

Discrimination in Hiring Based on Past Bankruptcy Filing Allowed for Private Employers

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Introduction

Section 525 of the Bankruptcy Code protects employees who currently are or have previously been in bankruptcy from discrimination.¹ It contains two subsections.² Subsection (a) states that *government* employers may not deny employment to, terminate the employment of, or discriminate with respect to employment against a person who has filed bankruptcy solely because of that filing.³ Subsection (b) provides that no *private* employer “may terminate the employment of, or discriminate with respect to employment against” individuals for declaring bankruptcy.⁴ The salient difference is that the section applying to private employers does not mention denial of employment in its list of prohibited discriminatory actions. The United States Supreme Court has never determined whether this discrepancy in language indicates that there should be different policies in place for the public and private sectors with respect to hiring practices. However, a number of courts, including the Third, Fifth, and Eleventh Circuits, have held that section 525 permits private employers are allowed to discriminate in hiring based on a prior bankruptcy.

¹ 11 U.S.C. § 525 (2006).

² *Id.*

³ 11 U.S.C. § 525(a).

⁴ 11 U.S.C. § 525(b).

In *Myers v. TooJay's Management Corp.*, the Court of Appeals for the Eleventh Circuit distinguished between public and private employers, and held that section 525(b) of the Bankruptcy Code does not prohibit a private employer from declining to hire a person because of a prior bankruptcy.⁵ The court applied a plain meaning interpretation of the statute and noted that the difference in the language of subsections (a) and (b) of section 525 intimates Congressional intent to differentiate between public and private protections.

Part I of this memorandum will discuss the ruling of the Eleventh Circuit in *Myers v. TooJay's Management Corp.* and its effect on those who have filed or intend to file bankruptcy petitions. It will also review the holdings of other circuit courts that have interpreted this statute. Part II will more specifically examine the rationale behind a New York case, *Leary v. Warnaco*,⁶ which came to a different conclusion from the circuit courts. Part III will then analyze the purpose of section 525 of the Bankruptcy Code with respect to both public and private employers. Finally, this memorandum will conclude by considering the interest of employees and the public as a whole in determining the impact this decision will have on the bankruptcy field.

I. Holding and Rationale of *Myers v. TooJay's Management Corp.*

In *Myers v. TooJay's Management Corp. (Myers)*, the Court of Appeals for the Eleventh Circuit affirmed the dismissal of a claim of discrimination against a private business, TooJay's, which had refused to hire a prospective employee, Myers, because of his prior bankruptcy filing.⁷ Eric Myers filed a chapter 7 bankruptcy petition in North Carolina in January 2008.⁸ A month later, he moved from North Carolina to central Florida and began working at a Starbucks

⁵ *Myers v. TooJay's Management Corp.*, 640 F.3d 1278 (11th Cir. 2011).

⁶ *Leary v. Warnaco, Inc.*, 251 B.R. 656 (S.D.N.Y. 2000).

⁷ *Myers*, 640 F.3d at 1283.

⁸ *Id.* at 1280.

coffeehouse.⁹ By May 2008, the bankruptcy court discharged Myers' debts and soon thereafter, Myers applied for a managerial position with TooJay's Gourmet Deli.¹⁰ At the end of his interview in July 2008, Myers scheduled a two-day on-the-job evaluation, during which he would be paid half the normal salary of a manager.¹¹ On the second day of Myers' on-the-job evaluation, he authorized a background check, which permitted TooJay's to review Myers' credit history and reports.¹² Although the regional manager of TooJay's did not officially offer Myers a job at the end of his two-day evaluation, he did schedule a start-date for Myers' employment.¹³ Myers gave his two weeks notice to Starbucks and eight days later, received a letter rescinding the previous offer of employment because of a "financial matter," presumably involving his previous bankruptcy filing.¹⁴

On September 2, 2008, Myers sued TooJay's alleging that TooJay's had violated section 525(b) of the Bankruptcy Code by refusing to hire him because after learning of his previously filed bankruptcy petition and, alternatively, by terminating him from the job after it had hired him because of his previous bankruptcy.¹⁵ The district court dismissed Myers's case, and the Eleventh Circuit affirmed.¹⁶ Both courts found that section 525(b) of the Bankruptcy Code does not prohibit a private employer from declining to hire a person based on a prior bankruptcy.¹⁷

Myers argued that section 525(b) should be interpreted to further the Bankruptcy Code's

⁹ *Id.*

¹⁰ *Id.*

¹¹ *Id.*

¹² *Id.* at 1281.

