ORAL ARGUMENT NOT YET SCHEDULED

IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

Nos. 08-1256, 08-1294

SECURITIES AND EXCHANGE COMMISSION,
Petitioner/Cross-Respondent,

v.

FEDERAL LABOR RELATIONS AUTHORITY,
Respondent/Cross-Petitioner,
and

NATIONAL TREASURY EMPLOYEES UNION,
Intervenor

ON PETITION FOR REVIEW AND CROSS-APPLICATION FOR
ENFORCEMENT OF A DECISION AND ORDER OF
THE FEDERAL LABOR RELATIONS AUTHORITY

BRIEF FOR THE FEDERAL LABOR RELATIONS AUTHORITY

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CERTIFICATE AS TO PARTIES, RULINGS, AND RELATED CASES

A. Parties and Amici

Appearing below in the administrative proceeding before the Federal Labor Relations Authority (Authority) were the National Treasury Employees Union (union) and the United States Securities and Exchange Commission (agency). The agency is the petitioner/cross respondent in this court proceeding; the Authority is the respondent/cross petitioner. The union is the intervenor.

B. Ruling Under Review

The ruling under review in this case is the Authority's decision in *United States Securities and Exchange Commission,* Case Nos. WA-CA-03-0127, WA-CA-03-0130, decision issued on May 30, 2008, reported at 62 F.L.R.A. 432.

C. Related Cases

This case has not previously been before this Court or any other court. Counsel for the Authority is unaware of any cases pending before this Court which are related to this case within the meaning of Local Rule 28(a)(1)(C).

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*Authorities upon which we chiefly rely are marked by asterisks.

GLOSSARY

ACT	*Ass'n of Civilian Technicians v. FLRA*, 269 F.3d 1112 (D.C. Cir. 2001)
ALJ	Administrative Law Judge
Authority or FLRA	Federal Labor Relations Authority
Border Patrol	*Dep't of Justice, United States Immigration and Naturalization Serv., United States Border Patrol, Laredo, Tex.*, 23 F.L.R.A. 90 (1986)
Br.	Brief
FAA	*Fed. Aviation Admin., Washington, D.C.* 27 F.L.R.A. 230 (1987)
FDIC	*Fed. Deposit Ins. Corp v. FLRA,* 977 F.2d 1493 (D.C. Cir. 1997)
FIRREA	Financial Institutions Reform, Recovery, and Enforcement Act of 1989
FLRA	Federal Labor Relations Authority
FY	Fiscal Year
Honeywell	*Honeywell Int'l, Inc.*, 253 F.3d 125 (D.C. Cir. 2001)
JA	Joint Appendix
Katz	*NLRB v. Katz*, 369 U.S. 736 (1962)
INS	*United States Dep't of Justice, United States Immigration and Naturalization Serv.*, 55 F.L.R.A. 892 (1999)

GLOSSARY
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NTEU or union	National Treasury Employees Union
NTEU	*Sec. and Exch. Comm. and NTEU*, 02 FSIP 122 (2002)
Panel	Federal Service Impasses Panel
Pay Parity Act	Investor and Capital Markets Fee Relief Act
PBGC	*Pension Benefit Guaranty Corp. v. FLRA*, 967 F.3d 658 (D.C. Cir. 1992)
QSI	Quality Step Increase
Scott AFB	*Dep't of the Air Force, Scott AFB, Ill.*, 5 F.L.R.A. 9 (1981)
SEC or agency	United States Securities and Exchange Commission
SEC	*United States Sec. and Exch. Comm., Washington, D.C.*, 61 F.L.R.A. 251 (2005)
Statute	Federal Service Labor-Management Relations Statute, 5 U.S.C. §§ 7101-7135 (2000)
WIGI	Within-grade Increase

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BRIEF FOR THE FEDERAL LABOR RELATIONS AUTHORITY

STATEMENT OF JURISDICTION

The Federal Labor Relations Authority ("Authority" or "FLRA") issued the decision and order under review in this case on May 30, 2008. The decision and order is published at 62 F.L.R.A. 432 and is included in the Joint Appendix (JA) at JA 793-806. The Authority exercised jurisdiction over the case pursuant to

§ 7105(a)(2)(G) of the Federal Service Labor-Management Relations Statute, 5 U.S.C. §§ 7101-7135 (2006) (Statute).[1] This Court has jurisdiction to review final orders of the Authority pursuant to § 7123(a) of the Statute, and to grant enforcement of Authority orders pursuant to § 7123(b) of the Statute.

STATEMENT OF THE ISSUES

1. Whether the Authority reasonably held that the United States Securities and Exchange Commission committed unfair labor practices by instituting a new pay system for its employees without bargaining with the union to the extent required by law.

2. Whether the remedy for the unfair labor practices ordered by the Authority was consistent with the Back Pay Act.

STATEMENT OF THE CASE

This case arises out of an unfair labor practice (ULP) proceeding brought under § 7118 of the Statute. The case involves an Authority adjudication of a ULP complaint based on a charge filed by the National Treasury Employees Union ("NTEU" or "union"). In pertinent part, the complaint alleged that the United States Securities and Exchange Commission ("SEC" or "agency") violated

[1] Pertinent statutory and regulatory provisions are set forth in the Addendum to this brief.

§ 7116(a)(1) and (5) of the Statute by implementing a new pay system without completing bargaining with the union to the extent required by the Statute. A hearing was held before an Administrative Law Judge (ALJ), who concluded that the SEC violated the Statute as alleged. After the SEC filed exceptions to the ALJ's decision and recommended order, the Authority issued a final decision holding that the SEC violated the Statute and ordering an appropriate remedy.

The SEC now seeks review and the Authority seeks enforcement of the Authority's final order. NTEU has intervened on behalf of the Authority.

STATEMENT OF THE FACTS

A. Background

The SEC is an independent Federal regulatory agency, whose mission is to administer and enforce the Federal securities laws in order to protect investors and maintain fair, honest, and efficient markets. At the time of the hearing before the ALJ, the agency employed approximately 3200 employees at its Washington, D.C. headquarters and in 11 regional and district offices around the country. A large percentage of its workforce are professionals such as attorneys, accountants, financial analysts, and securities examiners. In July 2000, NTEU was certified as the exclusive representative of the agency's headquarters, regional, and district employees, and approximately two-thirds of the agency's employees are in the

bargaining unit. During April and May of 2002, when the events material to this case were transpiring, the SEC and NTEU were negotiating, but had not reached, a comprehensive collective bargaining agreement. JA 680-681.

