

Payback time: Employer wanted its money back—and got it!

Forgive us if we pat ourselves on the back. In two recent decisions, our firm, Bond, Schoeneck & King, was successful in recovering relief against employees. The cases offer good news for employers frustrated with losing money when they haven't done anything wrong.

In one landmark case, employees engaged in wrongdoing, but failed to profit from it because the New York Supreme Court applied a New York legal concept known as the "faithless servant doctrine." We'll discuss that case this month.

Next month, we'll address a case we won in which we successfully recovered relief against employees who brought suit against an employer but were unsuccessful. That was just plain, common sense.

Embezzlement isn't just illegal, it's disloyal, too

This month's case involved the William Floyd Union Free School District, which took action against a former assistant superintendent and former treasurer under the little-noticed faithless servant doctrine.

New York courts adhere to the doctrine when employees have engaged in acts of disloyalty toward their employers. The doctrine holds that those employees may be required to return or abandon claims to employment compensation received during the period when they were behaving disloyally.

In this case, the disloyalty involved theft and embezzlement. Both employees pleaded guilty to various counts of grand larceny, including embezzling money from the school district. The school district sought to recover the stolen money, plus any deferred compensation that would have been owed to the defendants in retirement.

The simple reasoning: The district didn't owe anything to the very people who had stolen money from it.

When you suspect a disloyal employee ...

When you discover an employee has been stealing from your organization, think for a moment before you give in to the obvious knee-jerk reaction: terminating the employee immediately.

Advice: It may well pay—literally—to consider criminal prosecution, too. Follow that up with a lawsuit to recover any benefits or pay you may still be providing the employee.

Contact legal counsel as soon as you suspect potentially disloyal or criminal behavior. Your attorney can best advise you on the most effective approach.

The argument for payback

The essence of the first cause of action was that the employees had breached their fiduciary duty to the district by "committing egregious acts of disloyalty, disobedience, fraud and other misconduct." The district believed that it was entitled to recovery of paid compensation, as well as benefits.

In the second cause of action, the district sought a judgment under the faithless servant doctrine that it would not have to *continue to pay* the defendants any deferred compensation and health, life and dental insurance premiums, pursuant to employment and post-employment contracts "based upon their materially disloyal and egregious conduct."

The court noted the record had "clearly and unequivocally" established the defendants were guilty of stealing and laundering school district money. "It is a well established principle under New York law," stated the court, "that an agent is obligated 'to be loyal to his employer and is prohibited from acting in any manner inconsistent with this agency or trust

and is at all times bound to exercise the utmost good faith and loyalty in the performance of his duties.'"

An 'unfaithful agent'

New York law regarding disloyal or faithless performance of employment duties, developed over a century, allows the principal to recover "from its unfaithful agent any commission paid," and "an employer is entitled to the return of any compensation that was paid to the employee during the period of his disloyalty."

The court found that the "calculated larcenous conduct" warranted the "forfeiture of any and all obligations by the plaintiff school district for payments to them with respect to life, health, dental and any other insurance for a period of ten years."

Complete and permanent forfeiture

The case was appealed—and when the Appellate Division ruled, the school district came out an even bigger winner. The court did not agree that the defendants' forfeiture of insurance benefits should be limited to just 10 years.

Its decision said, "Where, as here, defendants engaged in repeated acts of disloyalty, complete and permanent forfeiture of compensation, deferred or otherwise, is warranted under the faithless servant doctrine." In other words, it concluded that those who steal from their employers are disloyal and shouldn't expect any return loyalty in the form of benefits that loyal employees receive.

The New York faithless servant doctrine can be a powerful weapon in the hands of a wronged employer.

As seen in this case, proof that an agent or employee has been disloyal and acted against an employer's interests means that the employee must return not only illegal profits, but also any compensation earned since the time of the misconduct.