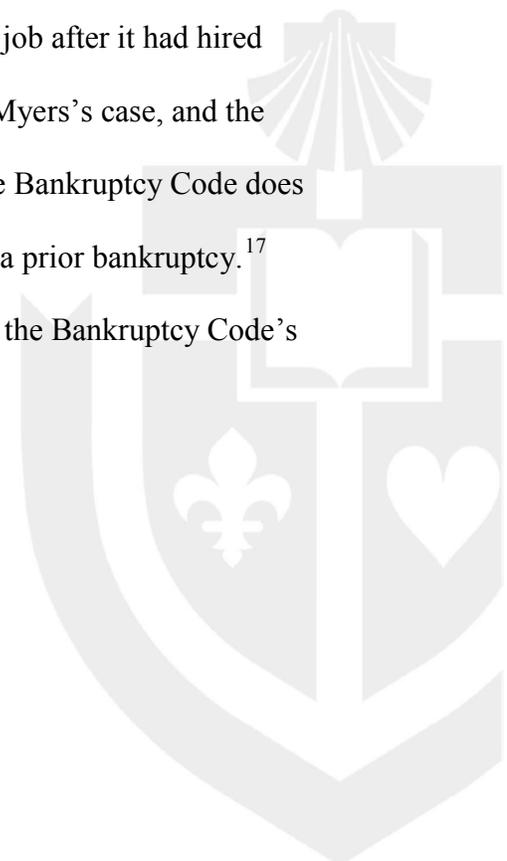
¹³ *Id.*

¹⁴ *Id.*

¹⁵ *Id.* at 1282.

¹⁶ *Id.* at 1283.

¹⁷ *Id.*



main purpose, which is to give debtors a fresh start.¹⁸ Although the Eleventh Circuit acknowledged that to be one of the broad purposes of the Code, it responded to Myers' arguments by stating that its job was to "interpret and apply statutes, not congressional purposes."¹⁹ The court stressed the importance of analyzing a statute based on its plain text, rather than looking at it with a skewed perspective, "attempting to see some hidden image formed by the broad purpose that lies behind the legislation."²⁰

In its interpretation of the statute, the Eleventh Circuit noted that section 525(a) explicitly referred to the denial of employment and found that Congress must have omitted it from section 525(b) "for a reason."²¹ The court inferred that if "Congress wanted to cover a private employer's hiring policies and practices in section 525(b), it could have done so the same way it covered a governmental unit's hiring policies and practices in section 525(a)."²² Furthermore, the court reasoned that it would be illogical to read the identical portions of each section, which state "or discriminate with respect to employment," to have different meanings.²³ Lastly, the court believed that if Congress intended to include the denial of employment in the portion of the statute using the language "discriminate with respect to employment," then the words "deny employment" in section 525(a) would be rendered meaningless and superfluous.²⁴

The Third Circuit and the Fifth Circuit have also had the occasion to address section 525 and have come to the same conclusion as the Eleventh Circuit. The Third Circuit dismissed a case of discrimination in hiring by a private employer in *Rea v. Federated Investors*, finding that

¹⁸ *Id.*

¹⁹ *Id.*

²⁰ *Id.* at 1286.

²¹ *Id.* at 1285.