In January 2002, the Investor and Capital Markets Fee Relief Act, Pub. L. No. 107-123, 115 Stat. 2390 (2002) (Pay Parity Act) was enacted. In response to documented difficulties the SEC was having recruiting and retaining its professional staff, the Pay Parity Act provided that the SEC could set and adjust pay rates "without regard to the provisions of chapter 51 or subchapter III of chapter 53" of title 5 of the United States Code.[2] 5 U.S.C. § 4802(c). On or about January 17, 2002, the union requested to bargain over setting pay.[3] Negotiations over pay took place between April 22 and May 17, 2002. However, the parties

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[2] Chapter 51 of Title 5 establishes the position classification system that applies to the majority of Federal employees. Subchapter III of chapter 53 specifically provides for the basic rates of pay that attach to the classification levels established in chapter 51, *i.e.,* the "General Schedule."

[3] Where, as here, Federal agencies have discretion to fix compensation, levels of compensation are negotiable conditions of employment under the Statute. *Fort Stewart Schools v. FLRA*, 495 U.S. 641, 649 (1990).

were unable to reach agreement and the union filed for assistance with the Federal Service Impasses Panel (Panel) on May 15, 2002.[4] JA 683-686.

Subsequently, on May 17, 2002, the SEC notified its employees that it would implement its proposed pay plan for all employees, including those represented by NTEU, effective May 19, 2002. JA 686. Under the terms of the plan implemented on May 19, employees working in "securities industry (SI) positions" were to receive on average a 16-percent pay increase, while non-securities industry employees were to receive on average a 14-percent increase. Under the plan, employees were no longer eligible for Within-Grade Increases (WIGIs) and Quality Step Increases (QSIs),[5] and the SEC's pay parity implementation plan stated that these pay increases would place employees' salaries "toward the lower end" of those that the agency had analyzed, specifically those of regulatory agencies governed by the Financial Institutions Reform,

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[4] The Panel is an entity within the FLRA whose function is to provide assistance in resolving bargaining impasses between agencies and unions. 5 U.S.C. § 7119(c)(1). If voluntary efforts to resolve the impasse are unsuccessful, the Panel may impose contract terms on the parties. 5 U.S.C. § 7119(c)(5)(B), 5 C.F.R. § 2471.11(a).

[5] Under the General Schedule, WIGIs are periodic salary increases awarded to an employee who performs at "an acceptable level of competence." 5 U.S.C. § 5335. QSIs are additional increases granted in recognition of "high quality performance." 5 U.S.C. § 5336.

Recovery, and Enforcement Act of 1989 (FIRREA), Pub. L. No. 101-73, 103 Stat. 183 (1989).[6] JA 685.

Although the SEC implemented its pay plan on May 19, 2002, the agency's payroll office was unable to process the new plan until August of that year. On November 8, 2002, the Panel resolved the parties' bargaining impasse by ordering the adoption of a modified version of the SEC's final offer. *Securities and Exch. Comm. and NTEU*, 02 FSIP 122 (2002) (*NTEU*) (addendum to SEC's brief (Br.) at 1-15). A significant aspect of the SEC's final offer was that it abolished WIGIs and QSIs in favor of pay for performance. In ordering the adoption of a modified version of the SEC's final offer, the Panel rejected NTEU's proposal of step increases and cash awards based only on a determination that the employee was performing at an acceptable level of competence. *NTEU* at 7-8. On November 18, 2002, NTEU filed an unfair labor practice charge, and on June 30, 2003, the FLRA's General Counsel issued a complaint, alleging that the SEC unilaterally instituted a new pay system for unit employees and ceased granting employees

[6] FIRREA authorized certain financial regulatory agencies to determine their own compensation and benefit levels for their employees, without regard to the limitations of the General Schedule. Those agencies include the Federal Deposit Insurance Corporation, National Credit Union Association, Office of the Comptroller of the Currency, and Office of Thrift Supervision. JA 682-83.

WIGIs or QSIs without completing bargaining as required by the Statute. Subsequently, the case was heard by an Authority ALJ.

B. The ALJ's Decision

The ALJ found that the SEC's unilateral implementation of the pay system constituted ULPs in violation of § 7116(a)(1) and (5) of the Statute. JA 710. The ALJ first noted the general rule that when parties are engaged in bargaining over a proposed change, an agency is obligated to maintain the *status quo* pending the completion of the entire bargaining process, including the opportunity to pursue impasse procedures (citing *U.S. Dep't of Justice, Immigration and Naturalization Serv.*, 55 F.L.R.A. 892, 902-03 (1999) (*INS*)). He further stated that an agency may, however, assert as an affirmative defense that unilateral implementation of the change was "consistent with the necessary functioning of the agency, such that a delay in implementation would have impeded the agency's ability to effectively and efficiently carry out its mission" (citing *INS* at 904). JA 692-93.

As relevant here, the ALJ found that the agency had not demonstrated that a delay in implementation would have impeded the agency's ability to effectively and efficiently carry out its mission.[7] JA 710. The ALJ had framed the question

[7] The ALJ also rejected a number of other contentions by the SEC relating to its obligation to bargain over the pay plan. JA 693-701. The agency did not except to

(footnote continued on next page)

before him as whether the necessary functioning of the SEC depended on implementing the new pay system in May 2002. JA 704.

In concluding that the SEC committed ULPs as alleged, the ALJ first noted that the SEC acted contrary to its claim that the necessary functioning of the agency depended on implementing the new pay system on May 19, 2002. According to the ALJ, the agency could have rewarded employees in an effort to retain them and could have continued to pay WIGIs had it so chosen past May 19, but chose not to do either. In addition, the ALJ found that the fact that previous pay increases and special rates had already considerably reduced the pay gap between many employees of the SEC and those in FIRREA agencies diminished the agency's claim that it needed to act immediately in an attempt to reduce attrition. Moreover, the ALJ stated that since the SEC's plan paid employees at the "lower end" of the salary structures at FIRREA agencies, the raise was not as substantial as the SEC asserted and, therefore, would not have a dramatic effect on attrition rate. JA 705.

