationship. If the element of dishonest intent is lacking because of a failure of proof, no actionable offense has been committed.** [*Id.* at 9 (emphasis added).]

He ordered the City to reinstate her with full back pay, seniority and other benefits.

The Circuit Court issued a lengthy opinion vacating the award for failure to give due consideration to all the issues, but a split panel of the Court of Appeals reinstated it. This Application for Leave followed.

If the Court does not grant leave and correct the matter, there is a strong danger that municipalities and other employers will avoid arbitration agreements with higher-profile employees. That will result in one of two bad outcomes. Either municipalities will end up in expensive and salacious litigation after they fire officials for dabbling in impropriety or creating the appearance of impropriety, or – perhaps worse – they will retain the officials anyway and wait for the public outcry over these matters. Both results tend to undermine the public's trust and the broader interest in good and efficient

government. A well run arbitration procedure that actually applied controlling law would be a better option.

III. ARGUMENT

A. Arbitration is Governed by Contract, and Courts Have the Power to Ensure that Arbitrators Stay Within the Bounds of Their Contractual and Legal Authority.

This case concerns arbitration. Admittedly, judicial review is narrow, and even the law and evidence only matter as much as the rules governing arbitration deem them to matter. See *Ann Arbor v AFSCME Local 369*, 284 Mich App 126, 144; 771 NW2d 843 (2009) ("Judicial review of an arbitrator's decision is narrowly circumscribed. A court may not review an arbitrator's factual findings or decision on the merits.") (citations omitted). Courts give arbitrators wide latitude within the scope of their contractual authority – wide enough that courts often overlook arbitrators' mistakes. See *Gordon Sel-Way, Inc v Spence Bros*, 438 Mich 488, 497; 475 NW2d 704 (1991) ("[C]ourts may not substitute their judgment for that of the arbitrators and hence [must be] reluctant to vacate or modify an award when the arbitration agreement does not expressly limit the arbitrators' power in some way."). If arbitrators had to be as careful as judges, arbitration might become as detailed and burdensome as litigation.

But the law still counts for something in arbitration, and so do the terms of the parties' agreement. Courts have the power to correct "an error of law that appears from the face of the award, or the terms of the contract of submission, or such documentation as the parties agree will constitute the record." *Dohanyos v Detrex Corp*, 217 Mich App 171, 175–176; 550 NW2d 608 (1996). That power comes from the Michigan Court Rules, which "authorize a court to vacate an arbitration award [if t]he arbitrator exceeded his or her powers," MCR 3.602(J)(2)(c), and "arbitrators can fairly be said to exceed their power whenever they act beyond the material terms of the contract from which they primarily draw their authority, or in contravention of controlling principles of law." *Detroit Auto Inter–Insurance Exchange v Gavin*, 416 Mich 407, 434; 331 NW2d 418 (1982). These kinds of errors are "evident without scrutiny of [the arbitrator's] mental indicia," and they are reviewable. *Id.* at 429.

Here, the Arbitrator exceeded his power in at least three ways that are evident from the "face" of the award:

- He contravened the controlling legal principle that employers have especially wide discretion to choose their leaders and executives and, therefore, the standard for just cause is especially low when they fire those executives and leading employees.
- He contravened the controlling legal principle that as a matter of law, an employer has just cause to fire an employee (perhaps

especially an executive or a high-profile employee) for engaging in conduct that might tarnish the employer.

- He contravened the controlling legal principle that as an arbitrator, he was bound by the Tribunals' findings that French actually filled out voting and property-tax forms that included false information, *and* the City of Holland had enough evidence to determine that she did not live in Holland despite those forms (and thus enough information that she filed forms that could tarnish the City's reputation and diminish the public's trust).

This Court must and does have the power to correct those errors, which if left uncorrected would have a state-wide chilling effect on arbitration by large employers such as municipalities.

1. The Arbitrator contravened the controlling legal principles that govern the definition and determination of "just cause."

The Arbitrator's interpretation of "just cause" contravened controlling principles of law in a variety of related ways. The Arbitrator repeatedly and fervently placed the burden on the City of Holland to prove that French engaged in illegal "falsification" or that she dishonestly carried out her public office. Just cause does not require anything of the sort. Under the law, a just cause is simply a good reason for letting someone go – in other words, something more than the "for no reason at all" that is the peril of at-will employment. Moreover, an employer has a good reason to fire employees when they engage in conduct that might tarnish the employer. Finally, if the employee is a corporate or governmental leader, the just-cause standard is

especially deferential because leaders undergo stricter scrutiny and employers must have strong control over the people who set their tone.

French now carries the Arbitrator's errors one step further. She argues that the Arbitrator was free to make up his own definition of just cause, without regard to any other law or contractual language. She argues that:

- the handbook gave the Arbitrator discretion to interpret the term "just cause", (Def-Appellee's Resp Br at 26);
- the handbook did not define the term at all, (*id.* at 27 n5); and
- although the handbook provided some examples of conduct that "could be" just cause, it did not require the Arbitrator to find just cause when actual instances of that conduct occurred, (*id.* at 30, 44 ("The handbook did not state that this type of conduct **was** just cause for discharge . . . .").

She fails to discuss the law of "just cause" and instead argues that even if just cause existed, the Arbitrator could force the City of Holland to keep her as its chief City Clerk anyway. (*Id.* at 26.) If that is the law, then "the law is a[n] ass . . . ." Charles Dickens, *Oliver Twist* ch 51, p 489 (1970).

But the law is not an ass. Ordinarily, where, as here, "a municipal officer is appointed . . . and no definite term is prescribed, he or she holds at the will or pleasure of his or her superior or the appointing or electing authority; hence, the power of removal may be exercised at any time by such agency." 4 McQuillin Muni Corp § 12:354 (3d ed.). Indeed, most non-union employees in Michigan labor under this at-will standard. The City of Holland chose to give

French some additional just-cause protection in the handbook, but that does not mean the City needed to prove misconduct. It only had to show just cause, which manifestly existed in her case.

"Just cause" has a meaning under the law, which the Arbitrator ignored. Courts generally interpret the words in contracts, statutes and constitutions according to their plain and ordinary meanings as of the time they were adopted or entered. See *Wayne Co v Hathcock*, 471 Mich 445, 468-69; 684 NW2d 765, 779 (2004) (constitution), *People v Blunt*, 282 Mich App 81, 83; 761 NW2d 427, 429 (2009) (statute), and *DeFrain v State Farm Mut Auto Ins Co*, 491 Mich 359, 367; 817 NW2d 504, 509 (2012) (contract). But when those documents use legal terms of art, the words are construed "in their technical legal sense." *Silver Creek Drain Dist v Extrusions Div, Inc*, 468 Mich 367, 375; 663 NW2d 436, 440 (2003) (interpreting "just compensation"), *quoted in Hathcock*, 471 Mich at 469. See *Blunt*, 282 Mich App at 83 (citations omitted). This is a controlling legal principle that arbitrators – like judges – must uphold and apply.

"Just cause" is a term of art. Although it is flexible enough to fit different circumstances, it still incorporates three clear legal principles that the Arbitrator failed to acknowledge or apply here.

(1) Just Cause is a Broad Standard, and It Includes Off-the-Job Actions that Could Reflect Badly on the Employer. Just cause is not limited to cases of misconduct, much less intentional misconduct. John E. Sanchez & Robert D. Klausner, *State & Local Govt Employment Liability*, Employment Status-Civil Serv: For Cause § 14:5 (West 2012). Misconduct *can* constitute cause, but cause also includes things like bringing the employer into disrepute or compromising one's ability to lead the current staff. See *Utah Dept of Corr v Despain*, 824 P2d 439, 445 (Utah Ct App, 1991) (internal policy prohibited off-duty alcohol usage that "will reasonably tend to bring discredit to the Department"; finding just cause to fire prison guard despite legally allowable blood alcohol content because he caused serious accident), and Don Pierson, *Fired In Disgrace At Michigan In 1995, Gary Moeller Stuck To His Profession And Has Risen To Lead The Detroit Lions*, Chicago Tribune (Nov 29, 2000), http://articles.chicagotribune.com/2000-11-29/sports/0011290350_1_big-ten-titles-chris-claiborne-senior-bowl (accessed Aug 30, 2013) (discussing the firing of Michigan Wolverine football coach after off-season alcohol-related incident).

Under the law, the broad standard of "just cause" simply means a good reason to fire someone in French's position. See 4 McQuillin Mun. Corp. § 12:311 (3d ed.) ("It is a common-law incident of all corporations to remove a

corporate officer from office for reasonable and just cause. * * * 'Cause' implies a reasonable ground of demotion or removal as distinguished from a frivolous or incompetent ground."). It includes such simple employment issues as failing to maintain one's teaching certificate, *Snyder v Jefferson Cty Sch Dist R-1*, 842 P2d 624, 632 (Colo, 1992), using profanity in public, *Pima Co v Pima Co Merit Sys Com'n*, 189 Ariz 566, 571; 944 P2d 508, 513 (1997) (upholding sanction against Victim Witness Program advocate), and insubordination, *Paige v Cisneros*, 91 F3d 40, 42 (CA 7 1996) (HUD attorney engaged in "defiance, including refusal to file litigation reports and contravention of office policy in the processing of cases").

In cases involving government officials, courts recognize that "[r]emoval 'for cause' . . . need not amount to a substantive dereliction of known duties or standards of performance . . . [and it] embraces many situations which are not encompassed under the 'misconduct' standard . . . ." *McSweeney v Town Manager of Lexington*, 379 Mass 794, 797; 401 NE2d 113, 116 (1980) (construing a similar statutory "for cause" standard). Compare *Free Enter Fund v Pub Co Accounting Oversight Bd*, _ US _; 130 S Ct 3138, 3154 (2010) (contrasting ordinary good cause standards with higher standards for officials who were removable respectively for "inefficiency, neglect of duty, or malfeasance in office" and for willful violations of a statute).

Executive officers are usually terminable for cause when they make false statements to other officials, regardless of whether the statements relate to core business performance. See, e.g., Darrell A. Hughes & Joann S. Lublin, *Arbitron CEO Resigns After Hill Testimony*, Wall Street J (Jan 13, 2010), http://online.wsj.com/article/SB10001424052748703672104574654392623606448.html (CEO avoided being fired for cause by resigning after he "admitted to a false statement made in his testimony before a U.S. congressional committee last month[, which] violated a company policy in a matter unrelated to its financial performance.") (accessed Aug 30, 2013).

A highly persuasive multistate authority, The National Conference of Commissioners of Uniform State Laws, recognizes these broad standards of just cause. The Conference's Model Employment Termination Act defines the equivalent term, "good cause," as:

> (i) **[A] reasonable basis related to an individual employee for termination** of the employee's employment in view of relevant factors and circumstances, **which may include** the employee's duties, responsibilities, **conduct on the job or otherwise**, job performance, and employment record, or (ii) the exercise of business judgment in good faith by the employer, including setting its economic or institutional goals and determining methods to achieve those goals, organizing or reorganizing operations, discontinuing, consolidating, or divesting operations or positions or parts of operations or positions, determining the size of its work force and the nature of the positions filled by its work force, and determining and changing standards of performance for positions. [Model Uniform Employment

Termination Act, *reprinted in* 9A Lab. Rel. Rep. (BNA) 21, § 1(4) (Aug 8, 1991) (emphasis added).]

The Conference also recognizes that when deciding if the employer's basis is reasonable, the fact-finder considers the management level of the employee, the importance of the employee's position to the business, and the potential for off-the-job conduct to affect the employer's reputation. *Id.* cmt. 4.[5] These are the same kinds of standards that the other Michigan cases discussed here support. The Arbitrator's narrow interpretation of just cause contravened these well established principles of good and just cause.

(2) Employee Activity that Could Tarnish the Employer's Reputation Constitutes Just Cause. The Conference's model statute illustrates a second controlling principle of law that the Arbitrator failed to consider. Just cause exists whenever employees do things on or off the clock that can tarnish the employer's reputation. It thus includes anything that "**violat[es] the implicit standards of good behavior imposed upon one who stands in the public eye as an upholder of that which is morally and**

[5] Although the Conference's comments do not trump clear statutory terms, *Fisher Sand & Gravel Co v Neal A Sweebe, Inc*, 494 Mich 543, _; _ NW2d _ (2013), Michigan often consults, follows or adopts the Conference's standards when terms are ambiguous. See, e.g., *Theophelis v Lansing Gen Hosp*, 430 Mich 473, 490; 424 NW2d 478, 485 (1988) (Uniform Contribution Among Tortfeasors Act); *Taylor v Walter*, 384 Mich 114, 133; 180 NW2d 24, 30 (1970), *adhered to* 385 Mich 599 (1971) (Uniform Rules of Evidence, Handbook); *Am Parts Co, Inc (Detroit Body Prods Div) v Am Arbitration Ass'n*, 8 Mich App 156, 173; 154 NW2d 5, 14 (1967) (Uniform Commercial Code), *White v Harrison-White*, 280 Mich App 383, 387; 760 NW2d 691, 695 (2008) (Uniform Child-Custody Jurisdiction and Enforcement Act), *Electrolines, Inc v Prudential Assurance Co, Ltd*, 260 Mich App 144, 152, 157; 677 NW2d 874, 880, 882 (2003) (Uniform Foreign Money–Judgments Recognition Act; the Uniform Enforcement of Foreign Judgments Act).

legally correct...." *Tuscon Civil Serv Comm v Livingston*, 22 Ariz App 183, 187-88; 525 P2d 949, 953-54 (1974), *quoted in Tucson v Mills*, 114 Ariz 107, 111; 559 P2d 663, 667 (1976). The Arbitrator paid one sentence of lip-service to the argument that French might have engaged in "conduct detrimental to [Holland's] image," but the Arbitrator never discussed or decided the issue.[6]

This was a critical mistake. More than private parties, the government has a fundamental responsibility to maintain the trust of the community it serves. Thus, prosecutors have a constitutional duty to avoid cases in which they have personal interests because such involvement "diminishes faith in the fairness of the criminal justice system in general." *In re Ligon*, _ SW3d _; No. 09-13-00242-CR, 2013 WL 4190402 (Tex App, Aug 14, 2013) (Appx Ex 1) (internal quotation omitted). See *Berger v United States*, 295 US 78, 88; 55 S Ct 629 (1935) ("obligation to govern impartially"). In employment matters, the interest in maintaining the public's trust is so substantial that it outweighs a management-level official's interest in free speech. The government can remove an official from a management position for speech that undermines the public's trust in the unit. See, e.g., *Faghri v Univ of Conn*, 621 F3d 92, 97-98

[6] The face of the award does not reflect any resolution of the issue. On the other hand, if the Arbitrator considered it at all, he must have equated it with the other intentionally deceptive misconduct that he was addressing. But that equivocating approach essentially reads the contractual term "conduct detrimental" as being duplicative of "dishonesty" and thus nugatory. Such a nugatory reading would contravene established principles of contract law.

(CA 1 2010) (university properly removed dean from the deanship for contrarian speech).

This responsibility falls not only on the public corporation, but also on the individual officials who compose it. "All public officers are agents, and their official powers are fiduciary. They are trusted with public functions for the good of the public; to protect, advance and promote its interests, and not their own." *People ex rel Plugger v Overyssel Twp Bd*, 11 Mich 222, at *2 (1863). They are guardians of the public trust.

The interest in preserving the public trust "may be particularly weighty if the employee in question holds an executive or policymaking position." *Id.* at 98. But even for non-management officials who have higher-profile positions, that governmental interest is so strong that employees' personal errors constitute just cause:[7]

- **Off-Duty Drunkenness, Threats and Abusive Language.** Conduct unbecoming a prosecutorial official justifies removal, including the drunken use of abusive language and threats against coworkers. See, e.g., *Feltri v Kelaher*, No. A-5628-06T1, 2008 WL 1874427 at *6 (NJ App, April 30, 2008) (Appx Ex 2).