²² *Id.*

²³ *Id.*

²⁴ *Id.* (referring to this action as "an interpretative no-no").

the exclusion of language specifying that discrimination in hiring based on a previous bankruptcy is prohibited in section 525(b), but inclusion of it in section 525(a), indicates that it should not be a protected action.²⁵ In his complaint, the debtor, Rea, argued that section 525(b) prohibits private employees from refusing to hire an individual who has filed for bankruptcy.²⁶ The defendant moved to dismiss the complaint, alleging that the debtor failed to assert a claim under section 525(b).²⁷ The District Court granted the motion, noting that language “should not be implied where excluded.”²⁸ Because Congress omitted language prohibiting a private employer from “deny[ing] employment to” a person because of a bankruptcy filing in a statute where that prohibition is present in the public sector context, the Third Circuit believed this act was intentional and refused to prohibit private employers from refusing to hire based on previous bankruptcies.²⁹

The Court of Appeals for the Fifth Circuit similarly rejected a claim for discrimination by a private employer in hiring in *In re Burnett*.³⁰ The court focused on the inclusion of language prohibiting discrimination of hiring in section 525(a) but exclusion of it in section 525(b) as indicative of Congressional intent to omit this type of discrimination from protections at law.³¹ The Fifth Circuit also stressed the importance of looking at the statute as a whole when interpreting a statute so as “not to render portions of it inconsistent or devoid of meaning.”³²

²⁵ Rea v. Federated Investors, 627 F.3d 937 (3d Cir. 2010).

²⁶ *Id.* Rea based her arguments on her reliance on *Leary v. Warnaco*, a New York case that is discussed later in this section. The Third Circuit found this reliance unpersuasive because *Leary* appears to be the only court holding that § 525(b) prohibits discrimination in hiring for private employers.

²⁷ *Id.*

²⁸ *Id.* at 939.

²⁹ *Id.* at 940.

³⁰ *In re Burnett v. Steward Title, Inc.*, 635 F.3d 169 (5th Cir. 2011).

³¹ *Id.*

³² *Id.* at 172.

Because allowing the phrase “discriminate with respect to employment” to include the act of hiring would render the phrase “deny employment to” superfluous, the court concluded that section 525(b) did not prohibit private employers from denying employment based on an individual’s bankruptcy status.³³

II. The case for interpreting section 525(b) to prohibit discrimination in hiring

In 2000, *Leary v. Warnaco*, a case from the Second Circuit, came to the opposite conclusion.³⁴ Marlene Leary filed a voluntary chapter 7 bankruptcy petition on December 17, 1998, and received her discharge on April 20, 1999.³⁵ On May 3, 1999, Leary interviewed with the defendant for an executive assistant position.³⁶ She had a second interview on June 23, 1999 and alleged that the company’s president of intimate apparel offered her the position, which was to begin on July 26, 1999.³⁷ On August 4, 1999, the defendant sent Leary a letter informing her it would not hire her because her credit report revealed a bankruptcy.³⁸ Leary sued Warnaco that September for violating “11 U.S.C. § 525(b)(1) and (3) by refusing to hire Plaintiff because of her bankruptcy status.”³⁹

The United States Bankruptcy Court for the Southern District of New York found that private employers were prohibited from discriminating in hiring based on bankruptcy, holding that discrimination in employment extended to all areas of employment, including hiring.⁴⁰ In its discussion, the court introduced section 525(b) as “one of the bankruptcy provisions Congress

³³ *Id.* at 173.

³⁴ *Leary v. Warnaco, Inc.*, 251 B.R. 656 (S.D.N.Y. 2000).

³⁵ *Id.* at 657. The Court noted that there was nothing unusual about this bankruptcy, which was referred to as a “plain vanilla case.”