The ALJ also found that the SEC's claim that it needed to implement its plan in May was undercut by several facts. First, the ALJ found that the employees did

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these findings and therefore they were not at issue before the Authority, nor are they at issue before the Court.

not actually receive additional compensation until August, 2002. Second, the ALJ rejected the agency's assertion that it needed to use $25 million in reprogrammed funds by September 2002 for employee pay, or face the prospect of losing this money for employee compensation. In rejecting the assertion, the ALJ relied on the testimony of the SEC's executive director who stated that the funds could be kicked forward into the next fiscal year as well. JA 705-06.

The ALJ also stated that if implementation was as urgent as suggested by the SEC, then the agency could have begun negotiations in January, when first requested by the Union, rather than waiting until April. Finally, the ALJ emphasized that implementation of the pay system was not an exercise of a management right because the SEC was required to bargain over the substance of the new pay system, which distinguished this case from *Department of Justice, United States Immigration and Naturalization Service, United States Border Patrol, Laredo, Texas*, 23 F.L.R.A. 90 (1986) (*Border Patrol*), on which the SEC relied. JA 708-710.

Accordingly, the ALJ concluded that the SEC violated § 7116(a)(1) and (5) of the Statute by implementing its pay system on May 19. To remedy the violation, the ALJ awarded retroactive WIGIs to employees entitled to such increases between May 19 and November 8, 2002, and ordered the Respondent to

recalculate their placement on the new pay schedule. Affected employees were to receive back pay for any pay actually lost as a result of the agency's illegal implementation.

C. The Authority's Decision

Before the Authority, the SEC excepted to both the ALJ's finding that the agency violated the Statute and to the ALJ's recommended remedy. With respect to the merits of the case, the Authority held that the record fully supported the AJL's conclusion that the SEC did not show that a delay in implementation of the pay system would have impeded the agency's ability to effectively and efficiently carry out its mission, and that none of the agency's arguments established otherwise. JA 800. In addition, the Authority held that the recommended remedy was not contrary to the Back Pay Act and did no more than make affected employees whole. JA 803.

1. The SEC's Violation of the Statute

The Authority affirmed the ALJ's holding that the SEC violated the Statute as alleged, specifically addressing the ALJ's conclusion that immediate implementation of the pay plan was not necessary for the effective functioning of the agency. The Authority held that the ALJ's conclusion was supported by his findings that the SEC could have used other financial inducements to retain

employees, and that SEC's proposed salary structure was placed toward the lower end of those of the other financial regulatory agencies. The Authority also noted that for the purposes of employee retention, the SEC had already narrowed the pay gap between it and other financial regulatory agencies with its pay increase in 2001 and that employees did not actually receive increased pay from the proposed new salary structure until August, 2002. Furthermore, the Authority cited the testimony of the Respondent's executive director that $25 million in FY 2002 funds could have been used in FY 2003 for purposes of pay implementation. Lastly, the Authority referenced the ALJ's determination that the SEC's pay implementation date was an artificial creation of agency management. JA 800.

The Authority also rejected the arguments raised in the SEC's exceptions. First, the Authority found that the ALJ was not required to consider uncertainty as to how long Panel resolution of the case might take when applying the necessary functioning test. Second, the Authority found even if it were to view certain of the ALJ's findings[8] as speculative, the SEC had not demonstrated that the ALJ erred in

[8] The SEC argued that the ALJ's finding that the SEC could have administratively prepared to implement its new pay system while the matter was before the Panel was speculative given the uncertainty of the Panel's decision. It argued further that the ALJ speculated in finding that the SEC would have presented the exact same pay system to the Panel even if it had continued to grant employees WIGIs between May 19, 2002, and the Panel's decision in November. JA 801.

concluding that it was not necessary for the functioning of the Agency to implement its pay plan on May 19. In this regard, the Authority noted that the SEC voluntarily chose to eliminate the payment of WIGIs, and it did not provide employees with any increase in pay until three months after implementation. JA 800-801

The Authority also rejected the SEC's claim that the ALJ erred in finding that the agency could have used the FY 2002 appropriations for the new pay system in 2003. It found that the Comptroller General decisions concerning retroactive pay raises relied upon by the agency were inapposite. According to the Authority, these are distinguishable because they involve retroactive promotions under the General Schedule, not implementation of a new pay system based on a specific congressional authorization. In addition, the Authority found that to the extent the agency disputed the ALJ's understanding of the testimony of the agency's executive director, the ALJ's factual finding in this regard is sufficiently supported by the record. In this regard, the Authority cited testimony of the executive director to the effect that the $25 million would "still be there" if not used in FY 2002 and that "it would be an easy matter . . . to have it then kicked forward into the next fiscal year as well[.]" JA (quoting Tr. at 244-45 (JA 251-52)). Moreover, the Authority noted, the executive director further testified that even if

that money were lost, he thought it "was highly likely" that the pay system would be funded from FY 2003 regular appropriations. Consequently, the Authority concluded that the executive director's testimony directly contradicts the SEC's claim that implementation of the pay system on May 19 was necessary to assure its funding. JA 801.

The Authority also rejected the SEC's contention that the ALJ applied an improper standard in reaching his conclusion and, in that regard, found that SEC's reliance on the Authority's decision in *Border Patrol* was misplaced. With regard to *Border Patrol*, the Authority noted that it involved a QCR (question concerning representation) that had been pending for nearly six years and that the unilateral change constituted the exercise of a management right that was not substantively negotiable. The Authority emphasized that in this case, the ALJ was presented with the question of whether the unilateral implementation of the fully negotiable salary system in May 2002 was necessary for the functioning of the agency. JA 802.

2. The Remedy

The SEC also excepted to the ALJ's recommended order insofar as it awarded retroactive WIGIs, contending that the order was contrary to the Back Pay Act because the agency committed no unjustified or unwarranted personnel action and that no employees actually lost money once the conversion to the new pay system was made.[9] JA 802

The Authority first noted that a "personnel action" under the Back Pay Act specifically includes a failure to take an action or confer a benefit (citing 5 C.F.R. § 550.803) and that the Authority has expressly ruled that employees have been affected by an unjustified or unwarranted personnel action when it is determined that they were affected by a ULP under the Statute (citing *Fed. Aviation Admin., Washington, D.C.,* 27 FLRA 230, 232-33 (1987) (*FAA*)). JA 802

The Authority found it undisputed that employees who would have otherwise received increases in pay through WIGIs prior to the Panel's decision did not receive those WIGIs. Accordingly, the Authority held that back pay was warranted because the employees entitled to a WIGI between May 19 and

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[9] In pertinent part, the Back Pay Act, 5 U.S.C. § 5596, authorizes back pay for employees affected by an unjustified or unwarranted personnel action which resulted in the withdrawal or reduction of all or part of the pay, allowances or differentials of the employee. 5 U.S.C. § 5596((b)(1).