- **Conduct Unbecoming a Teacher By Taking a False Sick Day.** *Laurel Cty Bd of Ed v McCollum*, 721 SW2d 703, 704-705 (Ky,

[7] One police chief was recently quoted as saying, "**Public trust is the foundation of Public Safety.** The Chief of Police is expected to hold all employees accountable for their actions, **on or off duty**, regardless of rank, tenure, or position." See *Former High Ranking Fort Worth Police Officer Fired For Driving Drunk*, CBS-DFW (May 16, 2013 9:29 PM), http://dfw.cbslocal.com/2013/05/16/former-high-ranking-fort-worth-police-officer-fired-for-driving-drunk/ (accessed Aug 30, 2013) (emphasis added).

1986) (teacher falsely called in sick to take a one-day job driving a coal truck).

- **Consorting with a Known Prostitute.** *Livingston*, 22 Ariz App at 187-88.
- **Domestic Disturbances and Assaultive Behavior.** *Mills*, 114 Ariz at 111.

Each of these instances involved violations that – even if understandable – reflected lapses of personal judgment that raised particular concerns for government representatives in the public eye.

Whether a person is a teacher, a police officer, or the head of a government department, when that person becomes a potentially "bad role model," there is just cause for their termination. See *Zelno v Lincoln Intermed Unit No 12 Bd of Dirs*, 786 A2d 1022, 1026 (Pa Commw Ct, 2001) (teacher fired for third DUI on grounds of "immorality"). Thus, a Missouri court upheld the decision to fire an "outstanding and exceptional" shop teacher who made false statements in his teacher application and in government-program documents, which the teacher described as "mistakes." *Cochran v Bd of Ed of Mexico Sch Dist No 59*, 815 SW2d 55, 63-64 (Mo App, 1991). The court found substantial evidence to support the school board's conclusion that "A classroom teacher must set an example for his students. His integrity must be beyond question," and this teacher's mistakes undermined that confidence and trust. *Id.* at 64. Other courts have recognized that "[g]overnment officials

and employees must exercise great care to avoid even the appearance of impropriety in their duties; for they, like Caesar's wife, must be above reproach." See *Westinghouse Elec Corp v Grand River Dam Auth*, 720 P2d 713, 717-18 (Okla, 1986).

Here, while failing to address one of the City's key grounds for firing French, the Arbitrator also failed to acknowledge or apply the controlling legal principle that like other municipalities across Michigan, Holland has a fundamental interest in maintaining the citizens' trust, which – as a matter of law – strongly weighed against French's personal interest in holding onto her position as City Clerk. If allowed to stand, the Arbitrator's decision makes a mockery of the authority that governments heretofore had to fire higher-profile employees whose conduct weakens the public's trust.

(3) Just Cause Considers the Management Level of the Employee. The Conference's model statute also illustrates the third controlling principle of law, which the Arbitrator failed to consider. All employers need to exercise special discretion in decisions about their high-ranking officials.

It is hardly revolutionary to suggest that management-level officials lose their necessary capacity to lead and manage an organization when they do something that undermines confidence in them. For government appointees, that is the whole idea behind a "no-confidence" vote. See e.g., *House Judiciary*

Subcommittee Takes Testimony on HALT Legislation: Report & analysis of immigration & nationality law, 88 NO. 30 Interpreter Releases 1863, 1864 (Aug 8, 2011) (discussing unanimous vote of no confidence against US-ICE Director John Morton by ICE union leaders). Many things – large and small – can lead to loss of confidence in a leader. See *Faghri*, 621 F3d at 97-98 (professors circulated no-confidence petition concerning dean who opposed university policies and initiatives). That is why even the notoriously employee-friendly California courts recognize that:

> an employer must have wide latitude in making independent, good faith judgments about high-ranking employees without the threat of a jury second-guessing its business judgment. Measuring the effective performance of such an employee involves the consideration of many intangible attributes such as personality, initiative, ability to function as part of the management team and to motivate subordinates, and the ability to conceptualize and effectuate management style and goals . . . . [*Cotran v Rollins Hudig Hall Intern, Inc*, 17 Cal 4th 93, 100-01; 948 P2d 412, 417; 69 Cal Rptr 2d 900, 905 (1998), quoting *Pugh v See's Candies, Inc*, 203 Cal App 3d 743, 769; 250 Cal Rptr 195 (1988).]

Although Michigan courts articulate the substantive standards somewhat differently,[8] they recognize that **leading officials have "supervisory and**

[8] With the benefit of hindsight, California and other courts chose to depart from Michigan's current rule, which gives fact-finders in misconduct-based cases the responsibility to decide if an employee actually committed the conduct *and* should be fired for it. This case offers the Supreme Court an opportunity to clarify a few things about its position.

In a sharply divided, ground-breaking 4-3 decision more than 30 years ago, this Court reached two controversial holdings in the now-famous *Toussaint* Case. The first was more legally significant, but it is not material here; namely, that an employer can create a "for-cause" employment relationship simply by making statements or implementing policies that assure employees that they will not be terminated without cause. *Toussaint v*

public relations responsibilities [that are] inherent in being the" visible person in charge. *Cole*, 229 Mich App at 649-50 (emphasis added). Ordinary employees can get away with things that cripple a leader's ability to marshal

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Blue Cross & Blue Shield of Mich, 408 Mich 579, 614-15; 292 NW2d 880, 892 (1980). The *Toussaint* Court's second holding is important here: for just-cause contracts, the trier of fact gets to decide if the employee's conduct justified being fired, regardless of whether the employer acted objectively reasonably or subjectively in good faith. *Id.* at 623. In other words, the trier of fact second-guesses the employer's business judgment.

The 4-Justice *Toussaint* majority apparently felt painted into this corner. On the one hand, the Court justifiably worried about the "danger" that the fact-finder "would substitute its judgment for the employer's," and the Court conceded that for-cause employment "does not include a right to be discharged only with the concurrence of the communal judgment of the jury." *Id.* at 622. At the same time, however, the Court did not want employers to be the "sole judge[s] and final arbiter[s]" of their own conduct. *Id.* at 621. The Court viewed at-will and "satisfaction" contracts as giving employers total leeway. Under a satisfaction contract, an employee can be fired as long as the employer – in good faith and not as a pretext – is dissatisfied with someone's performance. *Id.* The Court did not want good cause to essentially equate with satisfaction. But in rejecting this subjective good-faith standard, the Court went a step too far. It found no material difference between subjective good-faith and objective reasonableness and thus refused to review employers' decisions for objective reasonableness. *Id.* at 623.

In hindsight, there is a huge difference between good faith and reasonableness, and a review for reasonableness injects a fair degree of meaningful oversight while appropriately deferring to management's judgment. See *Cotran*, 17 Cal 4th at 102-07; 948 P2d at 418-22; 69 Cal Rptr 2d at 906-10 (extensively discussing the considerations). Other courts agree and adopt the reasonableness standard. See, e.g., *Towson Univ v Conte*, 384 Md 68, 85; 862 A2d 941, 950 (2004) ("[T]he jury may not review whether the factual bases for termination actually occurred or whether they were proved by a preponderance of the evidence submitted for its review. Instead, the proper role of the jury is to review the *objective* motivation, *i.e.*, whether the employer acted in objective good faith and in accordance with a reasonable employer under similar circumstances when he decided there was just cause to terminate the employee."). The *Toussaint* opinion overlooked this material distinction, and this Court can and should review the point.

Economic analyses offer additional reasons that lend support to this view in cases where the employer reasonably believes that an employee was negligent. See, e.g., Juan Carlos Bisso & Albert H. Choi, *Optimal Agency Contracts: The Effect of Vicarious Liability & Judicial Error*, 28 Int'l Rev. L. & Econ. 166, 167 (Sept 2008) ("If the principal cannot penalize the agent [for reasonably perceived, but judicially disavowed negligence], controlling the [employee's] actions requires the principal to leave a larger economic rent to the [employee]. As a result, . . . the principal becomes less likely to induce [compliance with standards of] care. * * * This [impacts] the wrongful discharge doctrine in employment law. . . . [S]hould an employer be allowed to discharge a [just-cause] employee for causing an accident, even before a court determines that the employee has been negligent? Not only does our analysis say yes, it goes further to argue that even if the employee is later exonerated by a court, the employer should not be liable for wrongful termination. [This approach] enables the employer to better solve the moral hazard problem.") (Appx Ex 3).

the staff or to be the "face" of the organization. Leaders must be able to deliver on those public relations and leadership responsibilities. When evaluating just cause to fire a leader, the standards for ordinary employees do not suffice.

Controlling Michigan law also recognizes that "those who have charge of public officers . . . have the authority to remove them if they fail to carry out their duties, [including those] duties . . . placed on them . . . by the inherent responsibilities and duties of the office itself." *Gray v Hakenjos*, 366 Mich 588, 594; 115 NW2d 411, 413 (1962). Another court put it, "[t]he governing board of any municipality has a duty to see to it that only properly qualified individuals are holding positions within the local government." *Auge v Anderson*, 112 RI 296, 298; 309 A2d 17, 19 (1973) (town building inspector). Thus, a city not only has the power, but also a duty to ensure that leading officials are qualified to lead.

One obvious way that leaders prove themselves unfit for leadership is by engaging in on-the-job misconduct. See *First Atl Leasing Corp v Tracey*, 738 F Supp 863, 870 (DNJ 1990) (bank had "good cause" to fire executive vice president because he engaged in questionable loan transactions). City Clerks who perform "services for personal friends but not . . . for others" commit a kind of malfeasance that justifies removal. *State ex rel DeLuca v Common Council of City of Franklin*, 72 Wis 2d 672, 679; 242 NW2d 689, 693 (1976).

The appearance of favoritism raises an "implication that [the clerk] was dishonest in the manner he operated his office." *Id.* Arguably French acted too personally when she passed documents through her office for her own benefit, which did not meet the legal voting standards that she was appointed to administer.

But official misconduct is not the only way a leader or visible official forfeits their ability to represent the government. Leaders lose the public's confidence for all sorts of reasons, public and private. See Associated Press, *Kerry Aide Cited for Solicitation to Step Down* (Aug 20, 2004), http://www.foxnews.com/story/2004/08/20/kerry-aide-cited-for-solicitation-to-step-down/#ixzz2dV3jYhnF (accessed Aug 30, 2013). From public drunkenness to false statements, a variety of conduct that might be excusable for an ordinary employee constitutes just cause to fire a government leader like French.

Taken as a whole, the controlling law dictates that where, as here, a leader undermines their own ability to lead – whether due to personal conduct, professional misconduct, or even the shadow that either casts on the office – municipalities must have the power to remove them. Here, the Arbitrator failed even to address whether French's conduct (namely, her submission of false voting and property-tax records while serving as a leading

city official) could tarnish the City of Holland's reputation. Holland did not get a fair hearing on that issue, and the Arbitrator's result-oriented failure to deal with it requires that the award be vacated. This Court has abundant authority to do that. If it does not do so, municipalities will learn the unfortunate lesson that there is no forum to address a wayward arbitrator's failure to apply controlling law in cases involving high-ranking and high-profile leaders, which can be the most important cases for a municipality to arbitrate.

2. The Arbitrator contravened the controlling legal principle that the Michigan Tax Tribunal's relevant factual findings were binding during arbitration.

> *If a[n employee] were allowed to relitigate a factual question previously decided by [a state agency], it would reduce the administrative process to a mere rehearsal; an employee satisfied with the [agency]'s findings could accept them, while a dissatisfied employee could start over with a clean slate by bringing the matters before an arbitrator. Although surely most dissatisfied litigants would enjoy a second bite at the apple, our system disfavors resort to successive litigation to resolve identical issues.*
>
> *Dearborn Hts Sch Dist No 7 v Wayne Cty MEA/NEA*, 233 Mich App 120, 128; 592 NW2d 408, 412-13 (1999).

While paying lip service to the Tribunal's proceedings, the Arbitrator also ultimately disregarded the parties' agreement "that the findings of fact and conclusions of law contained in the Final Opinion and Judgment and the Proposed Opinion and Judgment from the Michigan Tax Tribunal [were] binding on the[arbitration] proceedings." (Pl-Appellant's Appl Ex 2 at 7.) The real effect of that agreement was merely to amplify what the law already

required. It is well settled that the Tribunal's rulings are binding in later proceedings. *See, e.g., Baraga Cty v State Tax Comm'n*, 243 Mich App 452, 456; 622 NW2d 109, 111 (2001) ("Decisions of the Tax Tribunal have the effect of res judicata."; although State Tax Commission was not a party to the earlier proceedings, it was bound because its interests had been adequately represented there). Arbitrators – like other adjudicators – must give preclusive weight to prior administrative findings. *See Dearborn Hts Sch Dist No 7 v Wayne Cty MEA/NEA*, 233 Mich App 120, 128; 592 NW2d 408, 412-13 (1999). That is the fair result. Arbitrators' decisions have the same effect; if issues arise first in arbitration, their findings have preclusive effect on later administrative or judicial proceedings. *Cole v West Side Auto Emplees F Credit Union*, 229 Mich App 639, 647; 583 NW2d 226, 230 (1998) (discussing *Porter v Royal Oak*, 214 Mich App 478, 485; 542 NW2d 905 (1995)) ("factual findings made by an arbitrator after a proper arbitration proceeding are conclusive in a later-filed civil suit between the same parties"; arbitration governed CEO's wrongful discharge claims). See also, e.g., *Vacca v Viacom Broad of Missouri, Inc*, 875 F2d 1337, 1340 (CA 8 1989) ("Findings of an arbitrator will bind a court under the doctrine of collateral estoppel . . . .").

Part of the point of these doctrines is to avoid wasting everyone's time and resources. *Nummer v Treasury Dept*, 448 Mich 534, 541-42; 533 NW2d

250, 253 (1995) (citing *Univ of Tenn v Elliott*, 478 US 788, 798; 106 S Ct 3220, 3225–26 (1986)). It is a waste of time and a violation of settled law when a second forum – like the Arbitrator here – artificially parses the prior record to "distinguish" those claims while avoiding the obvious contractual or legal significance of the first forum's factual findings. Mere differences in the legal issues between the first and second proceeding have absolutely no impact on the second forum's duty to give thoroughgoing effect to the earlier factual findings – even where the just-cause termination of a long-time executive is at issue. *See Cole*, 229 Mich App at 652 ("while Cole was not obligated to submit his statutory civil rights claims to the arbitration procedure provided for by the employee handbook, the factual findings of the arbitrator were conclusive in this suit that was filed *after* the arbitrator's decision").[9]

Here, French decided to press her claims in the Tax Tribunal first. That was her choice. During the hearings, she had a strong interest in defending her

[9] *Cole* illustrates the right way to handle the situation. There, a roughly 22-year credit union employee distinguished himself and rose to the position of CEO. *Id.* at 641. He "accomplished much on behalf of the credit union during his long tenure." *Id.* at 649. But his drinking interfered with his work performance, *id.* at 648, and he eventually had a hit-and-run accident, *id.* at 649. The credit union fired Cole. Like here, the credit union's handbook contained just-cause provisions, a grievance procedure, and an arbitration agreement. *Id.* at 642-43. Cole disputed the matter first in arbitration, and later in an employment lawsuit. The arbitrator found that Cole's excessive drinking undermined his performance, *id.* at 648, and despite his past great work, his recent misconduct undermined his ability to lead as CEO, *id.* at 649. These findings were preclusive in the later suit. The diminished performance that resulted from his drinking meant that he was not disabled for purposes of a disability-discrimination claim, and the harm that he did to his ability to lead meant that he was "not qualified to handle the supervisory and public relations responsibilities inherent in being the CEO of the credit union." *Id.* at 649-50.

claim of residency, her sworn property-tax Affidavit, and her voter registration (which was one of her bases for her property-tax claim). She already knew the role that the Affidavit and the voter registration card played in the City's decision to let her go. She retained counsel before and during the proceedings. Despite her efforts, she failed to demonstrate her residency or to support her Affidavit. The Tribunal carefully received French's evidence, weighed it, and made important findings, namely:

- When Holland decided to fire French, it had sufficient evidence to believe that Holland was *not* her principal residence;
- When French submitted her *Holland*-based voter registration card, she actually and principally lived in Saugatuck Township;
- French failed to meet her burden to prove that her "true, fixed and permanent home" changed from Saugatuck to Holland by the time she submitted her sworn Affidavit claiming that Holland was her "Principal Residence" for tax purposes;
- Instead, the evidence "affirmatively proved" that by May 2005 (after French submitted these documents), Holland was not French's "true, fixed and permanent" residence; and
- In the tax years ending in 2005 and 2006, Holland still was not French's principal residence for tax purposes.

