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Orrick's *Global Employment Law Financial Services Industry Ticker* is the only publication dedicated to keeping in-house counsel and senior human resources executives informed on the most important employment law developments and trends in the financial services industry.

In this Issue:

TRENDS IN THE FINANCIAL SERVICES INDUSTRY

Orrick's Comprehensive Study of FINRA Arbitration Decisions in Employment Cases: Lessons Learned

With a large group of potential arbitrators who possess disparate skill sets and levels of experience, few detailed and reasoned decisions, and no clear binding precedents, arbitration proceedings before the Financial Industry Regulatory Authority ("FINRA") can be very unpredictable for employers. To assist employers better analyze and assess their risks and potential liabilities when faced with a FINRA arbitration, Orrick's Employment Law Group is working on a comprehensive study of all employment decisions issued by FINRA within the past two years.

Orrick is analyzing, among other things, the types of claims that are being filed, how frequently claimants are successful on their claims, how much claimants are recovering as compared to their demand for damages, how the forum fees are allocated, and which arbitrators are presiding over the matters. While the final results of Orrick's study and analysis will be available upon request at a later date, set forth below is a summary of some of our preliminary findings. Please contact Mike Delikat (mdelikat@orrick.com), Jill Rosenberg (jrose@orrick.com), Jim McQuade (jmcquade@orrick.com), or Lisa Lupion (llupion@orrick.com) if you would like to receive a briefing on the final report.

A large number of the employment cases decided by FINRA arbitrators over the past two years can be categorized as bonus disputes or other compensation disputes. Indeed, more than 35% of the FINRA decisions issued in the employment context have resolved bonus and/or compensation disputes. Of the decisions rendered in this category, claimants recovered at least a partial monetary award in more than 60% of the cases decided.

Despite this high percentage, there is some good news for employers. Our analysis suggests that claimants are more likely to recover on their compensation claims when the damages sought are under $250,000 than when claimants seek a larger award. It also appears that claimants are far more successful on their compensation claims when they seek to recover under a specific compensation or commission plan, as opposed to seeking to recover a performance bonus or other monetary award not governed by such a plan.

Our preliminary analyses also has revealed that claimants continue to file a large number of discrimination claims and other wrongful termination claims and that respondents have had significant success in defending such claims. In fact, our preliminary analysis reveals that respondents have avoided liability in more than 70% of the discrimination claims and almost 60% of the wrongful termination claims decided within the past two years.

Our preliminary findings also suggest that it is reasonable, and, in fact, prudent, for financial services firms to ask FINRA panels to assess the majority of the forum fees against the claimant, particularly if the claims are frivolous. While in the majority of cases forum fees continue to be split evenly between the claimant and respondent, panels in wrongful termination, discrimination, and bonus/compensation cases have assessed the majority of the forum fees against claimants in several recent cases.

CASES IMPACTING THE FINANCIAL SERVICES INDUSTRY

Orrick Actively Defending Class Actions Challenging Financial Services Firms' Employee Trading Policies

Financial services firms have a long-standing practice of requiring their employees who have brokerage accounts to hold those accounts with their firm. This practice has long been justified by a firm's obligations under federal securities laws to prevent insider trading and to properly supervise their employees.

Within the last year, several firms have found themselves defending this long-standing practice in different class action lawsuits filed in California. The plaintiffs in these lawsuits allege that the commissions and fees that full-service firms charge are grossly disproportionate to those charged at discount brokerages, and therefore, full-service firms profit by compelling their employees to keep their brokerage accounts with them, in contravention of California law, which prohibits employers from coercing their employees to patronize them. *See* Cal. Lab. Code § 450(a).

At least one of these class action complaints handled by Orrick has been dismissed under the Securities Litigation Uniform Standards Act of 1998 (the "SLUSA"). *See Hanson v. Morgan Stanley Smith Barney LLC*, 2:10-cv-06945, 2011 WL 311011 (C.D. Cal. Jan. 18, 2011). Congress had enacted the SLUSA after plaintiffs' attorneys began to bring securities lawsuits under the guise of state law claims in order to avoid the heightened pleading requirements and limited damages provisions set forth in the Private Securities Litigation Reform Act. SLUSA precludes any state law action that alleges a misrepresentation or manipulative and deceptive conduct in connection with the purchase or sales of securities.