November 8 did not receive them and because they were converted into the new pay system at a lower pay rate than they would have been had they first received a WIGI. JA 802-03

The Authority also rejected the SEC's arguments that the Panel's decision precludes the payment of WIGIs the employees would have received between May 19 and November 8, 2002. In that regard, the Authority noted that, although the Panel rejected WIGIs as part of the pay system that it ordered adopted, it was clear that the order was prospective, not retroactive, and therefore did not affect the ALJ's recommended remedy. JA 803.

The Authority also found the SEC's reliance on *United States Securities and Exchange Commission, Washington, D.C.*, 61 F.L.R.A. 251 (2005) (*SEC*) to be unavailing. The Authority stated that *SEC* was limited to the determination that locality pay may be considered part of base pay under the Pay Parity Act. Finally, the Authority determined that restoration of the WIGIs was an appropriate make-whole remedy. JA 803.

STANDARD OF REVIEW

Authority decisions are reviewed "in accordance with the Administrative Procedure Act," and may be set aside only if found to be "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law[.]" *Bureau of*

Alcohol, Tobacco and Firearms v. *FLRA*, 464 U.S. 89, 97 n.7 (1983); *see also Pension Benefit Guaranty Corp.* v. *FLRA*, 967 F.2d 658, 665 (D.C. Cir. 1992) (*PBGC*).

This Court has noted that "[w]e accord considerable deference to the Authority when reviewing an unfair labor practice determination, recognizing that such determinations are best left to the expert judgment of the FLRA." *Fed. Deposit Ins. Co.* v. *FLRA*, 977 F.2d 1493, 1496 (D.C. Cir. 1992) (*FDIC*) (internal quotations omitted). As a result, "[o]ur scope of review is limited." *PBGC*, 967 F.2d at 665. So long as the Authority "provide[s] a rational explanation for its decision," it will be sustained on appeal. *FDIC*, 977 F.2d at 1496.

Where, as here, the Authority interprets its own enabling statute, "[the Court is] mindful that we owe great deference to the expertise of the Authority as it exercises its special function of applying the general provisions of the Act to the complexities of federal labor relations." *Ass'n of Civilian Technicians* v. *FLRA*, 269 F.3d 1112, 1115 (D.C. Cir. 2001) (internal quotations omitted) (*ACT*). Similarly, "[the Court] defer[s] to the Authority's interpretation of its own precedent." *Nat'l Treas. Employees Union* v. *FLRA*, 399 F.3d 334, 339 (D.C. Cir. 2005).

Review of the Authority's factual determinations is narrow. The Court is "to affirm the FLRA's findings of fact if supported by substantial evidence on the record considered as a whole." *PBGC*, 967 F.2d at 665 (internal citations omitted); *see also* 5 U.S.C. § 7123(c) ("[t]he findings of the Authority with respect to questions of fact, if supported by substantial evidence on the record considered as a whole, shall be conclusive"). In addition, the Authority is entitled to have reasonable inferences it draws from its findings of fact not be displaced, even if the court might have reached a different view had the matter been before it *de novo*. *See AFGE, Local 2441 v. FLRA*, 864 F.2d 178, 184 (D.C. Cir. 1988); *see also LCF, Inc. v. NLRB*, 129 F.3d 1276, 1281 (D.C. Cir. 1997).

SUMMARY OF ARGUMENT

1. It is well established, in both the private and federal sectors, that an employer may not unilaterally implement changes in conditions of employment of represented employees without completing bargaining to the extent required by law. As the ALJ recognized in the instant case, enforcement of the unilateral change doctrine is necessary to protect the integrity of the bargaining process.

The federal employer agency here, the SEC, does not dispute that it implemented a new pay policy for bargaining unit employees before completing bargaining, including impasse resolution proceedings before the Federal Service

Impasses Panel. However, the agency contends that it should avoid ULP liability because its conduct fell within a recognized exception to the unilateral change doctrine, namely, that its actions were consistent with the "necessary functioning" of the agency, such that a delay in implementation would have impeded the agency's ability to effectively and efficiently carry out its mission. The agency's contentions lack merit.

In ULP proceedings, a party asserting an affirmative defense such as the "necessary functioning" exception bears the burden of establishing that defense. The Authority reasonably held in the instant case that the SEC failed to meet that burden. Contrary to the agency's contentions, the Authority found that implementation in May 2002 of a new pay structure for employees was not necessary to assure sufficient funding of the pay plan. In so finding, the Authority relied on testimony of the SEC's executive director that funds earmarked for FY 2002 could be used in FY 2003 and, that in any event, the executive director expected sufficient additional funding for FY 2003. The Authority also noted that although the agency announced the implementation in May 2002, no pay increases were received until August of that year. Although the raises granted in August 2002 were retroactive to May 2002, the fact that no raises were actually received until three months after implementation undercuts the agency's contention that it

was necessary to impose the new pay system before completing its bargaining obligation.

Contrary to the SEC's contention, the Authority properly refused to grant deference to the agency's judgment with respect to the necessity of the unilateral implementation. In that regard, and as noted above, the Authority's regulations specifically provide that affirmative defenses must be established by a preponderance of the evidence. Further, granting an agency deference with respect to the "necessary functioning" exception would turn the unilateral change doctrine on its head, allowing the exception to swallow up the rule. To the contrary, the Authority has consistently held employers asserting the necessary functioning exception to a "demanding" standard.

2. Contrary to the SEC's arguments, the Authority's remedy satisfies the criteria of the Back Pay Act. First, employees were affected by an unjustified or unwarranted personnel action, namely, the agency's illegal implementation of the new pay system. Second, subsequent to the unilateral implementation some employees suffered a withdrawal of specific pay increases, *i.e.*, WIGIs. Third, the agency's unilateral implementation of its pay plan was the cause of those withdrawals because had the SEC maintained the *status quo* until bargaining was completed as required by law, some employees would have received WIGIs.