Despite these facts (i.e., that French was a Saugatuck Township resident), it is undisputed that she submitted voter registration and tax-related documents stating that she was a Holland resident.

That might not demonstrate intentional fraud, but it has clear legal importance under the parties' contract. "Just cause" under the contract includes conduct that might tarnish the City of Holland or the Office of the City Clerk. That contractual language is consistent with the law of just cause. The Tribunal found that the evidence affirmatively showed that she was not a Holland resident for purposes of her sworn Affidavit. The Tribunal's factual findings also reflected on her residency for voting purposes. Both documents create at least an appearance of impropriety. The Tribunal's findings must bind the Arbitrator when he later reviews the City's determination that the false Affidavit could tarnish its image or weaken the public's trust. The Arbitrator failed to address this ground for termination, let alone to give preclusive effect to the Tribunal's relevant factual findings.

The Court of Appeals seems to think that the Arbitrator was presented with a different issue from the one the Tribunal faced. The court suggested that fraudulent intent is a relevant issue for determining just cause but not for identifying improper tax or voter filings. In other words, the court suggests that the issue of intent is a "relevant distinction" between the administrative findings and the arbitration. *Compare Dearborn Hts Sch Dist No 7*, 233 Mich App at 126 (discussing *Ingham Cty Emplee's Ass'n v Ingham Circuit Ct*, 170 Mich App 118, 428 NW2d 7 (1988)). That is mistaken. Intent is a distinction

without a difference here, because the potential for French's conduct to tarnish her office does not depend upon whether she intended to lie or even whether she engaged in impropriety. It depends upon whether there might be an appearance of impropriety – the same kind of appearance that judges and other leading officials must avoid. The Arbitrator's failures to deal with the issue and to accept the Tribunal's resolution of key facts were errors that must be reversed for the sake of municipalities and other employers state-wide.

To protect and serve their citizens, municipalities must have the power to determine whether leaders' conduct might create an appearance of impropriety that may tarnish the public office. When reviewing such cases, Arbitrators must be bound to the factual determinations of administrative agencies and courts who previously heard and adjudicated relevant factual issues. The Arbitrator refused to do that here, and the arbitration award should be vacated.

CONCLUSION AND RELIEF REQUESTED

Amici Curiae have a vital stake in the outcome here because the Arbitrator refused to acknowledge and apply controlling principles of employment, contract and other law in a way that presents a threat to municipalities across the state.

As the Holland's City Clerk, French was a leading and high-profile official. During her time there, she filed a false property-tax document, as well as a false voting document that concerned the core standards she was in charge of administering. At best, her conduct created an appearance of impropriety that could tarnish the City. Although the City presented this ground for termination to the Arbitrator, he refused to address it, instead focusing on intentional deception as the only basis for "just cause" termination under the contract. That result-driven approach contravened numerous controlling principles of contract, employment and procedural law that apply to all municipalities.

When handled properly, arbitration can present a good way for municipalities to resolve disputes without spending as much public money and without drawing unnecessary publicity and controversy. If the courts are impotent to correct this Arbitrator's failures, one of two things will happen, neither of which promotes good government. First, especially where leaders and high-profile officials are concerned, some municipalities will decide that the only way to get a fair shake is to avoid arbitration and fight these matters in court. But high-profile, salacious litigation over officials' ostensible misconduct diminishes public confidence in government. Alternatively, some municipalities will temporarily avoid the spotlight by figuring that they are

simply stuck with ill-fitting officials. Inevitably, the actual or apparent misconduct of those officials will surface and will further disappoint and diminish the public's trust. This can be avoided if municipalities have the reassurance that they will get a fair shake in arbitration because arbitrators will be bound to apply the law of just cause for leadership positions, and courts will not hesitate to correct arbitrators who fail to uphold these standards.

Accordingly, the League, the Defense Fund and the Section respectfully ask the Supreme Court to grant leave, reinstate the lower court's order vacating the arbitration award, and further hold that as a matter of law municipalities have just cause to fire a leading official for conduct that jeopardizes the public employer's reputation or affects the official's ability to lead in a public role. Alternatively, Amici respectfully request that the Court exercise its power under MCR 7.302(H) to grant immediate, peremptory relief to the same effect.

Respectfully submitted,

MILLER, CANFIELD, PADDOCK AND STONE, P.L.C.

By: _____

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Dated: September 5, 2013

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LIST OF APPENDICES EXHIBITS

Appx Ex

1. *In re Ligon*, _ SW3d _; No. 09-13-00242-CR, 2013 WL 4190402 (Tex App, Aug 14, 2013)

2. *Feltri v Kelaher*, No. A-5628-06T1, 2008 WL 1874427 (NJ App, April 30, 2008)

3. Juan Carlos Bisso & Albert H. Choi, *Optimal Agency Contracts: The Effect of Vicarious Liability & Judicial Error*, 28 Int'l Rev. L. & Econ. 166, 167 (Sept 2008)

EXHIBIT 1

2013 WL 4190402
Only the Westlaw citation is currently available.

Court of Appeals of Texas,
Beaumont.

In re Brett W. LIGON.

No. 09-13-00242-CR. | Submitted June 20, 2013. | Decided Aug. 14, 2013.

Synopsis

Background: Following trial court's order granting motions to appoint prosecutor pro tem and to disqualify district attorney from case in which he was complaining witness, district attorney petitioned for writ of mandamus.

Holdings: The Court of Appeals, Per Curiam, held that:

[1] trial court did not abuse its discretion by disqualifying district attorney, and

[2] trial court did not abuse its discretion by appointing prosecutor pro tem.

Petition denied.

Original Proceeding.

Attorneys and Law Firms

William J. Delmore III, for Brett W. Ligon.

Gilbert G. Garcia, for Joseph Michael Leners.

Katherine Shipman, for Robert Tyler Anderson.

Jerald D. Crow, for The State Of Texas.

Before McKEITHEN, C.J., GAULTNEY and HORTON, JJ.

Opinion

OPINION

PER CURIAM.

*1 The Montgomery County District Attorney, Brett W. Ligon, seeks mandamus relief from orders in misdemeanor prosecutions recognizing his disqualification and appointing a prosecutor pro tem. He is the complaining witness named in the charging instruments.

The trial court could reasonably conclude under the circumstances that the orders were required by due process of law. Because relator has not established a clear and indisputable right to the relief sought, we decline to issue a writ of mandamus compelling the trial court to vacate the orders.

THE CASES

Real parties in interest Joseph Michael Leners and Robert Tyler Anderson were arrested on warrants and charged by complaint and information with trespass. *See* Tex. Penal Code Ann. § 30.05(a) (West Supp.2012); *see* Tex.R.App. P. 52.2. Leners was also charged by complaint and information with burglary of a vehicle. [1] *See* Tex. Penal Code Ann. § 30.04(a) (West 2011). The entry on the property and the breaking in or entry in the vehicle are alleged by the State to be without the effective consent of the owner, Brett W. Ligon.

Leners and Anderson filed motions to disqualify the District Attorney due to his dual status in the cases. They supplemented the motions to specify that a failure to disqualify the District Attorney and his staff would violate due process. They asserted that the District Attorney is personally interested in the cases as a private citizen. The trial court signed orders granting the motions to disqualify and appointing a special prosecutor.

A trial court may appoint an attorney to represent the State "[w]henever an attorney for the state is disqualified to act[.]" Tex.Code Crim. Proc. Ann. art. 2.07(a) (West 2005). Relator contends the trial court may exercise this authority only when a district attorney voluntarily recuses himself. *See* Tex.Code Crim. Proc. Ann. art. 2.07(b-1) (West 2005); *see*

also Tex.Code Crim. Proc. Ann. art. 2.08 (West Supp.2012). Relator has not recused.

Relator does not distinguish recusal from disqualification. He asserts "[r]ecusal or disqualification is within the sole discretion of the elected district or county attorney, although the consequences of the exercise of that discretion are subject to review on appeal." He contends a defendant's only remedy for a due process violation is to seek reversal on appeal of the conviction.

A WRIT OF MANDAMUS

Relator argues he has no adequate remedy by appeal. *See State ex rel. Eidson v. Edwards,* 793 S.W.2d 1 (Tex.Crim.App.1990) (plurality opinion). He argues that a writ of mandamus is his appropriate remedy. *See* Tex.R.App. P. 52. The real parties in interest argue the trial court's decision was a judicial one concerning a matter on which the law is unclear, and a writ of mandamus is not appropriate in these circumstances. *See Bowen v. Carnes,* 343 S.W.3d 805, 810 & n. 6 (Tex.Crim.App.2011) (Relief may be granted when only one rational decision could be made under unequivocal, well-settled, clearly controlling principles.).

*2 [1] [2] The Court of Criminal Appeals has explained that, to be entitled to a writ of mandamus from an appellate court, "the State must demonstrate that: (1) there is no other adequate legal remedy, and (2) there is a clear and indisputable right to the relief sought." *State v. Patrick,* 86 S.W.3d 592, 594 (Tex.Crim.App.2002). When a trial court's ruling is a rational one supported by the law, and so does not represent a clear abuse of discretion, a writ of mandamus will not issue to compel a different ruling. *See State ex rel. Rosenthal v. Poe,* 98 S.W.3d 194, 198 n. 3 (Tex.Crim.App.2003). But a trial court has no discretion to rule on a matter when the court lacks authority to rule, or to decide a matter contrary to the law established by statute, rule, or a superior court. *See id.*

If the trial court clearly abused its discretion in ordering disqualification, a writ of mandamus will issue to require the trial court to vacate the order, assuming there is no other adequate legal remedy. *See Patrick,* 86 S.W.3d at 594. The real parties in interest do not dispute the relator's contention that he has no remedy by appeal. They contest only whether relator has shown a clear and indisputable right to mandamus relief.

[3] [4] "The standard of review for disqualification of the prosecutor by the trial court is whether the court abused its discretion." *Landers v. State,* 256 S.W.3d 295, 303 (Tex.Crim.App.2008). In ruling on the disqualification issue, "[t]he trial court abuses its discretion only when the decision lies 'outside the zone of reasonable disagreement,' " *Id.* The trial court's application of law is reviewed *de novo. Id.* This is an original proceeding not an appeal, but we consider a disqualification order for which there is no adequate remedy by appeal, and so we apply the appellate review standard in determining whether relator has shown a clear and indisputable right to a writ of mandamus.

DISQUALIFICATION

[5] As applied to prosecutors in Texas, disqualification and recusal are not interchangeable words. *See In re Guerra,* 235 S.W.3d 392, 410 (Tex.App.-Corpus Christi 2007, orig. proceeding [mand. denied]). Legal disqualification refers to the ineligibility to act as the prosecutor in a particular case. *See Coleman v. State,* 246 S.W.3d 76, 81 (Tex.Crim.App.2008) ("There are, however, a few instances in which the district attorney is legally disqualified from acting.)" Recusal refers to the voluntary removal of oneself as a prosecutor because of a conflict of interest or for other good cause. *See* Tex.Code Crim. Proc. Ann. art. 2.07(b–1); *Coleman,* 246 S.W.3d at 81. The trial court cannot require a prosecutor's recusal. *Coleman,* 246 S.W.3d at 81.

[6] Instances of legal disqualification are few. *Id.* The constitutional authority of a district attorney cannot be abridged or taken away. *See Eidson,* 793 S.W.2d at 4. Yet the State may not deprive a defendant of his liberty without due process of law. U.S. Const. amend. XIV. The trial court has the constitutional authority to decide questions of law in the case. *See* Tex. Const. art. II, § 1, art. V, § 1; Tex. Gov't Code Ann. § 21.001(b) (West 2004); *Armadillo Bail Bonds v. State,* 802 S.W.2d 237, 239–40 (Tex.Crim.App.1990); *Lytle v. Halff,* 75 Tex. 128, 12 S.W. 610 (1889). Consequently, "[a] district attorney may be disqualified only for a violation of the defendant's due-process rights[.]" *Landers,* 256 S.W.3d at 310.

*3 Legal disqualification may arise when the prosecuting attorney has dual roles in a criminal matter. *See In re Guerra,* 235 S.W.3d at 415–16 (A district attorney cannot assist a grand jury's criminal investigation of himself.). When *Guerra*

was decided, article 2.08 had not yet been amended to provide that a trial court may appoint an attorney pro tem to assist a grand jury in a criminal investigation of the district attorney. *See* Act of May 27, 1965, 59th Leg., R.S., ch. 722, § 2.08, 1965 Tex. Gen. Laws 317, 326 (amended by Act of May 27, 2011, 82nd Leg., R.S., ch. 977, § 2.08, 2011 Tex. Gen. Laws 2436, 2437 (West Supp.2011)) (current version at Tex.Code Crim. Proc. Ann. art. 2.08(b) (West Supp.2012)). The court in *Guerra* held nevertheless that article 2.07 authorized the trial court to appoint a prosecutor pro tem to investigate the elected district attorney. 235 S.W.3d at 414–15; *see* Tex.Code Crim. Proc. Ann. art. 2.07 ("[w]henever an attorney for the state is disqualified to act in any case or proceeding, ... the judge of the court in which he represents the state may appoint any competent attorney to perform the duties of the office during the absence or disqualification of the attorney for the state.").

Additionally, in *Guerra* the court found the trial court's appointment of a prosecutor pro tem "was implicitly authorized by a court's inherent power." *In re Guerra*, 235 S.W.3d at 415. By denying the district attorney the opportunity to participate in the grand jury's investigation into his own conduct, the appointment served to preserve the integrity of the court and aid in the administration of justice. *Id.*

In a separate issue in *Guerra*, the relator also challenged the particular prosecutor appointed, noting one of the allegations against relator involved election fraud, and the prosecutor pro tem was relator's opponent in the election. *Id.* at 428–29. The court decided under the circumstances of that case that the prosecutor pro tem was disqualified due to a conflict of interest that rose to the level of a due process violation. *Id.* at 431. The appellate court reasoned that a due process violation occurs where the prosecutor's personal interest generates a structural conflict that presents a potential for misconduct deemed intolerable. *Id.* at 430. The court also noted that under the circumstances the prosecutor pro tem "could be a material fact witness," and that if he testified "the confusion that would most likely result" from the "multiple roles as prosecutor, witness, and interested party would substantially affect the jury's verdict." *Id.* at 432.

The Court of Criminal Appeals cited *Guerra* and article 2.08 as "instances in which the district attorney is legally disqualified from acting," *Coleman*, 246 S.W.3d at 81 & n. 12 (citing *In re Guerra*, 235 S.W.3d at 420–24). The Court distinguished recusal from legal disqualification. *See id.* at 81. The recusal procedure "allows the district attorney to avoid conflicts of interest and even the appearance of impropriety by deciding not to participate in certain cases." *Id.* "The responsibility for making the decision to recuse himself is on the district attorney himself; the trial court cannot require his recusal." *Id.* But if a prosecutor is legally disqualified from prosecuting a case—if he is ineligible to act—the trial court is not powerless to protect the due process rights of the defendant. *See id.*; *Landers*, 256 S.W.3d at 305, 310.