In *Hanson*, the court found that SLUSA precluded plaintiffs' California claims, which challenged the firm's requirement that its employees maintain their brokerage accounts with that firm, as well as the firm's practice of charging employees' postage and handling fees in their brokerage accounts, even though many employees received their statements electronically. The court found that the plaintiffs' allegations fit the required alleged conduct under SLUSA because the plaintiffs accused the firm of misrepresenting its obligations under federal securities laws, and of misrepresenting the rationale for its postage and handling charges (and such allegations would be by nature manipulative and deceptive as well). The court further found that the alleged false justification for defendant's policy and the alleged false pretense of defendant's postage and handling fees were "in connection with" the purchase of securities, as defined under SLUSA, because the policies coincided with and were directly related to the purchase of securities.

In a related case, *Bloemendaal v. Morgan Stanley Smith Barney LLC*, No. 5:10-cv-01455 (C.D. Cal.), the defendant has moved for summary judgment on the California claims arguing that federal securities laws preempt California labor law prohibiting compelled patronage. The motion argues that because federal securities laws mandate that firms monitor employees' brokerage activities and maintain procedures that firms determine to be reasonably designed to prevent, detect, and investigate potential securities violations by employees, such laws conflict with (and therefore preempt) California law prohibiting compelled patronage. Briefing is complete, and the parties expect a decision within the next few months.

SOX Whistleblower Claims Affecting Financial Services Employers

Over the past year, employees in the financial services industry have continued to file a large number of Sarbanes-Oxley Act ("SOX") whistleblower claims against their employers. There also has been a number of significant decisions involving financial services firms over the past year involving SOX whistleblower claims, and employees have been experiencing some success with these claims both before the Department of Labor ("DOL") and before Federal District Courts. Several of these recent decisions are highlighted below.

Court Holds that the Dodd-Frank Act's Pre-Dispute Arbitration Ban In SOX Whistleblower Cases Is Retroactive

In *Pezza v. Investors Capital Corporation*, --- F. Supp. 2d ---, 2011 WL 767982 (D. Mass. Mar. 1, 2001), the court rejected a financial services firm's motion to compel arbitration of a SOX whistleblower claim that arose before the passage of the Dodd-Frank Act.

Section 922 of the Dodd-Frank Act amended SOX to provide that "[n]o predispute arbitration agreement shall be valid or enforceable, if the agreement requires arbitration of a dispute arising under this section." Thus, it is clear that employers may not rely on pre-dispute arbitration agreements to compel arbitration of SOX claims arising after the Dodd-Frank Act's passage in July 2010. However, in *Pezza*, the district court held that this provision of the Dodd-Frank Act is retroactive and that employers may not compel arbitration even of those SOX claims brought before the Dodd-Frank Act was enacted. Although the court found that nothing in section 922 expressed a clear congressional intent to make it retroactive, it nevertheless held that section 922 is principally a "jurisdictional statute," as opposed to a statute that "affects contractual or property rights," and that it could therefore be applied in suits arising before its enactment without raising typical concerns about retroactivity, such as impairing rights a party possessed when he acted, increasing a party's liability for past conduct, or imposing new duties with respect to transactions already completed. As a result, the court denied the motion to compel arbitration of Pezza's SOX whistleblower claims.

ALJ Finding of Merit

In *Stroupe v. Branch Banking & Trust Co*., 2008-SOX-47 (ALJ Apr. 1, 2010), a DOL Administrative Law Judge ("ALJ") found the complainant's SOX whistleblower claim to be meritorious and awarded her reinstatement, back pay, attorneys' fees, and other out of pocket losses.

Stroupe, a former police detective, was a corporate investigator for BB&T, whose job it was to investigate and report suspicious activities by bank employees or nonemployees. She alleged that she was terminated after investigating a series of suspicious loans BB&T had funded in what turned out to be a fraudulent real estate development scheme. Based on the information available at the time, the potential risk to BB&T of the loans was $20 million. As a result of Stroupe and BB&T reporting the issue to authorities, five co-conspirators in the scheme (none BB&T employees) ultimately pleaded guilty to mail fraud, wire fraud, bank fraud, and securities fraud.

Stroupe alleged that her employment was terminated 29 days after she met with bank officials to discuss the contents of her investigative report and whether the report should be provided to the FBI in a meeting scheduled for the next day. She also claimed that the manager in charge of the division she was investigating was displeased with her investigation, that he harbored animosity towards her as a result, and that his negative comments about her performance led to her termination.

BB&T argued that Stroupe had not engaged in protected activity because: (1) she was reporting in the course of her regular job duties; and (2) she had no "reasonable belief" of a fraud by BB&T because her investigation concluded that no BB&T employees were complicit in the fraud. BB&T also claimed that Stroupe was terminated not due to any protected activity but because she revealed details of her investigations to those without a "need to know," because she made negative comments about the manager in charge of the division she was investigating, and because she missed half a day of work without permission.