The SEC argues, however, that the back pay remedy is inappropriate because no employee actually suffered a loss of pay as a result of the agency's premature implementation of its pay plan. The agency's arguments are incorrect. The Authority's remedy guarantees that any employee who, in fact, lost pay as a result of the agency's action will be made whole, but does not, as the agency erroneously claims, award non-deserving employees a windfall.

It is not disputed that some employees would have received WIGIs but for the agency's illegal implementation. What is not known from the current record is which, if any, employees actually suffered a loss of net pay as a result of the agency's conduct. Accordingly, the Authority's order requires the agency to first determine which employees would have received WIGIs between May and November 2002. The agency must then award WIGIs to those employees retroactive to their eligibility date and recalculate the employees' compensation ,including the appropriate placement of those employees in the new system. Once the employees' entitlements are recalculated, the agency is required to pay back pay for the *difference* between what they would have received had they been granted the WIGIs and what they actually received under the new system. If, in fact, there was no net loss of pay, employees will not receive back pay. Accordingly, if the SEC is correct that no employee actually lost money as a result

of its illegal action, the agency will have no back pay liability. On the other hand, if any employees lost net pay, those employees will be made whole.

Further, it is settled law that where, as here, there are factual disputes about the extent, if any, of back pay liability, those disputes do not render the remedy inappropriate. Instead, these matters are appropriate for consideration during compliance proceedings. A definitive answer to the question of which employees, if any, actually lost pay because of the withdrawal of WIGIs can not be ascertained until the agency searches its records and makes the appropriate calculations.

Because the Authority reasonably held that the SEC committed ULPs and crafted an appropriate remedy, the agency's petition for review should be denied and the Authority's order should be enforced.

ARGUMENT

I. THE AUTHORITY REASONABLY HELD THAT THE UNITED STATES SECURITIES AND EXCHANGE COMMISSION COMMITTED UNFAIR LABOR PRACTICES BY INSTITUTING A NEW PAY SYSTEM FOR ITS EMPLOYEES WITHOUT BARGAINING WITH THE UNION TO THE EXTENT REQUIRED BY LAW

A. General Legal Principles

It is a cardinal principle of labor law, in both the private and federal sectors, that an employer may not unilaterally implement changes in conditions of employment of represented employees without completing bargaining to the extent

required by law. *NLRB v. Katz*, 369 U.S. 736, 742-43 (1962) (*Katz*); *Honeywell Int'l, Inc. v. NLRB*, 253 F.3d 125, 131 (D.C. Cir. 2001) (*Honeywell*); *FDIC*, 977 F.2d at 1497-98. It makes no difference whether the change adds to or subtracts from employee' wages, or whether it institutes a new policy or withdraws one that already exists. *Daily News of Los Angeles v. NLRB*, 73 F.3d 406, 411 (D.C. Cir. 1996).

A unilateral change in conditions of employment under negotiation circumvents the objectives of federal labor law as much as a flat refusal to bargain. *Katz*, 369 U.S. at 743. In that regard, this Court has stated:

> A unilateral change not only violates the plain requirement that the parties bargain over wages, hours, and other terms and conditions, but also injures the process of collective bargaining itself. Such unilateral action minimizes the influence of organized bargaining. It interferes with the right of self-organization by emphasizing to the employees that there is no necessity for a collective bargaining agent.

Honeywell, 253 F.3d at 131 (internal quotations omitted). As the ALJ found in the instant case, enforcement of the unilateral change doctrine protects the integrity of the bargaining process. JA 710; *see also Dep't of the Air Force, Scott Air Force Base, Ill.* 5 F.L.R.A. 9, 10-11 (1981) (*Scott AFB*) (the obligation to bargain would be rendered "meaningless," if a party were able to unilaterally change conditions of employment).

Like any rule, the unilateral change doctrine is subject to exceptions. For example, in the private sector, an employer may act unilaterally if faced with an "economic exigency." *Vincent Indus. Plastics, Inc. v. NLRB*, 209 F.3d 727, 734 (D.C. Cir. 2000). However, an economic exigency "must be a heavy burden and must require prompt implementation." *Id.* Further, the employer must demonstrate that the exigency "was caused by external events, was beyond the employer's control, or was not reasonably foreseeable." *Id.*[10]

Somewhat analogous to the private sector's economic exigency exception is the "necessary functioning" exception developed by the Authority for application in the Federal sector. Whether this exception applies in the instant case is the issue before this Court. Under this doctrine, an agency may escape liability for a unilateral change where it establishes, with evidence, that its actions were in fact consistent with the necessary functioning of the agency, such that a delay in implementation would have impeded the agency's ability to effectively and efficiently carry out its mission. *INS*, 55 F.L.R.A. at 904; *see also Dep't of the*

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[10] Another exception in both the private and federal sectors applies when the union waives its right to bargain. However, here also, there is a heavy burden for the employer to establish that the exception applies, *i.e.*, the employer must demonstrate that the union's waiver was "clear and unmistakable." *Honeywell*, 253 F.3d at 133; *Scott AFB*, 5 F.L.R.A. at 9-11.

Treasury, Bureau of Alcohol Tobacco and Firearms, 18 F.L.R.A. 466, 469 (1985).[11] Under the federal sector scheme, the obligation to bargain includes the maintenance of the *status quo*, subject to the necessary functioning exception, until the completion of proceedings before the Panel. *United States Immigration and Naturalization Serv., Washington, D.C.*, 55 F.L.R.A. 69, 72-73 (1999).

Where an agency asserts the necessary functioning defense, the issue is not the agency's judgment in adopting its proposed practice, but rather, the timing of the change – specifically, whether it was necessary to implement the practice *before completing the obligation to bargain. INS*, 55 F.L.R.A. at 904. As is the case with the other exceptions to the unilateral change doctrine, the employer bears a heavy burden to establish an entitlement to the "necessary functioning" exception.

As will be demonstrated below, the Authority reasonably held that the SEC did not demonstrate that a delay in implementing its pay policy would have impeded the agency's ability to effectively and efficiently carry out its mission. Further, none of the SEC's contentions to the contrary have merit.