*4 The briefs of the relator and the real parties in interest include citations to *Eidson* and *State ex rel. Hill v. Pirtle* to support the parties' respective positions. *See State ex rel. Hill v. Pirtle*, 887 S.W.2d 921, 932 (Tex.Crim.App.1994) (plurality opinion); *Eidson*, 793 S.W.2d at 1; *see also generally State v. Hardy*, 963 S.W.2d 516, 519 (Tex.Crim.App.1997) (discussing a plurality opinion's persuasive-versus-binding precedential effect). In *Eidson*, the trial court signed an order which "disqualified" the district attorney and his staff from a particular prosecution because an assistant district attorney had previously served in the case as counsel for the defendant. 793 S.W .2d at 3. In granting mandamus relief, the Court of Criminal Appeals noted that the office of district attorney being "constitutionally created and therefore constitutionally protected" cannot be abridged, and that the responsibility of recusal lies with the district attorney. *Id.* at 4, 6; *see also* Tex. Const. art. V, § 21.

In *Pirtle*, the Court of Criminal Appeals held that the trial court lacked authority to remove assistant attorneys general who were assisting the elected district attorney in a prosecution. 887 S.W.2d at 932. "[N]either an elected prosecuting attorney, nor his assistants, can be disqualified or prevented by a trial court from carrying out their duties to prosecute criminal cases." *Id.* The Court noted that "[i]n the instant case, the real parties in interest have not claimed their rights to due process were violated[.]" *Id.* at 927. And a concurring judge explained that "it is clear from the text of this opinion that the plurality judges do not mean [the trial court] would really have been without lawful authority to bar the AGs from serving as prosecutors had the evidence shown a conflict of interest rising to the level of a due process violation[.]" *Id.* at 933 (Meyers, J., concurring); *but see In re State ex. rel. Anderson*, 396 S.W.3d 653, 655 (Tex.App.-Houston 14th Dist.] 2013, orig. proceeding) ("[T]he trial court had no authority to order the disqualification of the Harris County District Attorney's office[.]").

In *Coleman*, the Court noted that *Eidson* had "discuss[ed] the distinction between legal disqualification and voluntary recusal[.]" *See Coleman*, 246 S.W.3d at 81 n. 14. And both *Pirtle* and *Eidson* describe the constitutional limitation on the holdings in those cases: the prosecutorial power granted to prosecuting attorneys is constrained by due process of law. *See Pirtle*, 887 S.W.2d at 927–28 ("A trial court may not disqualify a district attorney or his staff on the basis of a conflict of interest that does not rise to the level of a due process violation."); *Eidson*, 793 S.W.2d at 6 ("We do not wish to imply that a defendant would be left without recourse if the prosecution's failure to recuse itself violated his due process rights."); *see also* U.S. Const. amend. XIV.

*5 Few cases in any jurisdiction present situations where the prosecuting attorney is the alleged victim in the charged offense, or has a personal interest in the prosecution. We consider federal and state cases in other jurisdictions, not because of an interest in comparing the law of those jurisdictions, but because the guarantee of due process of law under the Constitution of the United States applies throughout the country. Although from other jurisdictions, court opinions addressing similar circumstances may identify uniform principles to be considered in addressing the due process guarantee.

In *People v. Zimmer*, 51 N.Y.2d 390, 434 N.Y.S.2d 206, 414 N.E.2d 705 (1980), the district attorney was also the corporate counsel and a stockholder of the corporation alleged to be the victim of the crimes. The court noted the broad discretion a prosecutor has "to investigate, initiate, prosecute and discontinue[,]" and observed "that, overall, more control over individuals' liberty and reputation may thus be vested than in perhaps any other public official[.]" *Id.* at 208.

> Even our thumbnail description of prosecutorial power is enough to indicate that resulting prejudice can at least as easily flow from an act of omission as from one of commission, from discretion withheld as from discretion exercised. In this context, whether abuse is express or implied may be difficult to determine....
>
> Thus, the practical impossibility of establishing that the conflict has worked to defendant's disadvantage dictates the adoption of standards under which a reasonable potential for prejudice will suffice[.]
>
> ...
>
> Assuming he intended to be as fair and objective as fair could be, in presenting this evidence where did his role as partisan corporate attorney end and where did that of nonpartisan District Attorney begin? At what point was he serving which of his two masters? To put the questions is to state the problem, a problem instinct with due process implications.

Id. at 208–09. In dismissing the indictment, the court emphasized that the responsibilities carried out in the name of the state must be conducted in a manner that "fostered rather than discouraged public confidence in our government" and in the rule of law. *Id.* at 208; *see also People v. Adams*, 20 N.Y.3d 608, 613, 964 N.Y.S.2d 495, 987 N.E.2d 272 (2013).

The Kentucky court in *May v. Commonwealth* considered the issue in an appeal from a conviction of a justice of the peace for assault and battery on a prosecutor. 285 S.W.2d 160, 162 (Ky.1955). The trial court had overruled the defendant's motion to remove the prosecutor. *Id.* The appellate court did not hold that the dual capacity was absolutely impermissible, but suggested that "looking at the whole proceeding objectively, we have a strong feeling that another attorney should have tried the action, in order to remove the self-interest factor and thereby reduce to a minimum the display of passion and prejudice that can scarcely be kept in abeyance where, as here, the same person was the victim of the offense and the prosecutor." *Id.* The appellate court reversed the conviction for improper argument by the prosecutor. *Id.* at 163–64. The decision arguably supports relator's position that a court should wait until specific identifiable prejudice develops. But the opinion also demonstrates some of the troubles inevitably presented when the alleged victim prosecutes the case.

*6 In an appeal from a trade secrets prosecution in California, the court considered the due process concerns that arise where the victim of the alleged crime contributes financially to the costs of the district attorney's investigation. *See People v. Eubanks*, 14 Cal.4th 580, 59 Cal.Rptr.2d 200, 927 P.2d 310, 312 (Cal.1996). The court reasoned that financial assistance to the prosecutor's office may disqualify the prosecutor if the assistance is of a character and magnitude as to render it unlikely that the defendant will receive fair treatment during all portions of the criminal proceedings. *Id.* California law disallows private prosecutions; all criminal prosecutions are conducted in the name of the People and by their authority. *Id.* The court explained that "a public prosecutor must be free of special interests that might

compete with the obligation to seek justice in an impartial manner [.]" *Id.* at 314–315.

> The importance, to the public as well as to individuals suspected or accused of crimes, that these discretionary functions be exercised "with the highest degree of integrity and impartiality, and with the appearance thereof" (*People v. Superior Court (Greer), supra,* 19 Cal.3d at p. 267, 137 Cal.Rptr. 476, 561 P.2d 1164) cannot easily be overstated. The public prosecutor " 'is the representative not of any ordinary party to a controversy, but of a sovereignty whose obligation to govern impartially is as compelling as its obligation to govern at all; and whose interest, therefore, in a criminal prosecution is not that it shall win a case, but that justice shall be done. As such, he is in a peculiar and very definite sense the servant of the law, the twofold aim of which is that guilt shall not escape or innocence suffer.' " (*Id.* at p. 266, 137 Cal.Rptr. 476, 561 P.2d 1164, quoting *Berger v. United States* (1935) 295 U.S. 78, 88 [79 L.Ed. 1314, 1321, 55 S.Ct. 629].)

Id. at 315. The court emphasized that the prosecutor represents the interest of the state in his role as prosecutor, and the interest is not that a case be won, but that justice be done. *See id.*

In Kansas, a defendant accused of planning to detonate an explosive device at the courthouse moved to disqualify the district attorney's office on the ground that the office was a crime victim. *State v. Cope,* 30 Kan.App.2d 893, 50 P.3d 513, 515 (Kan.Ct.App.2002). The court reasoned that a disqualifying conflict of interest affecting the defendant's due process rights occurs when the conflict is "so grave as to render it unlikely that the defendant will receive fair treatment during all portions of the criminal proceedings." *Id.* at 515–16. The court held, however, that the defendant's due process rights were not violated in that case because the defendant never directly threatened the district attorney's office. *Id.* at 516. Despite the distinction drawn by the court between the levels of threat to the prosecutor, the reasoning cautions that a prosecutor's status as a direct crime victim poses a due process problem.

*7 In a domestic assault case, a federal habeas court found a due process violation occurred where the prosecuting attorney was also representing the victim in the parties' divorce. *See Ganger v. Peyton,* 379 F.2d 709, 713 (4th Cir.1967). The court reasoned that "the conduct of this prosecuting attorney in attempting at once to serve two masters, the people of the Commonwealth and the wife of Ganger, violates the requirement of fundamental fairness assured by the Due Process Clause of the Fourteenth Amendment." *Id.* at 714; *see also generally Wright v. United States,* 732 F.2d 1048, 1056 (2nd Cir.1984) (A prosecutor "is not disinterested if he has, or is under the influence of others who have, an axe to grind against the defendant[.]").

Although relying on "supervisory authority to avoid the necessity of reaching any constitutional issues[,]" the United States Supreme Court in *Young v. United States ex rel. Vuitton et Fils. S.A.,* 481 U.S. 787, 809 n. 21, 107 S.Ct. 2124, 95 L.Ed.2d 740 (1987), showed the obstacle to fundamental fairness presented when a prosecutor has a private interest in the case.

> A prosecutor exercises considerable discretion in matters such as the determination of which persons should be targets of investigation, what methods of investigation should be used, what information will be sought as evidence, which persons should be charged with what offenses, which persons should be utilized as witnesses, whether to enter into plea bargains and the terms on which they will be established, and whether any individuals should be granted immunity.

Id. at 807. Injecting a personal interest into the enforcement process may bring irrelevant or impermissible factors into the exercise of that discretion. *Id.* at 808. The problem is structural. *Id.* at 807. "It is a fundamental premise of our society that the state wield its formidable criminal enforcement powers in a rigorously disinterested fashion, for liberty itself may be at stake in such matters." *Id.* at 810. And when the prosecutor has a personal interest in the case, the circumstance "diminishes faith in the fairness of the criminal justice system in general." *Id.* at 811.

CONCLUSION

[7] [8] The United States Supreme Court has held that, although prosecutors "are necessarily permitted to be zealous in their enforcement of the law[,]" due process imposes limits. *See Marshall v. Jerrico, Inc.,* 446 U.S. 238, 242, 248–50, 100 S.Ct. 1610, 64 L.Ed.2d 182 (1980) (administrative prosecution); *Berger v. United States,* 295 U.S. 78, 55

S.Ct. 629, 79 L.Ed. 1314 (1935). This Court presumes no misconduct in these cases. But that does not eliminate the structural conflict and the obstacle to due process. The constitutional guarantee of due process preserves the appearance and the reality of fundamental fairness. *See Marshall*, 446 U.S. at 242, 248–250. In rare instances, when a structural conflict is actual and obvious and the "potential for misconduct is deemed intolerable" so as to constitute a due process violation, no showing of a specific prejudice is necessary to require disqualification. *See Young*, 481 U.S. at 807 n. 18; *see also Marshall*, 446 U.S. at 248–50; *Landers*, 256 S.W.3d at 304; *Ex parte Spain*, 589 S.W.2d 132, 134 (Tex.Crim.App.1979).

*8 [9] The indisputable facts of these cases are that the district attorney, in whose office is solely vested the State's power to prosecute offenses of this level in Montgomery County, is the victim alleged in the charging instruments. *See* Tex. Gov't Code Ann. § 43.105(b) (West 2004). In signing the orders, the trial court implicitly recognized the discretionary powers of a prosecutor and the importance of the appearance of "fairness of the criminal justice system in general" identified in *Young*. 481 U.S. at 807, 811. But more specifically, from the facts before the court in these cases when the orders were signed, the trial court could reasonably find that relator would not recognize the legal disqualification, that relator had a personal interest in the prosecution, that jeopardy would attach with relator acting in dual roles as the district attorney responsible for the prosecutions and as the alleged victim, and that relator would be a trial witness. The trial court could, on these findings, rationally conclude that relator's competing roles, as both district attorney and complainant, present an "intolerable" potential to compromise the fundamental fairness guaranteed defendants by the due process clause. *See Young*, 481 U.S. at 807 n. 18 ("deemed intolerable"); *Marshall*, 446 U.S. at 248–50; *Ganger*, 379 F.2d at 713; U.S. Const. amend. XIV. In these circumstances, the trial court could reasonably conclude that the actual and obvious structural conflict amounted to a denial of due process and a legal disqualification. *See Young*, 481 U.S. at 807–08; *Landers*, 256 S.W.3d at 304.

[10] Relator appoints the assistant district attorneys who carry out the duties of his office. *See* Tex. Gov't Code Ann. § 43.105(c) (West 2004). Following uniform case-law, the trial court could reasonably rule that because the District Attorney is disqualified, all Assistant District Attorneys in the district are also disqualified. *See Marbut v. State*, 76 S.W.3d 742, 748–49 (Tex.App.-Waco 2002, pet. ref'd); *Scarborough v. State*, 54 S.W.3d 419, 424 (Tex.App.-Waco 2001, no pet.); *State v. May*, 270 S.W.2d 682, 684 (Tex.Civ.App.-San Antonio 1954, no writ). *See also generally, Edwards*, 793 S.W.2d 1, 5–6 n. 5 ("*May*, however, stands only for the proposition that *if* an elected district attorney has been lawfully disqualified from prosecution of certain causes, so have his assistants who serve at his will and pleasure."). A trial court may appoint a prosecutor pro tem if a district attorney is legally disqualified. Tex.Code Crim. Proc. Ann. art. 2.07.

[11] To obtain a writ of mandamus from an appellate court requiring a trial court to withdraw an order, the relator must demonstrate not only that there is no adequate legal remedy, but also that there is a clear and indisputable right to the relief. *Greenwell v. Court of Appeals for Thirteenth Judicial Dist.*, 159 S.W.3d 645, 648 (Tex.Crim.App.2005). We cannot say the trial court's disqualification decision "lies 'outside the zone of reasonable disagreement.' " *See Landers*, 256 S.W.3d at 303. On the mandamus record presented, relator has failed to show a clear and indisputable right to the relief sought. *See Patrick*, 86 S.W.3d at 594. The petition for writ of mandamus is therefore denied.

*9 PETITION DENIED.

Footnotes

1 Anderson was indicted for burglary of a vehicle as a repeat offender. *See* Tex. Pen.Code Ann. § 30.04(d)(2) (West 2011). That case is not at issue in this mandamus proceeding.

End of Document

EXHIBIT 2

2008 WL 1874427
Only the Westlaw citation is currently available.

UNPUBLISHED OPINION. CHECK COURT RULES BEFORE CITING.

Superior Court of New Jersey, Appellate Division.

Sean FELTRI, Plaintiff-Appellant,
v.
Thomas F. KELAHER (misspelled "Kellaher"), Ocean County Prosecutor, Office of The Ocean County Prosecutor, and County of Ocean, Defendants-Respondents.

Argued April 15, 2008.
Decided April 30, 2008.

On appeal from the Superior Court of New Jersey, Law Division, Ocean County, L-2685-05.

Attorneys and Law Firms

David J. De Fillippo argued the cause for appellant (Klatsky Sciarrabone & De Fillippo, attorneys; Mr. De Fillippo, of counsel and on the brief).

R. Scott Clayton argued the cause for respondents (Berry, Sahradnik, Kotzas & Benson, attorneys; Mr. Clayton, on the brief).

Before Judges WINKELSTEIN, YANNOTTI and LEWINN.

Opinion

PER CURIAM.