³⁶ *Id.*

³⁷ *Id.*

³⁸ *Id.*

³⁹ *Id.*

⁴⁰ *Id.*

enacted to effectuate the ‘fresh start’ policy” behind personal bankruptcies.⁴¹ The district court expressed issue with allowing discrimination in hiring for private employers, finding it unsupported by the plain meaning of the statute, which prohibits an employer from discriminating “with respect to employment.”⁴²

The court specifically referred to section 525(b) as a remedial statute enacted by Congress to effectuate the “fresh start” policy behind many personal bankruptcies.⁴³ The court took issue with the narrow construction of this statute by other courts, stating that the plain meaning of the statutes does not support an inference of allowed discrimination in hiring for private employers.⁴⁴ It stated that the language of the statute was broad enough to extend to hiring someone for employment and further posited that this interpretation plausible since the “fresh start” policy would be impaired in both a firing and a refusal to hire based on a past bankruptcy.⁴⁵ The bankruptcy court also noted the importance of the plaintiff’s claim as one for “discrimination with respect to employment,” including all aspects of employment in this meaning, including hiring, firing, and material changes in job conditions.⁴⁶

III. Purpose of Section 525

Section 525 of the Bankruptcy Code was originally enacted in 1978 to ensure that debtors would actually receive a fresh start and be free from discrimination based solely on a bankruptcy filing.⁴⁷ In fact, the main purpose of bankruptcy law as a whole is to provide debtors with a

⁴¹ *Id.* at 658.

⁴² *Id.*

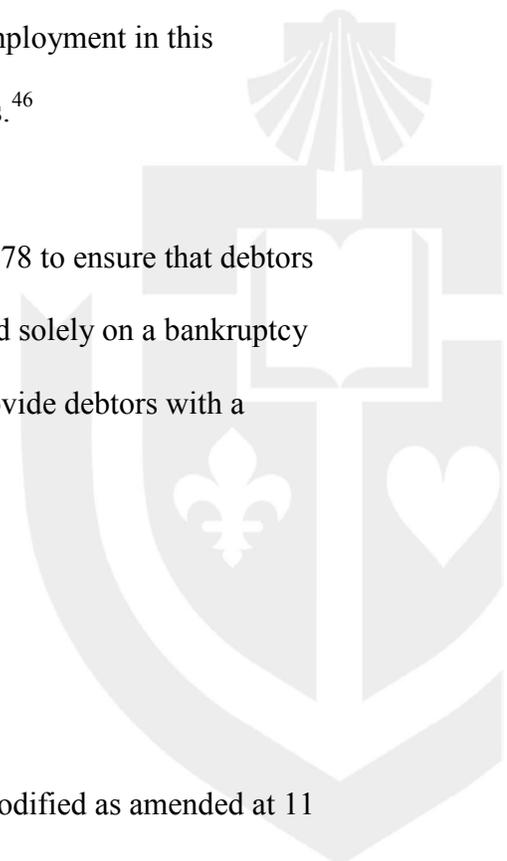
⁴³ *Id.*

⁴⁴ *Id.*

⁴⁵ *Id.*

⁴⁶ *Id.* at 659.

⁴⁷ Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (codified as amended at 11 U.S.C. §§ 101-1330).



“new opportunity in life and the clear field for future effort.”⁴⁸ Often times, there is a social stigma surrounding those who have used the bankruptcy system, mainly that they are unable to handle their finances and repay debts and thus are irresponsible, or even untrustworthy, people. When drafting section 525, Congress intended to “prevent an automatic reaction against an individual for availing himself of the protection of the bankruptcy laws.”⁴⁹ This section was meant to serve as protection for the debtor and codified the holding of *Perez v. Campbell*,⁵⁰ which held that “a State would frustrate the Congressional policy of a fresh start for a debtor” if it could refuse to renew a drivers license because of an unpaid tort judgment as a result of a discharge in bankruptcy.⁵¹

When it was first enacted in 1978, the Bankruptcy Code only prohibited “governmental units and quasi-governmental entities from discriminating against debtors in bankruptcy with respect to employment.”⁵² Yet, in 1984, after seeing several Bankruptcy Courts refuse to extend these protections to also disallow discrimination by private employers, Congress added a provision codified as 11 U.S.C. § 525(b) barring private employers from discriminating in employment solely because an individual had gone through a bankruptcy proceeding.⁵³ This addition indicates that Congress intended all protections for creditors to extend to the private sector.⁵⁴ This idea would have been in accordance with Congress’s intention in drafting section 525(a), which was partially to protect debtors from being denied the chance to earn a living

⁴⁸ *Local Loan Co. v. Hunt*, 292 U.S. 234, 245 (1934).