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[11] The exception has also been characterized as one involving "an overriding exigency . . . which required immediate implementation." *U.S. Dep't of the Air Force, 832D Combat Support Group, Luke Air Force Base, Ariz.*, 36 F.L.R.A. 289, 300 (1990) (ALJ decision adopted by the Authority)

B. The Authority's Holding was Consistent with Law and Supported by Substantial Evidence

As discussed above, an employer is generally prohibited from changing conditions of employment of represented employees without completing bargaining to the extent required by law. The SEC does not dispute that it implemented a new pay policy for bargaining unit employees before completing bargaining, including impasse resolution proceedings before the Panel. However, the agency contends that its action was justified because it fell within the necessary functioning exception to the general rule.

In defending its conduct, the SEC introduced evidence that it was granted authority to establish its own compensation plan in order to enhance the recruitment and retention of the professional staff required to accomplish its mission and that its proposed pay plan would further that goal. However, the question before the ALJ and the Authority was not whether the agency's pay plan would in some measure increase the effectiveness and the efficiency of the agency, but whether a *delay in implementation* would significantly undermine the effective functioning of the agency.

Under the Authority's procedures, the burden rests on the party asserting an affirmative defense to prove that defense by a preponderance of the evidence. 5 C.F.R. § 2423.32. The Authority's determination that the SEC had not met its

burden in the instant case is supported by substantial evidence. Substantial evidence is "such relevant evidence as a reasonable mind might accept as adequate to support a conclusion." *Thomas v. NLRB*, 213 F.3d 651, 657 (D.C. Cir 2000). It is "something less than the weight of the evidence, and the possibility of drawing two inconsistent conclusions from the evidence does not prevent an administrative agency's finding from being supported by substantial evidence." *Consolo v. Fed. Maritime Comm.*, 383 U.S. 607, 620 (1966).

The SEC specifically contends that two factual findings are not supported by substantial evidence. First, the Authority rejected the SEC's contention that implementation of the pay system in May 2002 was necessary to assure its funding.[12] In so doing, the Authority reasonably relied on the testimony of the agency's executive director. Although the executive director stated that the $24.8 million reprogrammed for pay purposes was earmarked for Fiscal Year (FY) 2002, nothing in his testimony indicated that the agency would be unable to fund pay increases granted after May 2002. To the contrary, the executive director testified that the $24.8 million was more than the agency needed to fund the FY 2002 pay

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[12] It bears repeating that the question before the Authority is whether implementation in May 2002 was necessary for the effective accomplishment of the agency's mission, not whether implementation at that time would be the most efficient use of resources.

increases and that the agency requested the entire amount "so that if we didn't spend it all the fiscal year, it would still be there . . . and it would be an easy matter . . . to have it kicked into the next fiscal year." JA 251-52. Further, the executive director testified that for FY 2003, "it was highly likely that we were going to get other money for [pay] from our regular appropriation." Accordingly, nothing in the executive director's testimony indicated that sufficient funding to pay for whatever compensation system resulted from negotiations would not be available if the agency did not implement its new pay system in May 2002.

The Authority also found that the fact that there was a three-month delay before employees actually received a pay increase undercuts the agency's claim that immediate implementation was necessary. Contrary to the SEC's suggestion in its brief (Br. 43), the ALJ recognized that the pay increases actually paid out in August 2002 were made retroactive to May 19, 2002. JA 686-87 n.7. Nonetheless, it remains true, as the ALJ and the Authority found, that employees received no actual (as opposed to potential) benefit until August. In addition, as the Authority noted, during the interim, employees otherwise due WIGIs were denied such, thus actually reducing the pay the employees would have received during that period, but for the agency's action. Such a result is at odds with the SEC's contention that it had to increase employee pay as quickly as possible. Finally, the impact on

recruitment and retention of potential retroactive increases is somewhat speculative. In any event, and as the ALJ noted (JA 706-07), the agency could have achieved the same result by agreeing to make any negotiated salary increases retroactive.

C. The SEC was not Entitled to Deference Before the Authority

The SEC also contends (Br. 45-49) that its judgment on the necessity of immediate implementation should have been granted a high degree of deference. The agency's contentions are without merit.

In that regard, the SEC concedes (Br. 45-46) that the cases it cites in support of this claim all arise in the context of judicial review of agency actions under the Administrative Procedures Act (APA), and that there is no support in either statute or judicial precedent for according deference to a party in Authority ULP proceedings. Nonetheless, it baldly asserts (Br. 46) that there is ample reason to grant deference here. Contrary to the agency's contention, there is no reason to do so and there are reasons not to. With respect to judicial review under the APA, § 706 of the APA expressly provides for a limited scope of review of agency actions. Agency actions are to be set aside only when they are arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law. 5 U.S.C. § 706(2)(A). Further, agency factual determinations will be reversed only if

they are unsupported by substantial evidence. 5 U.S.C. § 706(2)(E). No similar deferential standards are found in the Statute's ULP provisions or in the Authority's regulations. Rather, the Authority's General Counsel must prove the elements of the ULP by a preponderance of the evidence and the party asserting any affirmative defenses bears the same burden with respect to those defenses. 5 C.F.R. § 2423.32.

Further, granting an agency deference with respect to the "necessary functioning" exception would turn the unilateral change doctrine on its head. As discussed above (pp. 21-22), the unilateral change doctrine is designed to protect the integrity of the statutorily-mandated collective bargaining process. As such, both the National Labor Relations Board and the Authority properly place a heavy burden on those employers seeking to escape ULP liability for unilateral changes. According agencies deference whenever they assert the necessary functioning exception would allow the exception to swallow up the rule.[13]

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[13] The ALJ noted (JA 703) that, to the extent *Border Patrol*, 23 F.L.R.A. at 93, might be read to imply that the Authority will defer to agency determinations of necessity in unilateral change cases, *Border Patrol* is atypical. To the contrary, appeals to deference have been rejected, and the Authority has consistently required agencies asserting the necessary functioning exception to provide affirmative support for their contentions. *See, e.g., INS*, 55 at 904-05; *Id.* at 915 (ALJ decision adopted by the Authority) (Authority's standard is "demanding");

(footnote continued on next page)

The SEC concludes (Br. 48-49) by asserting that the Authority should give deference to the SEC's judgment because determining whether delaying implementation would adversely affect the agency's mission is not "within the areas of expertise of the FLRA." The SEC misstates the role of the Authority. Resolving complaints of ULPs, and balancing the rights of employees to bargain with the need for an effective and efficient government are within the Authority's expertise. *See, e.g., EEOC v. FLRA*, 744 F.2d 842 (D.C. Cir. 1984) (Statute was designed to balance the collective bargaining rights of federal employees with the need for federal managers to achieve an effective and efficient government. Congress established the Authority to administer the Statute). In carrying out this responsibility the Authority must, based on the record created by the parties, make the findings necessary to resolve the disputes before it. In that regard, this Court has specifically recognized "the expertise of the Authority as it exercises its special function of applying the general provisions of the [Statute] to the complexities of federal labor relations." *ACT*, 269 F.3d at 1115. Presumably, the Authority was exercising that function in the instant case.