*1 Plaintiff, Sean Feltri, was an investigator with the Ocean County Prosecutor's office. He appeals from a May 23, 2007 order of the Law Division affirming the prosecutor's termination of his employment. We affirm.

Since 2001, while an employee of the prosecutor's office, plaintiff received favorable job performance evaluations. He had, however, been involved in a physical altercation in 2003 for which he received a disciplinary charge and was temporarily suspended.

The events that resulted in plaintiff's termination occurred on the evening of June 5, 2005, beginning at approximately 11:30 p.m. A police patrol car was parked in front of Temptations bar, facing south on the shoulder of the northbound lane of the Boulevard in Seaside Heights, when plaintiff drove his car past. Both plaintiff and his passenger, Joseph Cohen, an off-duty police officer, had been drinking since approximately 4:00 p.m. Plaintiff had consumed six to seven beers and a "shot" of hard liquor.

Two on-duty police officers, Patrolmen Jason Mahr and Jason Mroczka, were in the parked patrol car when plaintiff drove by. They followed plaintiff's car and pulled it over into the parking lot of a bar. Mahr called Sergeant Thomas Yannacone for backup. Prior to Yannacone arriving, Patrolman Victor Tomaro also arrived on the scene. Plaintiff and the officers engaged in heated discussions. Ultimately, Yannacone demanded and received plaintiff's keys.

At approximately 12:43 a.m. on June 6, 2005, plaintiff called the Seaside Heights Police Department and left a voice mail message for Yannacone. The message was saved and transcribed. Plaintiff stated:

> Hey let me tell you something, I know this line's being taped. I'm just gonna tell you this right now, I know that what you did was personal and let me tell you something. Those assholes had no probable cause to stop me and you had no probable cause to do what you [did] so I just hope you know that and I hope that you know that I'm gonna forward this information to whoever I can because you know what, you were fuckin, you went overboard and you're gonna pay the price.

Several minutes later, plaintiff again called Sergeant Yannacone.

> Yannacone: Sergeant Yannacone.
>
> Plaintiff: Hey Tommy it's Sean Feltri, how are you?
>
> Yannacone: Okay.
>
> Plaintiff: Good, Uh I just want to let you know I just uh left a message on your voice mail, I'm gonna be talking to your superiors about this so called motor vehicle stop that I was on and we're gonna hash it out during the week.

> Yannacone: Sean that's fine, you do whatever you have to do. My officers were in the right, they did what they did and I did what I did and I felt that it was in your best interest due to the state of mind that you were in. If you want to debate that you have every right to do so.
>
> Plaintiff: Great.
>
> Yannacone: Okay?
>
> Plaintiff: Thank you very much.
>
> Yannacone: Take care.

The prosecutor brought three disciplinary charges against plaintiff stemming from these incidents: (1) misconduct pursuant to *N.J.S.A.* 2A:157-10.1; (2) conduct unbecoming an investigative member of the prosecutor's office; and (3) failure to report the incidents. A disciplinary hearing was held before Kenneth Fitzsimmons, a hearing officer, on July 19 and 22, 2005, where the officers involved in the incident testified. Plaintiff also testified, as did his supervisor in the prosecutor's office, and another officer, who saw plaintiff earlier in the evening on the date of the incident.

*2 We will not repeat the verbatim testimony of the witnesses. Suffice it to say that officers Mahr and Mroczka, and Sergeant Yannacone, all testified that plaintiff appeared to have been drinking. He gave the officers a hard time, cursed them, used other derogatory language, and threatened their jobs.

Cohen testified that he and plaintiff were "impaired," but not "falling down" drunk. He did not hear plaintiff use the word "fuck," but plaintiff was "arrogant" to the officers. Cohen testified that plaintiff did not threaten the officers' jobs or call them "assholes."

Plaintiff's supervisor at the prosecutor's office testified that plaintiff was "one of the finest investigators [he] ever worked with," and the other officer testified that plaintiff did not appear impaired earlier in the evening of the incident.

Plaintiff disputed the testimony of the prosecutor's witnesses. He testified that as he was passing by Temptations bar, he saw a patrol car "parked against the flow of traffic with its rear passenger side partially into [his] lane of travel." He slowed down, "tapped the horn a few times and traveled around" the patrol car. He believed he was traveling approximately twenty-five to thirty miles per hour.

After parking at Captain Hooks and getting out of his car, an officer told him to get back in the car and he complied. When the officer then asked for his identification, plaintiff identified himself as an investigator for the prosecutor's office. He claimed that the officers were rude to him but that he never threatened their jobs. He testified that it was a "good possibility," however, that he used profanity towards the officers and a "possibility" that he called them "assholes." Plaintiff did not remember telling Yannacone to "go fuck himself," as Yannacone had testified. At the hearing, plaintiff had no memory of his first call to Yannacone in which he left a message.

The hearing officer found plaintiff guilty of all charges and recommended suspension without pay for 180 days. The prosecutor rejected the hearing officer's suggested penalty and terminated plaintiff.

Plaintiff appealed de novo to the Superior Court. On February 9, 2007, Judge Buczynski issued an oral decision, which he memorialized in a February 23, 2007 order. The court found plaintiff guilty of the first two counts, and not guilty on count three. The court said:

> The Court finds though as a fact that there was sufficient consumption of alcohol by [plaintiff and Officer Cohen] that it influenced their behavior or judgment. It does not find, however, that either of the officers were intoxicated to the extent that it would necessarily have violated a State Statute.
>
> ....
>
> The Court finds though that based on the totality of the reports by Mr. Mahr and Mr. Mroczka and [plaintiff] that his vehicle was exceeding the speed limit on that evening in question which would give rise to probable cause to stop the vehicle.
>
> *3 ... Both Patrolman Mahr and Patrolman Mroczka indicate in their reports and on testimony that when they stopped the vehicle [plaintiff] began the encounter by stating, "What the F," and that's an expletive deleted, "did you pull me over for?" ...
>
> The Court finds that, in fact, this occurred.
>
> ....

[Plaintiff] admits that he probably used inappropriate language or foul language to the officer, although he does not recall the exact use of those words....

The Court does note that although he did utilize the language as explained by Mr. Mahr and Mr. Mroczka, that this language alone would not support a charge of misconduct under *N.J.S.A.* 2A:157-10.1 although it would be characterized as offensive.

The most salient part of the testimony and the reports by Officers Mahr and Mroczka pertained to the alleged threat that [plaintiff] made during the stop. Patrolman Mahr stated in his report under P-4 and again under oath that [plaintiff] threatened his employment by saying, "I'll have your job." ...

The Court also considered the report of Officer Mroczka in this area, and he too corroborates that [plaintiff] made that threat.

The Court finds as a matter of fact that, in fact, [plaintiff] did indicate to one of the officers in the presence of both that he would have their job, and that constituted a threat against their employment.

Patrolman Cohen, also sitting in the Jeep during the exchange, corroborates [plaintiff's] chastising of these officers. When Mr. Cohen was asked if [plaintiff] showed any disrespect to the officers, he responded, quote, "[y]eah, but in a way that I necessarily wouldn't have acted. If it's disrespectful then, you know," close quote.... And when Mr. Cohen was asked whether he thought [plaintiff] was being arrogant to the patrolman, he responded, "[s]ure, he was arrogant." Mr. Cohen also indicated ... that [plaintiff showed] a lack of judgment and that he was impaired and/or intoxicated....

I am satisfied that the behavior as characterized as disrespectful towards those police officers, in fact, did occur.

... After Sergeant Yannacone arrived, [plaintiff] indicated that he and the sergeant were, in fact, yelling at each other and that during this exchange he may have possibly referred to Patrolman Mahr and Mr. Mroczka as, quote, "a-holes," expletive deleted....

I'm satisfied that, in fact, during this conversation that characterization of those officers did, in fact, occur.

....

Within one hour after this encounter [plaintiff] made two separate phone calls to the Seaside Heights Police Department....

....

Those two calls, the first one in particular, supports the charge that [plaintiff], in fact, was utilizing his position to threaten the employment of the other parties. It further corroborates statements made by the prior officers prior to the stop and ultimately amounts to misconduct that is recognizable under 2A:157-10.1.

*4 I'm satisfied that [plaintiff's] stop was based upon probable cause resulting from the speeding and sounding of the horn.

....

In furtherance of the Court deciding on the credibility of [plaintiff], it had the opportunity to review and to listen to the video tape of his deposition which occurred approximately seven days after the events on July 22nd. During that interview[, plaintiff] denied leaving the verbal statement on the voice mail. The Court does not find that as a matter of lacking credibility but simply corroborates the fact that he was, in fact, influenced by the consumption of alcohol that evening and his memory because of that in some way was lacking.

....

The Court does find though that [plaintiff] did violate the internal rules and regulations and Code of Conduct and Ethics....

....

Therefore, based on the Court's findings that, in fact, [plaintiff] threatened two police officers with the loss of their job, his innapropriate behavior during the course of that stop, his voice mail that he left to Sergeant Yannacone that evening, all corroborates the findings of this Court that there was official misconduct under 2A:157-10.1; that he did exhibit a lack of judgment, unprofessional conduct, and disrespect towards fellow police officers. He did abuse his position as an investigator for the Ocean County Prosecutor's Office. And that, in fact, he violated the internal rules and regulations and the Code of Conduct....

The court did not impose a penalty at that time. Plaintiff subsequently moved to compel discovery of the disciplinary records of other investigators on the prosecutor's staff. The court denied the motion, finding that whether other members of the prosecutor's staff had been disciplined was irrelevant to plaintiff's potential penalty.

On May 18, 2007, the court issued an oral decision affirming plaintiff's termination. The judge made the following pertinent findings:

> [I have] examined the record favorable to the plaintiff including the plaintiff's police and fire training, his job history, commendations and award [s] issued to plaintiff in his capacity as a law enforcement officer and volunteer firefighter in addition to periodic evaluation reports issued while employed at the Ocean County Prosecutor's Office.
>
> Nonetheless, this Court's decision is to affirm the decision of Prosecutor Thomas Kelaher to terminate [plaintiff's] employment. This Court adheres to the adage that a police officer is a special kind of public employee. He represents law and order to the citizenry and must present an image of personal integrity and dependability in order to have the respect of the public....
>
> [Plaintiff] had opportunities in advance of the internal investigation to come forward and honestly disclose his inappropriate behavior and lack of good judgment, but chose to do otherwise.... [Plaintiff's] behavior is evidenced by the two significant convictions sustained by this Court which cannot be tolerated. This Court finds plaintiff's utility as a credible investigator [has] been irreparably undermined.

*5 On appeal, plaintiff's primary argument is that the evidence was insufficient to warrant his conviction. That argument is without merit.

Under the County Detectives and County Investigators Act, *N.J.S .A.* 2A:157-1 to -23, the county prosecutor has the power to appoint and remove county investigators. *N.J.S.A.* 2A:157-10. *N.J.S.A* . 2A:157-10.1 provides, in part:

> Except as otherwise provided by law, a county investigator employed by the county prosecutor shall not be removed from office, employment or position for political reasons or for any cause other than incapacity, misconduct, or disobedience of rules and regulations established by the prosecutor, nor shall such investigator be suspended, removed, fined or reduced in rank from or in office, employment, or position therein, except for just cause as hereinbefore provided....

N.J.S.A. 2A:157-10.7 provides county investigators with the right of de novo review in the Superior Court for disciplinary convictions and penalties. "The court shall hear the cause de novo on the record below and may either affirm, reverse or modify such conviction." *Ibid.* On appeal from the trial court, this court plays "a limited role in reviewing the de novo proceeding." *In re Phillips*, 117 *N.J.* 567, 579 (1990). We decide only whether the trial court's decision was "supported by substantial credible evidence in the record as a whole" and was not "arbitrary, capricious or unreasonable." *Ibid.* The quantum of proof for a disciplinary proceeding is the preponderance of the evidence. *Id.* at 575.

Applying this standard of review, we find no basis to overturn Judge Buczynski's well-reasoned decision. The Prosecutor's Office Employment Policy Manual provides, in part:

> The members of the staff, in addition to performing their assigned duties, must cooperate with each other, municipal police departments and the public and must display loyalty to the goals and philosophy of the Office.... It is of paramount importance that the Office earn and maintain the confidence and respect of the law enforcement agencies with which the Office works and with which the Office shares information. Similarly, the Office must work to earn the confidence and trust of the public at large....

The policy manual also includes a Code of Ethics applicable to all employees of the prosecutor's office, which provides, in part: "DUTIES AND PROHIBITIONS ... No county prosecutor or employee of a county prosecutor's office may use an official position to secure unwarranted privileges, benefits, or advantages for any person or to impose unwarranted burdens or disadvantages on any person."

The policy manual includes a Standard of Conduct applicable to all employees of the prosecutor's office. It provides, in part:

> Personnel in both their private and public lives shall conduct themselves in a manner that will not reflect adversely on the reputation of the Ocean County Prosecutor's Office. They shall maintain the dignity and integrity of their office through exemplary conduct and adherence to all administrative policies, rules and regulations. They shall maintain respect for the welfare and rights of all citizens.... They shall recognize that service in the Ocean County Prosecutor's Office is a public trust requiring dedication to ethical principles of the highest order.... All employees are reminded that acceptance of a position with the Prosecutor's Office places them at a standard above and beyond that of the average citizen.

*6 In light of these standards, as to count one, misconduct pursuant to *N.J.S.A.* 2A:157-10.1, the court found that plaintiff had made "two calls, the first one in particular ... utilizing his position to threaten the employment of the other parties. It further corroborates statements made by the [other officers at] the stop and ultimately amounts to misconduct that is recognizable under 2A:157-10.1."

As to count two, conduct unbecoming a county investigator under the rules and regulations of the prosecutor's office, the court found that plaintiff had exercised a "lack of judgment, unprofessional conduct, and disrespect towards ... fellow police officers, and that he abused his position as an investigator with the Prosecutor's Office."

The record supports those findings. The trial court found that plaintiff threatened the job of one of the officers. Both in their reports and at trial, Mroczka and Mahr asserted that plaintiff told them he would "have [their] fucking jobs." Plaintiff denied making the statement, but the court found that his memory was "influenced by the consumption of alcohol that evening." Plaintiff admitted consuming several beers and a shot of hard liquor that evening and Cohen testified that they were both "impaired." Yannacone smelled alcohol on plaintiff's breath and observed that plaintiff's pupils were dilated.

The court also found that plaintiff "utiliz[ed] his position to threaten the employment" of the officers in his phone calls to the Seaside Heights Police Department that evening, which constituted misconduct under *N.J.S.A.* 2A:157-10.1. Plaintiff's message and subsequent phone call to Sergeant Yannacone support this finding.

The court credited Mroczka's testimony that plaintiff repeatedly called Mahr and Mroczka "assholes." Both officers' reports corroborate that plaintiff was uncooperative and asked repeatedly, "why the fuck did you pull me over?" Cohen testified that plaintiff was "arrogant" to the officers. Yannacone testified that plaintiff called him and the other officers "assholes"; that plaintiff told him repeatedly to "go fuck [him]self," and "this is bullshit"; and that plaintiff referred to the officers as "jerkoff specials." Plaintiff admitted in his testimony that there was a "good possibility" that he used profanity towards the officers and a "possibility" that he called them "assholes."

The record supports the court's findings that plaintiff's actions were sufficient to warrant his convictions for misconduct under *N.J.S.A.* 2A:157-10.1 and for conduct unbecoming a county investigator under the rules and regulations of the prosecutor's office. According to the evidence accepted by the trial court, plaintiff repeatedly used his position to threaten the jobs of Yannacone, Mahr, and Mroczka. He was uncooperative with the officers and reflected an attitude of general disrespect for their positions by referring to them in derogatory language. His actions are inconsistent with the public's expectations of an individual entrusted with his authority, and they undermine public trust in the prosecutor's office and inter-departmental cooperation with municipal police departments.