⁴⁹ H.R. REP. NO. 595, 95th Cong., 1st Sess. 165, *reprinted in* 1978 U.S. CODE CONG. & ADMIN. NEWS 5963, 6126.

⁵⁰ *Perez v. Campbell*, 402 U.S. 637 (1971).

⁵¹ 11 U.S.C. 525, notes.

⁵² John E. Theuman, *Protection of debtor from acts of discrimination by private entity under § 525(b) of Bankruptcy Code of 1978 (11 U.S.C.A § 525(b))*, 105 A.L.R. Fed. 555 (1991).

⁵³ *Id.*

⁵⁴ *Id.*

because of a preconceived notion that those who have filed for bankruptcy should not be dealt with.⁵⁵ In fact, many consider one of the most serious obstacles threatening the “fresh start” to be the “social stigma which commonly attaches to those who have sought the protections of bankruptcy.”⁵⁶ Since the Bankruptcy Code was drafted in 1978, there have been many questions regarding the application of section 525(b), including whether or not it should prohibit refusals to hire.⁵⁷

Traditionally, private employers do enjoy more liberties in employment decisions than public employers. However, there is little aside from the plain language of the statute to indicate that Congress intended for a strict reading of the plain language of section 525 and, thus, courts should consider the purpose behind the creation of the statute itself when applying restrictions on hiring decisions of both private and public employers.

Conclusion

The Third, Fifth, and Eleventh Circuits have allowed private employers to discriminate in hiring based on a bankruptcy filing, relying on a strict understanding of the plain language of section 525 of the Bankruptcy Code, and ignoring the Congressional intent behind the creation of this statute.⁵⁸ By weakening the protections available for individual debtors working in the private sector, the holdings of the Circuit Courts may affect the propensity of individuals to file for bankruptcy petitions. Because individuals working in the private sector would now need to be concerned with the impact a bankruptcy filing would have on future employment options, they may be deterred from filing for bankruptcy or delay filing until it is required or involuntary.

⁵⁵ *Id.*

⁵⁶ *Id.*

⁵⁷ *Id.*

⁵⁸ Myers, 640 F.3d at 1283.

In a sense, the recent *Myers* decision reaffirms protections for private employers, who can now engage in discrimination predicated on a previous bankruptcy filing without concern for any legal repercussions. Furthermore, the inconsistency between subsections (a) and (b) may be confusing for individuals who have expectations of certain protections against discrimination. Thus, this memorandum proposes, at least, a clarification by Congress or the Supreme Court of the United States as to the proper meaning of section 525(b), and, at most, an amendment to the statute that would properly protect all employees from discrimination predicated on a bankruptcy proceeding.

Although *Leary v. Warnaco* is still the only decision on this matter in the Second Circuit, it is unclear whether the Second Circuit will rule on the issue given the holdings in the Third, Fifth, and Eleventh Circuits. Furthermore, the question of how to best interpret section 525(b) has not been addressed by many of the circuit courts or district courts, and the Supreme Court of the United States has not expressed interest in granting certiorari on the issue. Yet, the general agreement by the three circuits that have addressed this matter possibly indicates that a different interpretation of section 525 would have to come in the form of legislation, rather than from a judicial decision.

The rulings of the Third, Fifth, and Eleventh Circuits conflict with the purpose of bankruptcy protections as a whole and are a setback for debtors with prospects of working in the private sector.⁵⁹ These rulings create uncertainty for debtors as to whether or not they will actually receive a fresh start from bankruptcy. Furthermore, they confuse the expectations of private employers in a jurisdiction that has not yet interpreted section 525(b) and perpetuates the social stigmas associated with a person who has filed for bankruptcy. In order to truly protect

⁵⁹ See Hunt, 292 U.S. at 245.

both debtors and employers in the private sector, these decisions should be re-evaluated or addressed by the Supreme Court of the United States. In the alternative, section 525(b) should be re-drafted or amended to better articulate its purpose, inclusions, and limitations.