Olam Sw. Air Defense Sector (TAC) Point Arena Air Force Station, Point Arena Cal, 51 FLRA 797, 827 (1996) (ALJ decision adopted by the Authority).

D. The Authority's Application of the "Necessary Functioning" Exception was not Arbitrary and Capricious

The SEC also contends (Br. 49-53) that the Authority's decision was arbitrary and capricious because it failed to give a reasoned explanation for its findings and conclusions. However, in none of the specific instances cited by the agency did the Authority fail to provide an adequate explanation.[14]

First, the agency mistakenly contends (Br. 36-37) that the Authority failed to adequately distinguish *Border Patrol*. In *Border Patrol*, the Authority found that the agency did not commit ULPs when it unilaterally changed shift and rotation schedules for agents patrolling the Mexican border. As the Authority noted (JA 802), *Border Patrol* was based in part on the fact that the change involved the exercise of a statutorily reserved right. *See Border Patrol*, 23 F.L.R.A. at 93 (holding that "the changes in the shift and rotation schedules *which involved the exercise of management's section 7106(b)(1) rights* were necessary for the

[14] In addition to the specific matters discussed immediately below, the SEC states (Br. 50) that the Authority failed to address "why the [SEC] did not satisfy the 'consistent with the necessary functioning' test generally." However, both the ALJ and the Authority pointed out that the burden is on the agency to establish necessity and proceeded to discuss at length each of the agency's proffered reasons. *See* JA 701-710 (ALJ); JA 800-802 (Authority). No further explanation is required.

[agency] to perform its mission." (emphasis added)).[15] Here, in contrast, the change involved a fully negotiable condition of employment.[16]

The SEC also contends (Br. 50-52) that the Authority did not articulate the requirements that an agency must meet to satisfy the "necessary functioning" exception and that the FLRA did not discuss its rationale for refusing to grant the agency's determination deference. To the contrary, in its regulations and in its precedent the Authority has made it clear that the party asserting any affirmative defense must establish that defense by a preponderance of the evidence. 5 C.F.R. § 2423.32; *United States Dep't of Defense, Defense Contract Mgmt. Agency, Orlando, Fla.*, 59 F.L.R.A. 223, 226 (2003). Further, the test for establishing the necessary functioning exception is well established in Authority precedent. An agency must establish, *with evidence*, that a delay in implementation would have

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[15] With respect to the agency's obligation to bargain the impact and implementation of the change in *Border Patrol*, the Authority found that the union had filed a grievance over that issue and therefore consideration of that issue was barred by § 7116(d) of the Statute. *Border Patrol*, 23 F.L.R.A. at 93.

[16] The SEC also contends (Br. 38) that its rights under § 7106(a) of the Statute are indirectly implicated by its decision to implement the new pay policy. As this argument was not presented to the Authority, it is not properly before the Court. 5 U.S.C. § 7123(c). Nonetheless, the Authority has held that indirect effects on management rights do not affect the obligation to bargain under the Statute. *See, e.g., AFGE, Local 1698*, 38 F.L.R.A. 1016, 1023-26 (1990); *see also NFFE, Local 951 v. FLRA*, 412 F.3d 119, 339-43 (D.C. Cir. 2005).

impeded the agency's ability to effectively and efficiently carry out its mission. *INS*, 55 F.L.R.A. at 904 (1999). The agency cannot claim here that it did not understand its burden.

Finally, the agency mistakenly claims that the Authority did not adequately discuss the cited precedent from the General Accounting Office (now Government Accountability Office) (GAO). The SEC cited the GAO precedent to support its contention that the funds reprogrammed for pay purposes in FY 2002 could not be used for payroll purposes in FY 2003. As the Authority correctly noted, these cases (*Matter of Wirth - Retroactive Personnel Action*, B-228711 (Comp. Gen. 1988); *Matter of Levy - Arbitration of Retroactive Promotion and Backpay*, B-190408, (Comp. Gen. 1997)), involved an entirely different matter, namely an agency's authority under the General Schedule to grant individual employees retroactive promotions. These cases did not involve the allocation of appropriations over different fiscal years. As such they did not support the contention the agency was making before the Authority.

II. THE REMEDY FOR THE UNFAIR LABOR PRACTICES ORDERED BY THE AUTHORITY WAS CONSISTENT WITH THE BACK PAY ACT

A. Back Pay Is Appropriate For All Employees Who Would Have Received Higher Pay But For The Agency's Unwarranted Personnel Action

An award under the Back Pay Act (5 U.S.C. § 5596) requires a determination that: 1) the employee was affected by an unjustified or unwarranted personnel action; 2) the employee suffered a withdrawal or reduction of all or part of his pay, allowances, or differentials; and 3) but for the unjustified action, the employee would not have experienced the withdrawal or reduction. *SSA v. FLRA*, 201 F.3d 465, 468 (D.C. Cir. 2000).

The Authority's remedy in the instant case clearly satisfies the Back Pay Act's criteria. It is well established, and the SEC does not dispute, that employees have been affected by an unjustified or unwarranted personnel action when it is determined that the employees were affected by a ULP under the Statute. *See* 5 U.S.C. § 5596(b)(1); *FAA*, 27 F.L.R.A. at 232-33. Secondly, it is also undisputed that specific pay increases, *i.e.*, WIGIs, were terminated after the SEC unilaterally implemented its new pay plan in May 2002. Thus, employees suffered a withdrawal of pay. Thirdly, it is also undisputed that some undetermined number of employees were scheduled for WIGIs between May 2002 and November 2002

when bargaining was completed with the FSIP decision. Had the SEC maintained the *status quo* as required by law until bargaining was completed, those employees would have received WIGIs. Accordingly, it is evident that the agency's unilateral implementation of its pay plan caused those employees not to have received their otherwise scheduled pay increases. Thus, the third criterion is satisfied as well.