*7 Plaintiff further asserts that the penalty, termination of his employment, was severe, excessive and arbitrary, and "runs afoul of the basic tenets of the 'progressive discipline' doctrine." We disagree. The trial court's reasons for termination of plaintiff's employment were fully supported by the record.

Plaintiff relies on *In re Carter*, 191 *N.J.* 474 (2007), in support of his argument. In *Carter*, the Court described progressive discipline as the principle that a proposed

sanction may be based on more than the "severity of the current infraction alone ." *Id.* at 483. A prior disciplinary record is "inherently relevant to determining an appropriate penalty for a subsequent offense." *Ibid.* (internal quotations omitted).

The concept of progressive discipline is not, however, a "fixed and immutable rule to be followed without question." *Id.* at 484. "[S]ome disciplinary infractions are so serious that removal is appropriate notwithstanding a largely unblemished prior record." *Ibid.* "[T]he question for the courts is whether such punishment is so disproportionate to the offense, in light of all the circumstances, as to be shocking to one's sense of fairness." *Ibid.* (internal quotations omitted).

In light of the seriousness of plaintiff's convictions, the penalty imposed was not "so disproportionate to the offense ... as to be shocking to one's sense of fairness." *Ibid.* The judge found that plaintiff's use of his position to threaten fellow law enforcement officers' jobs; his lack of judgment; his disrespect of fellow law enforcement officers; and his general conduct were inconsistent with the expected conduct of an officer entrusted with the public's welfare. The record supports the court's conclusions.

Plaintiff's remaining arguments are without sufficient merit to address in a written opinion. *R.* 2:11-3(e)(1)(E).

Affirmed.

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EXHIBIT 3

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OPTIMAL AGENCY CONTRACTS: THE EFFECT OF VICARIOUS LIABILITY AND JUDICIAL ERROR

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ABSTRACT

Under the doctrine of vicarious liability, a deep-pocket principal is often held responsible for a third-party harm caused by a judgment-proof agent's negligence. We analyze the incentive contract used by the principal to control the agent's behavior when a court can make an error in determining the agent's negligence. We show that (1) reducing the error of declaring the agent not negligent even when he was (pro-defendant or type II error) is better than reducing the error of declaring the agent negligent even when he was not (pro-plaintiff or type I error) and (2) allowing the principal to penalize the agent even when the court declares the agent not negligent improves welfare. The latter supports the argument that causing an accident (or a reliable allegation of misconduct) should be sufficient to justify a "just cause" termination of an employee.

1. Introduction

Courts often impose liability not only on the injurer (e.g. an agent), but also on a party (e.g. a principal) that has the means to control the injurer's actions. This is the principle of vicarious liability, which is justified on the grounds that the agent tends to have insufficient assets to pay for the harm he causes and so will have suboptimal incentive to take care when performing a potentially hazardous task. Making the deep-pocket principal also liable for the harm will induce her to exert better control over the agent's actions, for instance, through better monitoring or a stronger incentive scheme. [1] While attempting to control the agent's behavior through the principal may not be the perfect solution, vicarious liability can alleviate the agent's judgment-proof problem and make the agent take more socially beneficial care.

We build a simple model of vicarious liability in which a principal attempts to control a judgment-proof (and risk-averse) agent's behavior using an incentive contract. The court holds the principal liable for the third-party harm caused by the agent only when it determines the agent to have been negligent. [2] Although the agent's behavior is not observable to anyone, we assume that the court, at trial, obtains evidence (particularly from the harmed third party) that correlates with the agent's behavior and uses this evidence to determine the agent's negligence. We consider two possibilities: (1) a court that finds out the agent's true behavior for certain and (2) a court that can commit an error by either declaring the agent negligent even when he was not (pro-plaintiff or type I error) or declaring the agent not negligent even when he was (pro-defendant or type II error). The court's judgment, which is correlated with the truth, becomes an additional contractible signal for the principal to control the agent's behavior. [3]

*167 When the court does not make any error, imposing vicarious liability can induce the principal to provide care incentive to the agent: If the agent is risk-neutral, court's perfect information can allow the principal to completely eliminate the rent that might have accrued to the agent (due to judgment-proofness) and achieve the first best. If the agent is risk-averse, because the optimal compensation punishes the agent for causing an accident and imposes risk on the agent, the principal will have to compensate the agent for that risk. For that reason, the first best may not be achieved. If the court can commit an error, now the agent may be exposed to two sources of risk: probabilistic accident and court error. The principal will need to compensate the agent even more for the increased exposure to risk and she becomes less likely to induce efficient care from the agent. Even if the agent is risk neutral, because the court's judgment becomes a less informative signal of the agent's behavior, the principal finds it more expensive (due to the rent left to the agent) to provide care incentive to the agent. [4]

We then compare the relative importance of two types of error. Reducing the pro-defendant (type II) error increases the principal's expected liability from not inducing care from the agent. On the other hand, reducing the pro-plaintiff (type I) error decreases the principal's expected liability from inducing care from the agent. What is important, from the principal's perspective, is how the difference in the two expected liabilities changes with respect to the reduction in error. However, because the accident and the (subsequent) court adjudication are more likely when the agent has not taken care than when he has, a marginal reduction in the court's pro-defendant (type II) error will have a bigger impact on the difference than a marginal reduction in the court's pro-plaintiff (type I) error. Therefore, reducing the pro-defendant (type II) error is more beneficial than reducing the pro-plaintiff (type I) error. In short, what is important is not only the court's propensity to commit an error but also the chances that the court will be in the position to commit such an error. [5] We also show that reducing the pro-defendant (type II) error better aligns the principal's marginal cost with the social marginal cost of inducing care. [6]

Finally, we consider a regime where the principal is prohibited from penalizing the agent when the agent is declared not negligent by the court. One could argue that since the court exonerated the agent ex-post, the principal should be forbidden from, for instance, terminating the agent's employment. We show that without any restrictions on contract, the principal will often penalize the agent for causing an accident regardless of a court's subsequent judgment. The reason is that while the court's judgment may be informative, the combination of an accident (which is suggestive of the agent's negligence) with the court's declaration of non-negligence provides only a weak (and conflicting) signal about the agent's behavior to the principal. If the principal cannot penalize the agent after the court's declaration of non-negligence, controlling the agent's actions requires the principal to leave a larger economic rent to the agent. As a result, inducing care becomes more expensive and the principal becomes less likely to induce care.

This finding has a normative implication for the wrongful discharge doctrine in employment law. While at-will employees can be discharged for almost any reason, the courts are split on whether discharging a definite-term employee for alleged misconduct will violate the employer's implied promise that the employee will be discharged only for "just cause." [7] Specifically, should an employer be allowed to discharge a definite-term employee for causing an accident, even before a court determines that the employee has been negligent? Not only does our analysis say yes, it goes further to argue that even if the employee is later exonerated by a court, the employer should not be liable for wrongful termination. Allowing the employer to sanction

the employee based on a good faith (or reasonable) allegation of misconduct or harm, regardless of subsequent judicial determination, enables the employer to better solve the moral hazard problem.

The paper is organized as follows: in the next section, we present a simple principal-agent model, where the agent is judgment-proof so that neither the principal nor the court can impose a monetary sanction on the agent's personal assets. We assume that while the principal is risk-neutral, the agent can be risk-averse. The agent can take care, which is unobservable to the principal, to reduce the probability of harm, and the court holds the principal liable for the harm only after finding the agent negligent. We analyze two cases: (1) a court that perfectly discovers the agent's behavior and (2) a court that can err in favor of the plaintiff (type I error) or in favor of the defendants (type II error). We also conduct policy experiments of (1) reducing the court's propensity in making errors and (2) imposing a "just cause" termination condition that prohibits the principal from sanctioning the agent when the court declares the agent not negligent. The final section concludes with suggestions for future research.

2. The model

There are four players: a principal, an agent, a third party, and a court; the agent is (weakly) risk-averse while the other players *168 are risk-neutral. [8] There are four periods t # (1, 2, 3, 4) and there is no time discounting. In the first period ($t = 1$), the principal hires the agent and offers an employment contract, <<EQUATION>>, that stipulates state-contingent payments to the agent. We will be more precise about the terms of this contract. In the second period ($t = 2$), when performing his duty, the agent can either take care ($e = 1$) or be careless ($e = 0$) at cost #(e). We assume that the agent chooses e to maximize his quasi-linear expected utility << EQUATION>>, where <<EQUATION>> and <<EQUATION>>. Although being careless costs the agent nothing, <<EQUATION>>, taking care imposes a non-monetary cost of << EQUATION>> on him. We assume that whether the agent takes care or not is unobservable to the principal, so that this choice cannot be directly contracted upon. [9] On the other hand, the court, in the process of adjudication, collects (previously unavailable) evidence regarding the agent's behavior, so that the court's judgment either partially or fully correlates with the agent's behavior. [10]

At $t = 3$, the principal receives an expected revenue of $R > 0$ from the venture. [11] Depending on the agent's choice of care (e), the third party suffers a verifiable harm ($L > 0$) with probability <<EQUATION>>. We assume that <<EQUATION>>, so that the accident that causes the harm is less likely to occur when the agent takes care. We also assume that taking care is more efficient, i.e. <<EQUATION>>, and the legal standard is such that the agent is negligent only when $e = 0$. If there is no accident, the game proceeds to $t = 4$. If the third party suffers harm, she always sues the principal under the doctrine of vicarious liability. [12] We assume that the agent has no personal assets and therefore cannot satisfy any court judgment, i.e. he is judgment-proof. At the same time, the principal becomes liable for the harm only when the agent is declared negligent. [13] The court declares the agent to have been negligent ($e = 0$) with probability <<EQUATION>>, where << EQUATION>>. From the assumptions, q_1 represents the pro-plaintiff (type I) error, where the court declares agent negligent even though the agent was not, while ($1 - q_0$) represents the pro-defendant (type II) error, where the court finds agent not negligent even though the agent was. [14] For simplicity, we assume that litigation is costless for all the parties, [15] and the third party cannot affect the probability of accident. [16]

At $t = 4$, payoffs are realized. If there was no accident in $t = 3$, the principal pays the agent <<character cannot be displayed>>. If there was an accident but the court declared the agent not negligent, the principal pays the agent <<character cannot be displayed>>. Finally, after the accident and the court's declaration that the agent was negligent, the principal compensates the third party for her loss (L) and pays the agent <<character cannot be displayed>>. Since the agent is judgment-proof, we assume that all payments to the agent must be weakly positive: <<EQUATION>>. The three state-contingent transfers, in effect, become the contract (K) that the principal offers to the agent at $t = 1$. We assume that the agent has an outside reservation value of $u(0)$, so that, in equilibrium, we must have <<EQUATION>>. We also assume that the principal designs K to maximize her expected profit: <<EQUATION>>

2.1. Benchmarks

As a benchmark, consider a legal regime that only makes the agent, and not the principal, liable for the third-party harm. Since the principal will never be liable, her only source of cost is the agent's compensation. If she wants the agent to take care ($e = 1$), she will have to compensate him at least for the cost of effort (#). On the other hand, if she does not want to induce care ($e = 0$), she can simply pay the agent zero in every state <<EQUATION>>. Clearly, not inducing care is more profitable for the principal. The agent also *169 has no incentive to take care since, without any assets, he will never have to pay for the third-party harm. In equilibrium, therefore, the principal pays the agent zero in all states and the agent never takes care.

Now, suppose that the court makes principal liable for the third-party harm but that both the principal and the court can observe the agent's care choice, i.e. the agent's care choice is observable and contractible. If the principal does not want to induce care from the agent ($e = 0$), she will simply pay him zero in all states and realize an expected profit of $R - p_0L$. If she wants to induce care from the agent ($e = 1$), she will promise to pay the agent t^* if the agent takes care and zero otherwise, such that <<EQUATION>>. The agent will take care and, because the court also observes this, too, the principal is never liable. The principal's expected profit, in this case, is $R - t^*$. We will assume that <<EQUATION>>, so that if the agent's care choice is contractible, the principal will always induce care from the agent and achieve the first best.

2.2. An error-free court

Let us go back to the original assumption that the agent's care choice is not observable to (and contractible for) the principal. If the court can ascertain the agent's true behavior ex-post with perfect accuracy, we will have $q_0 = 1$ and $q_1 = 0$. This may be feasible if the court, based on the evidence presented by the parties in litigation, can perfectly and costlessly infer the level of care chosen by the agent at $t = 2$.[17] The principal, in designing the employment contract (K) at $t = 1$, has two choices: she can either induce care from the agent and never be liable for damages, or induce no care from the agent and always be liable for damages. As the following proposition demonstrates, making the principal vicariously liable is better than holding only the agent liable, but if the agent is risk-averse, the principal may have to bear additional cost. The reason is that, even when the court does not make any error, the principal may need to compensate the agent for bearing the risk generated by uncertain accident.

Proposition 1. *When the court never makes any error ($q_0 = 1$ and $q_1 = 0$), holding the principal vicariously liable dominates imposing liability only on the agent. If the agent is risk-neutral, the principal will induce the agent to take care only when it minimizes the expected social cost. As the agent becomes more risk-averse, inducing care from the agent becomes more expensive for the principal.*

If the principal does not want to induce care from the agent, the principal's profit from hiring the agent has three components: (1) the gross revenue, R, (2) the expected loss of p_0L from the accident and subsequent adverse judgment, and (3) the agent's expected salary, <<EQUATION>>. The second component of the contract, <<character cannot be displayed>>, is not relevant since, in equilibrium, the agent does not take care and the court does not relieve the principal from liability. The cheapest way to induce no care from the agent is by giving him an expected salary such that he is just willing to accept the contract instead of going for his next-best alternative. Because we have normalized the cost of exerting no care to zero and and the agent's outside option to $u(0)$, at optimum, <<EQUATION>> and the principal realizes an expected profit of $R - p_0L$.

If the principal attempts to induce the agent to take care, on the other hand, since the agent will not be declared negligent in equilibrium, the principal's expected profit consists only of (1) the gross revenue R and (2) the expected salary paid to the agent, <<EQUATION>>. The third component of the contract, <<character cannot be displayed>>, is not relevant since the court, in equilibrium, declares the agent not negligent. When the court does not make any error, because the court's judgment is more informative of the agent's care choice than the accident, the principal will compensate the agent more when he is declared not negligent than when there is no accident: <<EQUATION>>. When the agent is risk-neutral, the principal needs to compensate the agent only when he is declared not negligent <<EQUATION>>, since that is the only state in which the principal knows for

sure that the agent has taken care. As the agent becomes more risk-averse, however, the principal will need to compensate the agent for bearing the risk that comes from the uncertain accident: << EQUATION>>. The principal's private cost of inducing care rises as the agent becomes more risk-averse.

2.3. Introducing judicial error

The assumption that the court can infer the agent's past behavior with perfect accuracy is unrealistic. It is difficult to argue that the evidence presented by the interested parties can always reveal the truth to the court or that the court has more information about the agent's behavior and the nature of the moral hazard problem than the principal. On the other hand, given that the litigation often discovers relevant, extrinsic evidence (particularly from the harmed third party), the court's judgment will often correlate with the truth. To reflect this, we assume that <<EQUATION>>. With the possibility of court error, the principal's expected profit from hiring the agent is composed of the gross revenue, R, minus potential damages L, which occur with probability p_e q_e, and minus the agent's expected salary, <<EQUATION>>

Proposition 2. *When the court makes both pro-plaintiff (type I) and pro-defendant (type II) errors (<<EQUATION>>), holding the principal vicariously liable still dominates imposing liability only on the agent. Compared to the case where the court makes no error, however, the principal is less likely to induce care from the agent because the agent receives a bigger rent in equilibrium and, if the agent is risk-averse, the principal has to pay a larger risk premium.*

If the principal does not want to induce care from the agent, the optimal employment contract entails setting all three payments equal to zero: << EQUATION>>. If the principal wants to induce care from the agent, however, the principal will have to set either <<character cannot be displayed>> > 0 and/or <<character cannot be displayed>> > 0, depending on how informative the court's judgment is. If the court's judgment is very accurate <<EQUATION>>, the optimal contract will resemble the one in the case with no court error, i.e. << character cannot be displayed>> > 0, whereas if the court's judgment is not very reliable <<EQUATION>>, the principal will set <<character cannot be displayed>> > 0.[18] Compared to the case when the court's judgment is perfectly accurate, however, it is more expensive for the principal to induce care from the agent. This additional cost stems from two different sources. First, because the court's judgment is less informative, the principal needs to provide a larger incentive (higher <<character cannot be displayed>> and/or << character cannot be displayed>>) to the agent to induce care, and this translates to more rent being captured by the agent. Second, the agent now faces two types of risk: one with respect to the uncertain accident and the other with respect to the uncertain judgment. If the agent is *170 risk-averse, the principal will need to compensate the agent more for bearing these risks.

2.4. Implications

When the court can make both pro-plaintiff (type I) and pro-defendant (type II) errors, the principal becomes less likely to induce the agent to take care because (1) the principal has to leave more rent to the agent due to the agent's being judgment-proof, and (2) if the agent is risk-averse, the principal has to compensate the agent for additional risk-bearing. If we can reduce both types of errors, i.e. make $q_1 \dashrightarrow 0$ and $q_0 \dashrightarrow 1$, socially efficient care will be implemented more often by the principal in equilibrium. If reducing both types of errors is not feasible, should the court focus more on mitigating the pro-plaintiff (type I) error or the pro-defendant (type II) error? In other words, should the court try to decrease q_1 or increase q_0? The following corollary shows that attempting to eliminate the pro-defendant (type II) error is better.

Corollary 1. *When the court makes both pro-plaintiff (type I) and pro-defendant (type II) errors* (<<EQUATION>>), *a marginal increase in q_0 (reducing the pro-defendant, type II error) lowers the social cost (weakly) more than a marginal decrease in q_1 (reducing the pro-plaintiff, type I error).*

If the principal is already inducing care from the agent ($\#_1 > \#_0$), a marginal increase in q_0 or a marginal decrease in q_1 will not have any efficiency ramifications. If the principal is not inducing care, i.e. $\#>>_1 < \#_0$, the question becomes whether increasing q_0 or decreasing q_1 is more likely to restore proper incentives for the principal. There are two reasons that reducing the pro-defendant (type II) error is better than reducing the pro-plaintiff (type I) error. First, a marginal increase in q_0 increases the principal's expected liability in case of no care by p_0L. Similarly, a marginal decrease in q_1 decreases the principal's expected liability in case of care by p_1L. While both reduce the gap between the profits, $\#_0 - \#_1$, because the accident is more likely to happen when the principal does not induce care than when she does ($p_0 > p_1$), a marginal increase in q_0 closes the gap faster than a marginal increase in q_1 does.

Second, conditional on accident, when the agent does not take care, a marginal increase in go will make him more likely to realize $u(0)$ instead of u (<<character cannot be displayed>>). Similarly, conditional on accident, when the agent does take care, a marginal decrease in q_1 will make him more likely to receive u(<<character cannot be displayed>>) instead of $u(0)$. Comparing the two, the magnitudes (not the directions) of the effect these changes have on the agent's utility, conditional on accident, are the same: <<EQUATION>>. However, because accident is more likely when the agent does not take care than when he does ($p_0 > p_1$), the decrease in the agent's expected utility due to an increase in q_0 from not taking care is bigger than the increase in the agent's expected utility due to a decrease in q_1 from taking care: << EQUATION>>. In other words, a marginal increase in q_0 punishes the agent more for not taking care than a marginal decrease in q_1 rewards the agent for taking care. Hence, compared to a decrease in q_1, an increase in q_0 will make it easier for the principal to provide care incentive to the agent.

Finally, the second effect, reduction in compensation, is stronger when the court's judgment is more accurate. When the court's judgment is not informative of the agent's behavior, i.e. $q_0 \# q_1$, the principal is unlikely to condition the payment on the court's judgment, i.e. <<EQUATION>>, so that a marginal increase in q_0 or a marginal increase in q_1 will not affect the expected compensation. Only when the court's judgment is sufficiently accurate ($q_0 > q_1$), will the principal condition the payment on the court's judgment, i.e. <<EQUATION>> and <<EQUATION>>, and can the principal reduce the agent's compensation from a marginal improvement in the accuracy of the court's judgment (increase in q_0 or decrease in q_1). In other words, when the court's judgment is uninformative, the principal does not use that information and a marginal improvement in that information does not affect the principal's cost. When the court's judgment is accurate enough for the principal to rely on it, a further improvement in that accuracy allows the principal to reduce the agent's compensation.

Our model also has a normative implication for employment law. Unless a small number of public policy exceptions are triggered, courts allow an employer to discharge an at-will employee for causing a third party harm or for misconduct. For definite term employees with implicit "just cause" protection, the courts are split on whether an employer can fire an employee without a subsequent judicial determination that the employee indeed misbehaved or was negligent. [19] The model implies that, without any restrictions on contract, the principal will often sanction (e.g. fire) the employee for causing an accident regardless of subsequent judicial determination of agent's negligence: << EQUATION>>. [20] The question we focus on is whether the courts should declare that the employee has been wrongfully discharged (or reprimanded) when a court finds him not negligent. To analyze this, we impose a constraint, << character cannot be displayed>> = <<character cannot be displayed>>, on the principal's problem. The following corollary shows that imposing this restriction will reduce social welfare by making the principal less likely to induce care from the agent.

Corollary 2. *When the principal is prohibited from sanctioning (e.g. firing) the agent when the court declares the agent not negligent (<<character cannot be displayed>> = <<character cannot be displayed>>), the principal is less likely to induce socially beneficial care from the agent.*

Without any restrictions on contract, when the court's determination of negligence is not very informative, e.g. when $q_0 - q_1$ is small, the principal would want to sanction (e.g. discharge) the agent whether or not the court declares the agent negligent. Only when the court's determination is very informative, e.g. when $q_0 - q_1$ is large, would the principal wait for the court's

confirmation before sanctioning the agent. The additional constraint, therefore, makes inducing care from the agent more costly from the principal's perspective, and this cost makes the gap between social and private costs of care larger, making it less likely that the principal will induce care. The analysis supports the view that, unless otherwise specified in the contract, causing a third party harm or a reasonable allegation of misconduct should be enough to satisfy *171 the just cause requirement Allowing an employer to discharge an employee for a third party harm or a bona fide allegation of misconduct would enable the employer to reduce the contracting cost and better control the moral hazard problem.

2.5. The assumption of judgment-proofness

We have assumed that the agent has no personal assets to pay for the third party harm, so that when the agent alone is liable, he will have no incentive to take care. What is important for our analysis is not the zero asset assumption but whether the agent has enough assets to pay for the damages. If the agent has a sufficient amount of wealth to pay for the damages and there is no restriction on the principal's imposing a negative wage on the agent, whether or not we hold the principal vicariously liable will have little effect on deterrence. [21] Even if the principal is vicariously liable for the agent's negligence, she will pass this cost onto the agent through a (large) negative wage (<<character cannot be displayed>> < 0), so that the agent ultimately becomes responsible for the damages. [22] If the agent is risk-averse, however, holding the principal vicariously liable may be better because she may be better at reducing the size of the risk born by the agent (through wage adjustment) than the court. [23]

If the agent has positive but limited amount of wealth or no wealth to pay for the damages or the negative wage, this limits the size of punishment the principal or the court can impose on the agent. However, as we have shown in the paper with the assumption of no wealth, holding the principal vicariously liable will be better than making only the agent liable. [24] The primary reason has to do with how the principal can use the additional information generated from the court's judgment. When the court imposes liability only on the agent, there are only two types of wealth transfers that the agent must experience: zero or the damages (L) imposed by the court. On the other hand, because the principal can make three different wage payments, (<<character cannot be displayed>>, <<character cannot be displayed>>, <<character cannot be displayed>>), the principal can better harness the information generated by the court, and impose a more efficient care incentive. Furthermore, as in the case with unlimited wealth, when the agent is risk-averse, the principal may be better at reducing the risk born by the agent than the court.

3. Concluding remarks

When a court imposes liability on a principal for a harm caused by her judgment-proof agent, the principal is likely to adopt an incentive system to encourage the agent to take more care. We show that when the court makes an error in determining the agent's negligence, the principal becomes less likely to induce care from the agent. While eliminating both types of error would be beneficial, reducing the pro-defendant (type II) error would have a more beneficial impact than reducing the pro-plaintiff (type I) error. We also show that the principal often sanctions (e.g. fires) the agent after the accident regardless of subsequent court determination of negligence. If we prohibit the principal from unconditionally sanctioning the agent, this will generally increase the agency cost and make the principal less likely to induce care from the agent. We argue that this supports the view that an employer should be able to discharge an employee based on a reasonable allegation of misconduct or for causing an accident without violating the (explicit or implicit) agreement that the employee can only be discharged for "just cause."

Our focus has been on the agent's conduct. We have assumed that once the agent has been found negligent by a court, the principal becomes automatically (or strictly) liable. In reality, employers sometimes argue that, despite the employee's negligence, liability should not be imposed on them because they have taken all necessary precautions, such as providing proper training to the employees and actively monitoring their conduct. This is an interesting issue that has not been fully addressed in the law and economics literature. Because the principal, in the model, does not take any "action" except for offering a contract to the agent, our model cannot address this issue. The principal's liability based on the *principal's* negligence suggests the possibility of some active behavior or omission, such as monitoring or training, by the principal. Because we must consider

both the agent's and principal's actions (and also how these two interact), this will complicate the analysis. We intend to address this issue in our future research.

Proof of Proposition 1. If the principal does not want to induce care ($e = 0$) from the agent, she wants to

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subject to:

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Here the principal will choose the lowest possible values for <<character cannot be displayed>> and <<character cannot be displayed>>. which are bounded below by the limited liability constraints (LL1s). Therefore, at optimum << EQUATION>>. and from (IC1) we obtain <<EQUATION>>. The principal's expected profit, at optimum, is

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When the principal chooses to induce care from the agent ($e = 1$), her objective is to

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subject to:

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We first note that the agent's participation constraint (PC2) is implied by the incentive compatibility (IC2) and the limited liability constraints (LL2s) and, therefore, PC2 is not binding. The Lagrangian is

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*172 where (μ, #, #, #) are the multipliers for IC2 and LL2s. The first order conditions, with respect to (<<character cannot be displayed>>, << character cannot be displayed>>, <<character cannot be displayed>>) are

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From the first equation, since $\mu > 0$ and <<EQUATION>>, we must have << EQUATION>>.

Next, we must have <<EQUATION>> at optimum. Suppose not. If <<EQUATION>>, the first order conditions imply that <<EQUATION>> and <<EQUATION>>. However, since <<EQUATION>>, this implies that <<EQUATION>>, which is a contradiction. Assuming <<EQUATION>> also leads to the same contradiction. Finally, since << character cannot be displayed>> = 0, we cannot have <<EQUATION>>. If, on the other hand, <<EQUATION>>, this again leads to the contradiction since << EQUATION>>. Therefore, at optimum, <<EQUATION>> and <<character cannot be displayed>> = 0.

Let us compare this to the case when the agent's care choice is contractible. Since <<EQUATION>>. Therefore,

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Proof of Proposition 2. The principal's program when she chooses not to induce care from the agent ($e = 0$) is

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subject to:

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Just like in the case of no court error, the principal will choose the lowest possible values for <<character cannot be displayed>>, <<character cannot be displayed>>, and <<character cannot be displayed>>, which are bounded below by the limited liability constraints (LL3s). Therefore, at optimum <<EQUATION>>. The principal's expected profit at optimum is

TABULAR OR GRAPHIC MATERIAL SET FORTH AT THIS POINT IS NOT DISPLAYABLE
If the principal chooses to induce care from the agent ($e = 1$), her program is to

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subject to:

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TABULAR OR GRAPHIC MATERIAL SET FORTH AT THIS POINT IS NOT DISPLAYABLE
Note that PC4 is implied by LL4s and IC4, so that PC4 is not binding. The Lagrangian is

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where (μ, #, #, #) are multipliers for IC4 and LL4s. The first-order conditions with respect to <<character cannot be displayed>>, <<character cannot be displayed>>, and <<character cannot be displayed>> are

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Note that, in equilibrium, we must have $\mu > 0$, since otherwise <<EQUATION>>. Now, since <<EQUATION>>, and <<EQUATION>>, we must have <<EQUATION>>, or << character cannot be displayed>> = 0.

We must analyze two separate possibilities. First, if <<EQUATION>>, we will have <<EQUATION>>. We can have <<character cannot be displayed>> = 0, particularly if <<EQUATION>>, which is possible when <<EQUATION>>. In other words, when the court's judgment is a poor indicator of the agent's behavior, the principal has less of a reason to compensate the agent when the court declares the agent not negligent after an accident The principal receives little additional information from the court's judgment and there is less of a reason to differentiate the agent's compensation based on this uninformative signal.

On the contrary, if <<EQUATION>>, we will have <<EQUATION>>. In this case, we can also have <<character cannot be displayed>> = 0, provided that <<EQUATION>>and that the agent has a sufficiently low degree of risk aversion. The condition that <<EQUATION>> guarantees that the court's judgment is accurate enough so that the principal may want to reward the

agent only if the agent is declared not negligent after an accident. The condition that the agent have a low degree of risk aversion ensures that the risk premium for receiving a reward in a single state of the world is not too large.

Let us we compare this equilibrium to the case when the agent's choice of care is contractible. Since <<EQUATION>>. Therefore.

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The principal only induces the agent to take care if <<EQUATION>>. Equivalently, the principal only induces care if the risk premium, << EQUATION>>, is not greater than <<EQUATION>>.

Now we can show that the agent's risk premium is larger when there's court error. When the court makes error, at optimum, from IC4 we have <<EQUATION>>. Consider an improvement in the court's accuracy that stems from either a marginal increase in q_0, or a marginal decrease in q_1. Conditional on optimal (<<character cannot be displayed>>, <<character cannot be displayed>>), increasing q_0 by dq_0 lowers the right hand side of the IC4 by <<EQUATION>>but leaves the right hand side the same. This, in turn, allows the principal to decrease the agent's compensation across the board, thus reducing the agent's risk premium. Similarly, decreasing q_1 by dq_1 keeps the right hand side the same but raises the left hand side by <<EQUATION>>, which, again, allows the principal to reduce the expected wage. Hence, conditional on inducing care, the agent's risk premium is lower when the court's judgment is more accurate. Therefore, as the court's ***173** judgment becomes more accurate, (q_0, q_1) --> (1,0), conditional on inducing care, the principal's expected return rises (while the agent's expected rent falls), and the principal becomes more likely to induce care from the agent.

Proof of Corollary 1. If $\#_0 > \#_1$, since the principal is already inducing the agent to take care, either increasing q_0 or decreasing q_1 will not have any effect on social welfare. So, let's assume that << EQUATION>>. First, because, at optimum. <<EQUATION>>, we have

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From the envelope theorem, we know that, at optimum, <<EQUATION>>, and << EQUATION>>, where #(.) is the Lagrangian from the proof of Proposition 2 with the optimal (<<character cannot be displayed>>, <<character cannot be displayed>>, <<character cannot be displayed>>). In other words.

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Combining the two, we get

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Since <<EQUATION>>: a marginal increase in q_0 will decrease the gap between $\#_0$ and $\#_1$ faster than a marginal decrease in q_1. Hence, reducing the pro-defendant (type II) error lowers the social cost more than reducing the pro-plaintiff (type I) error.