The SEC contends (Br. 59-61), nonetheless, that the causal criterion is not satisfied. However, the SEC never denies that WIGIs would have been granted but for its unilateral action. Rather, the agency appears to be arguing something different. Relying on *AFGE, SSA Council 220 v. FLRA*, 840 F.2d 925, 931 (D.C. Cir. 1988) (*Council 220*) and *FAA*, the agency contends that the measure of the impact of the agency's unilateral action was not the withdrawal of the WIGIs, but the ultimate result of bargaining, *i.e.*, the Panel's order. The agency is mistaken, because the situations in *FAA* and *Council 220* are readily distinguishable from the instant case. In both *FAA* and *Council 220*, the agency committed ULPs by implementing operational changes pursuant to their reserved management rights without bargaining the impact and implementation of the changes. In *FAA*, the change was a reorganization that impacted premium pay of some unit members, 27 F.L.R.A. at 230, and in *Council 220*, the employer implemented changes in employee performance evaluations, 840 F.2d at 926. In both cases, the precise

impact on employee compensation could not be determined. Accordingly, in *FAA* the Authority determined that the result of subsequent bargaining "will most closely approximate the result which would have occurred if the agency had initially bargained as required." 27 F.L.R.A. at 234. This Court applied the same principle in *Council 220*. 840 F.2d at 930-31.

Here the agency was not implementing a change that had uncertain impact on employee compensation, but rather was implementing a direct change in compensation policy. The impact was thus immediate and certain, *i.e.,* employees who would otherwise receive WIGIs would no longer receive them. Thus, it is evident that back pay is warranted under the Back Pay Act for any employee who suffered a net loss of pay as a result of being denied a WIGI.[17]

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[17] The SEC suggests (Br. 60) that the Authority cannot prove that any reduction in pay would not have occurred absent a ULP, because the Panel's order did not specifically order retroactive awards of WIGIs (Br. 60, n.24). The Authority considered and rejected that argument because the Panel does not resolve ULP allegations. JA 803. Although the Panel rejected WIGIs as part of the pay system that its order adopted, it is clear that the order was to have only prospective, not retroactive effect.

B. Individual Entitlement to Back Pay is a Matter for Compliance Proceedings

The SEC's principal argument regarding the remedy is that back pay is not appropriate because, in fact, no employee suffered a loss of pay as a result of the agency's premature implementation of its pay plan. *See* Br. 54-59. The agency contends (Br. 56 n.20), therefore, that the Authority's remedial order would result in "a windfall to the vast bulk of employees who from the outset profited from the new system." However, the agency's concerns are unfounded. Careful attention to both the Authority's order and the terms of the Back Pay Act reveals that no employee will receive such a windfall.

The ALJ found that an undetermined but small group of employees would have received more pay, not only in 2002, but in subsequent years, had the agency not implemented the new pay plan in May 2002. JA 714. In so concluding, the ALJ noted that an employee who would have been eligible for a WIGI between May 19 and November 8 would have benefited in a delay in implementation, because he or she would have been converted to the new system at a higher step, a benefit that would continue to accrue in subsequent years. *Id.* However, neither the ALJ nor the Authority could determine from the record which, if any, employees were so impacted or, if they were, the precise extent of the any impact. JA 715.

The Authority properly determined that any employee who did, in fact, lose pay as a result of the agency's action should be made whole. *See Council 220*, 840 F.2d at 930 (finding a preference in favor of make whole relief in ULPs). To effectuate the required make whole relief, the Authority crafted an appropriate order. The order requires the agency to first review the personnel records of unit employees to determine who met the statutory criteria for WIGIs. JA 804, ¶ 2(a)(1) and (2). The agency is then to award WIGIs to those employees retroactive to their eligibility date and recalculate the appropriate placement of those employees in the new system. *Id.* at ¶ 2(a)(3) and (4). Once the employees' entitlements are recalculated, the agency is required to pay back pay, with interest, *for all pay they lost, i.e.*, the difference between what they would have received had they been granted the WIGIs and what they actually received. *Id.* at ¶ 2(b). If, in fact, there was no net loss of pay, employees will not receive back pay. Accordingly, if the SEC is correct that no employee actually lost money as a result of its illegal action, the agency will have no back pay liability and no employee will receive a windfall.

In that regard, the ALJ made it clear that he intended the order to provide back pay only to those employees who actually lost money, not provide a windfall to employees. According to the ALJ, "the agency must . . . calculate what pay

and allowances these employees would have received in the years since 2002, while deducting the pay and allowances the employees actually received, and *to pay the employees the difference*." JA 715. Further, the Authority's order, as described above, is consistent with the terms of the Back Pay Act which provide that upon correction of unwarranted personnel actions, an employee is to receive an amount equal to all or any part of the pay, allowances, or differentials, as applicable, which the employee would have earned or received during the period if the personnel action had not occurred, less other amounts earned by the employee. 5 U.S.C. § 5596(b)(1)(A)(i).

Finally, it is well established that where there are factual disputes about the extent, if any, of back pay liability, those disputes do not render the remedy inappropriate. Instead, these matters are appropriate for consideration during compliance proceedings. *Sure-Tan, Inc. v. NLRB*, 467 U.S. 883, 902 (1984) (holding that compliance proceedings provide the appropriate forum where the Board and employer will be able to offer concrete evidence as to the amount of back pay, if any, to which affected employees are entitled); *United States Dep't of Justice, Immigration and Naturalization Serv., Los Angeles, Cal.*, 59 F.L.R.A. 387, 389 (2003) (same with respect to restoration of leave); *Ark Las Vegas Restaurant Corp. v. NLRB*, 334 F.3d 99, 107 (D.C. Cir. 2003) (holding that whether employee

has already been made whole and thus not entitled to back pay is best left to compliance proceedings). This principle clearly applies here as well. A definitive answer to the question of which employees, if any, actually lost pay because of the withdrawal of WIGIs can not be ascertained until the agency searches its records and makes the appropriate calculations.

For all these reasons, the Authority's remedy is appropriate and in accord with the Back Pay Act.

CONCLUSION

The petition for review should be denied and the Authority's order should be enforced.

Respectfully submitted,

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