Proof of Corollary 2. When the court does not make any error, Proposition 1 demonstrates that no matter whether the principal induces the agent to take care or not, at optimum, we will have <<EQUATION>>. Hence, the imposition of the just-cause restriction will not affect the optimal compensation structure.

Suppose that the court makes type I and type II errors. From Proposition 2, if the principal does not want to induce care from the agent, the optimal contract is <<EQUATION>>, so that the just-cause restriction (<<EQUATION>>) is again satisfied. In this case the principal's expected profit is <<EQUATION>>

Now when the principal wants to induce care from the agent, the restriction is binding only if the unrestricted equilibrium is such that <<EQUATION>>, which is equivalent to <<EQUATION>> from the first order conditions. In the unrestricted equilibrium, we know that IC4 binds and the principal's expected profit is <<EQUATION>>. Imposing the just-cause constraint implies that << character cannot be displayed>> must increase and/or <<character cannot be displayed>> must decrease so that <<EQUATION>>.

Starting from the unrestricted equilibrium, consider a marginal increase in << character cannot be displayed>> and a corresponding change in <<character cannot be displayed>> so as to keep providing just enough incentive for the agent to take care. The impact of this change on the principal's profit is: << EQUATION>>. From the binding IC4, the total differentiation leads to << EQUATION>>. This implies that <<EQUATION>>. That is, profits from inducing care decrease as as <<character cannot be displayed>> and <<character cannot be displayed>> get closer to each other (or as the just-cause restriction is imposed), and, therefore, the principal will be less likely to induce care from the agent with the restriction.

More intuitively, when the restriction is binding, the principal has to pay the agent the same salary either if he was not negligent for an accident or if an accident did not occur. Conditional on inducing care, this occurs with probability $1 - p_1 q_1$. Therefore, the likelihood ratio used by the principal when she faces the restriction is equal to <<EQUATION>>. Note that << EQUATION>>: the likelihood ratio used in the program with the restriction is simply a weighted average of the likelihood ratios used in the program without the restriction. Since (1) the weighted average will always be between the two likelihood ratios and (2) in the unrestricted program, the principal always chooses the state with the higher likelihood ratio to compensate the agent, the principal's expected compensation is higher with the restriction than without. Therefore, the principal is more likely to induce care from the agent without the restriction.

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Footnotes

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1 For comprehensive analyses of the doctrine of vicarious liability, see Kornhauser (1982) and Sykes (1984, 1988, 1998). Both scholars emphasize the agent's inability to pay damages as a basis for imposing liability on the principal. See also Shavell (2004. pp. 232-236). For a more general treatment of the "judgment-proof" problem and how minimum asset requirement or compulsory liability insurance could be used, see Shavell (1986, 2005). To be precise, both the agent and the principal are jointly and severally liable for the harm, a principle that is ignored in some literature. In our model, since the principal already imposes the maximum monetary sanction against the agent, unless the court can impose a non-monetary criminal sanction on the agent, as in Polinsky and Shavell (1993), the fact that the liability is joint and several does not play a big role.

2 There is a sizable literature that analyzes the implication of vicarious liability on the principal's contracting problem. See Newman and Wright (1990, 1992), Arlen (1994), Chu and Qian (1995), Dominique and Fluet (1999), Mattiacci and Parisi (2003), Hiriart and Martimort (2006) and Arlen and MacLeod (2005). Our work differs in that we examine (1) how the court's propensity to make an error in negligence determination affects the optimal contract and the incentive to induce care and (2) whether the law should prohibit the principal from penalizing the agent when the agent is declared not negligent.

3 See Laffont and Martimort (2002, pp. 167-172) for how the presence of an additional, informative signal can allow the principal to improve contracting and reduce the agency cost. See also Bolton and Dewatripont (2005, pp. 136-137). The problem we are analyzing is also closely related to the monitoring intensity principle. According to that principle, when the principal uses a high-powered incentive on a risk-averse agent, it becomes more worthwhile for the principal to improve the accuracy of the information (signal) that the incentive structure relies on. See Milgrom and Roberts (1992, p. 226). In our model, the ex-post monitoring is done by the court and only when there is an accident. The model analyzes how the improvement in the court's judgment (reducing pro-plaintiff and pro-defendant errors) affects the incentive system the principal uses to control the agent's behavior. This is the flip-side of the problem analyzed by the monitoring intensity principle.

4 Leaving rent to the agent when the agent is judgment-proof and the signal that the principal relies on is not entirely accurate has a close resemblance to the efficiency wage literature. See, e.g. Becker and Stigler (1974), Dickens, Katz, Lang and Summers (1989), Eaton and White (1982), and Shavell (1997). We would like to thank an anonymous referee for directing us to this literature.

5 Another easy way to think about this is to imagine the following scenario. Suppose that if the principal induces care from the agent, accident never happens, but if the principal does not, accident happens with a positive probability. When the principal induces care from the agent, reducing pro-plaintiff error will have no impact on the principal's expected liability because adjudication never

happens anyway. On the other hand, if the principal does not induce care from the agent, reducing the pro-defendant error will increase the principal's expected liability because there is a positive probability of adjudication.

6 Mullin and Snyder (2005) also consider an authority that can make type I and type II errors. Their model differs from ours in that the principal has an incentive to induce the agent to commit a crime, and they examine whether the law should allow the principal to indemnify the agent. Ayotte and Robinson (2006) examine the relative importance of type I and type II errors, but in a different setting. In their model, the detrimental impact of type II error can be eliminated through contract.

7 For at-will employees, there is only a small number of public policy exceptions that would support their wrongful discharge claim. See Schwab (1995-1996). See also *Loughridge v. Overnite Transportation Company*, 649 F.Supp. 52 (1986) and *Pantoja v. Holland Motor Express, Inc.*, 965 F.2d 323 (7th Cir. 1992) for cases where employers discharge at-will employees for causing an accident. For definite term employees without an explicit "for cause" termination provision in their contract, the courts are split. The California Supreme Court's decision in *Cotran v. Rollins*, 17 Cal. 4th 93 (1998), supports the view that the employer should be able to discharge an employee so long as there was a reasonable basis for the allegation. The Michigan Supreme Court's decision in *Toussaint v. Blue Cross & Blue Shield of Michigan*, 408 Mich. 579 (1980), on the other hand, supports the view that an employer's good faith belief of employee's wrong-doing is not sufficient; the employee should be found guilty before she can be discharged. See also *Chiodo v. General Waterworks Corp.*, 413 P.2d 891 (1966), where Utah Supreme Court ruled that allegations of payroll padding, insubordination, and disloyalty were not sufficient to discharge a definite term employee. See generally Rothstein, Craver, Schroder and Shoben (1999, pp. 696-698). The South Dakota legislature has enacted a statute that allows an employer to discharge a definite term employee for "habitual neglect of duty or continued incapacity to perform or any willful breach of duty." S.D. Codified Laws Ann. Section 60-4-5.

8 Our analysis presumes the existence of an "agency" relationship for the purposes of imposing vicarious liability; it does not ask the question of when should such a relationship exist, e.g. when should a corporate veil be pierced or when should an "independent contractor" become an agent. The courts, in such situations, often examine the existence of control. We would suspect that one contracting party being able to use an incentive contract for the other, as in our example, would often lead the courts to conclude the existence of control. If so, the "principal" will be less inclined to impose incentive contract on the "agent," and the problems with judgment-proofness can be worsened. See, e.g. Easterbrook and Fischel (1985). This is an issue that we would like to explore further in our future research. We would also like to thank an anonymous referee for this suggestion.

9 What is more important is the assumption of non-contractibility than that of non-observability. If the principal can observe the agent's behavior but that cannot be contracted upon, unless there are other ways of solving the moral hazard problem (e.g. through repeat relationship), observability does not matter. If, on the other hand, the agent's choice is observable and can be verified at a cost, unless the verification cost is very high, the principal may contract upon the court's (error-prone) judgment as to the agent's behavior. See, e.g. Choi and Triantis (2007). Now, the principal may need to deal with two possible courts, one that will adjudicate the claim of tort liability and the other that will adjudicate the claim of (wage) contract liability. As the first court becomes more error-prone, the principal will be more likely to contract on the agent's behavior and rely on the second court. This is a very interesting issue that we would like to explore future in the future. We would also like to thank an anonymous referee for pointing this out.

10 If we assume that the principal can collect all verifiable information (including from the third party) about the agent's behavior before proceeding to litigation, then the court's judgment will only introduce noise to the principal's problem. There may be at least a few reasons why this may not be feasible. First, the court may be better at collecting additional verifiable information after an accident. Especially with respect to the information that the third party has, because the third party is biased (toward imposing liability), the court, with its power to impose sanctions against perjury and with strict procedures on evidence presentation at trial, may be better at teasing out the unbiased portion of the evidence. Second, because the principal may be biased ex-post (she would rather pay the agent less than more), the agent may be concerned about the principal's opportunism unless such ex-post information collection procedure is contractible ex ante. We would like to thank an anonymous referee for suggesting these two possible explanations.

11 This assumption implies that the incentive structure used by the principal to control the agent's behavior does not affect the total revenue (R) from the venture. This assumption can most easily be justified if the principal is operating in a competitive product/output market where she has little or no market power. Alternatively, if we assume that the third-party is not the consumer and reducing the liability does not affect the marginal cost of production (i.e. it only affects the fixed cost), then again the price the principal will charge at the product/output market will be independent of her liability strategy.

12 We assume that the parties do not settle. Settlement poses a potential danger to the principal's contracting solution, since, if they always settle, the principal will not be able to use the court's judgment. In the model, the principal knows the care level induced by her while the third party does not: the principal knows which q she will face at trial but the third party can only make an educated guess about it. The parties are asymmetrically informed of the true state of nature and this will, in certain cases, prevent settlement, allowing the principal to (sometimes) obtain the court's judgment. We would like to thank an anonymous referee for this suggestion.

13 Whether the court holds only the principal liable or hold both the principal and the agent jointly and/or severally liable does not make any difference. The reason is that when the court declares the agent negligent, the principal does not compensate the agent and the agent has no assets to pay for the harm.

14 The court, in theory, can also hold the principal strictly liable for accident, i.e. impose liability regardless of the agent's negligence. It is fairly easy to show that, in the model, the strict liability standard will perform (weakly) worse than the negligence standard. The comparison is the easiest when the agent is risk-neutral and the court makes no error. As we will show, with the negligence standard, the first best will be achieved. If the court were to hold the principal strictly liable, however, because the principal can no longer rely on the court's accurate judgment, the agent captures more rent and the principal becomes less likely to induce care in equilibrium.

15 If the third party has to bear litigation cost (c), so long as the stake of the litigation is large enough, i.e. <<EQUATION>>, the third party sue the principal after the accident. For the principal, litigation cost provides an additional incentive to avoid the accident: <<character cannot be displayed>> is more likely to be positive. However, she still faces a trade-off of rewarding the agent in the case of no accident (<<character cannot be displayed>> > 0) versus rewarding the agent in the case of judicial determination of no negligence (<<character cannot be displayed>> > 0). The rest of the analysis, therefore, is not affected.

16 If we are concerned about the victim's level of precaution, we can adopt some type of contributory or comparative negligence standard.

17 Alternatively, if the court can observe the principal's maximization problem, the court may be able to figure out the level of care induced by the principal through the incentive contract. This was the assumption made in Dominique and Fluet (1999), which allowed them to demonstrate that the negligence-based regime is better than the strict liability-based regime.

18 In technical language, the relative compensation depends on the relative likelihood ratios. The likelihood ratios of no accident and accident but no negligence are given by <<EQUATION>> and <<EQUATION>>, respectively. When the first is higher, <<character cannot be displayed>> > <<character cannot be displayed>>, and when the second is higher, <<character cannot be displayed>> > <<character cannot be displayed>>. While the likelihood ratio associated with the no accident state is determined entirely by p's, the other depends also on court error, q's. As $q_0 - q_1$ gets larger, so does the second likelihood ratio.

19 The public policy exceptions for at-will employees include refusal to perform an unlawful act, reporting employer's illegal activity, exercising the employee's right, and performing a legal duty. See Rothstein (1999, pp. 698-709). There are three ways that a definite term contract can include a "just cause" requirement for termination. First, by law, an employment contract for a definite term may not be terminated without cause before the expiration of the term, unless the contract provides otherwise. Second, the written contract can provide explicit just cause protection. Third, courts may find just cause protection to be implied from an oral agreement, employee handbook, or course of conduct. See Rothstein (1999, pp. 696-698). For definite term employees, employers are also free to contract around the implicit "just cause" protection, for instance, by stipulating that the employee will be fired for causing an accident regardless of the subsequent court judgment. The policy proposal we are advancing in the paper, therefore, has to do with whether, as a default rule, an employer should be allowed to punish an employee for causing an accident.

20 In our model, the principal does not necessarily have to fire the agent. She can reprimand the agent, through a salary cut or demotion, to provide care incentive. Most just cause cases deal with the claims of unjust termination, and the case law on other types of, less drastic, sanctioning is quite thin. This is probably due to the fact that most employees, when they receive an allegedly unjust reprimand on the job, will quit their job and bring litigation based on constructive discharge. The case in California, however, suggests that the just cause termination doctrine can be applicable to other types of sanctioning. The California Supreme Court, in *Scott v. Pacific Gas & Electric Co.*, 904 P.2d 834 (Cal. 1995), held that an implied agreement not to demote except for good cause may be enforced by demoted employees. See Willborn, Schwab, and Burton (2002, p. 127).

21 This is consistent with Kornhauser (1982), Sykes (1984), and Arlen and MacLeod (2005), who find that when the agent is not judgment-proof, imposing liability only on the agent is equivalent to making the principal vicariously liable.

22 When the agent is neither risk-averse nor wealth-constrained, the agent will be responsible for all damages and the agent will always take socially beneficial care. As suggested in Milgrom and Roberts (1992, pp. 236-237), however, the assumption of the agent having sufficient amount of assets to pay for the damages maybe unreasonable in many circumstances.

23 This assumes that the agent has no independent source, such as a third-party insurance, through which he can reduce the risk he is bearing. If he does, different regimes of liability will have no welfare implication.

24 This is consistent with Arlen and MacLeod (2005). They conclude that entitylevel liability is superior to individual liability when physicians (agents) are judgment-proof. In their model, the principal can monitor the agent's actions and sanction the agent if she believes that the agent was negligent. This allows the principal to apply lower but more frequent sanctions on the agent with limited wealth, which is better than the regime where the court imposes (potentially large but less frequent) damages. Notwithstanding the improvement, because the agent may still have insufficient amount of wealth to pay for the sanctions, achieving the first best may not be feasible.

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IN THE MICHIGAN SUPREME COURT
APPEAL FROM THE COURT OF APPEALS

CITY OF HOLLAND,

Plaintiff – Appellee,

v

JENIFER L. FRENCH,

Defendant – Appellant.

Supreme Court No. 147492
COA No. 309367
Lower Ct No. 10-0011684-CZ
Ottawa Circuit Court

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Rhonda R. Fleming, being first duly sworn, deposes and says that I am employed by the law firm of Miller, Canfield, Paddock and Stone, PLC, and on September 5, 2013, I caused to be served a copy of:

Brief of Amici Curiae The Michigan Municipal League And The State Bar of Michigan Public Corporation Law Section In Support Of The Appellee City of Holland's Response on Appeal and Proof of Service

upon the following, via first class mail:

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Subscribed and sworn to before me
this 5th day of September, 2013.

Notary Public

PHYLLIS JEAN DAHL
NOTARY PUBLIC - STATE OF MICHIGAN
COUNTY OF INGHAM
My Commission Expires Sept. 20, 2013
Acting in the County of Ingham

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