After a full evidentiary hearing, the ALJ concluded that reporting within normal job duties is protected under SOX, that Stroupe's report did not have to be about fraud by BB&T to be protected, but that even if it did, Stroupe had a reasonable belief that BB&T was aiding in the fraud being perpetrated by the real estate developer by funding four loans after becoming aware of the fraud. The ALJ also concluded that it was "virtually unfathomable that BB&T would fire an employee as highly regarded as Stroupe, and who had recently provided invaluable service to BB&T, over one or two essentially minor issues and without following its progressive disciplinary system." Accordingly, the ALJ found BB&T liable under SOX and awarded Stroupe reinstatement, back pay, attorneys' fees, and other out of pocket losses.

District Court Enforces Preliminary Reinstatement Order

In *Solis v. Tennessee Commerce Bancorp, Inc*., 713 F. Supp. 2d 701 (M.D. Tenn. 2010), the court held that: (1) it had jurisdiction to enforce a preliminary order of reinstatement of a former employee issued by OSHA after an investigation under SOX; (2) the DOL's procedures during the SOX investigation at issue complied with procedural due process requirements; and (3) the agency satisfied the traditional factors for an award of a temporary restraining order and preliminary injunctive relief. As a result, the court entered a temporary restraining order and preliminary injunction enforcing the DOL's preliminary order of reinstatement of the employee. A day later, the court denied the defendants' motion for a stay of the order, stating that the motion was "a challenge to the policy choice made by Congress" and that "Defendants cannot supplant this statutory mandate." 2010 U.S. Dist. LEXIS 49827 (May 20, 2010).

Five days later on appeal, the Sixth Circuit granted the stay, holding that the defendants' motion raised "a substantial question as to the authority of the district court to issue the preliminary injunction." The court found that the balancing of the harms weighed in the bank's favor as the immediate physical reinstatement of the employee would cause a disruption to the bank's personnel and operations that could not be undone if the court were to later find that the district court lacked authority to issue the injunction. 2010 U.S. Dist. LEXIS 15302 (May 25, 2010). The issue was never ultimately decided, as the employee subsequently withdrew his OSHA complaint. *See* 2010 U.S. Dist. LEXIS 114071 (Oct. 25, 2010).

This case is just the latest in which a plaintiff (here, the DOL) has encountered difficulties in enforcing preliminary reinstatement orders under SOX. *See, e.g., Welch v. Cardinal Bankshares Corp.*, 454 F. Supp. 2d 552 (W.D. Va. Oct. 5, 2006). The one prior court of appeals decision to address the issue was the Second Circuit decision in *Bechtel v. Competitive Technologies, Inc.*, 448 F.3d 469 (2d Cir. 2006), which denied enforcement of the preliminary reinstatement order in a plurality decision that did not provide definitive guidance on the issue. Thus, the enforceability of SOX preliminary reinstatement orders will remain an unsettled question of law until more courts weigh in on the issue.

Court Holds Reporting of Client Fraud Protected Under SOX

In *Sharkey v. J.P. Morgan Chase & Co*., 2011 WL 135026 (S.D.N.Y. Jan. 14, 2011), the plaintiff, a former Vice President and Wealth Manager in JPMC's Private Wealth Management division, claimed that her employment was terminated following her report to management that a new client that had been assigned to her was violating securities laws. Although the district court dismissed Sharkey's complaint for lack of specificity with leave to replead, it held that Sharkey properly pled that she engaged in protected conduct by reporting a client's illegal activity, determining that "[t]he statute by its terms does not require that the fraudulent conduct or violation of federal securities law be committed directly by the employer that takes the retaliatory action."

Although not noted in the court's decision, prior ALJ decisions were mixed on the issue of whether reporting of a third party's fraud is protected under SOX. *Compare Adam v. Fannie Mae*, 2007-SOX-50 (ALJ Feb. 25, 2008) (report that respondent was victim of fraud by vendors not protected by SOX as complainant did not report any alleged illegal activity by respondent) *with Stroupe v. Branch Banking & Trust Co.*, 2008-SOX-47 (ALJ Apr. 1, 2010) (report of fraud by respondent bank's loan recipient protected).

SIFMA Files an *Amicus* Brief in *Dukes v. Wal-Mart*

On January 27, 2011, SIFMA, acting as *amicus curiae* and represented by Orrick's Employment Law Group, filed an *amicus* brief with the United States Supreme Court in *Dukes v. Wal-Mart*. *Dukes* is the largest employment class action in history, and it threatens to pose substantial risks to employers in various industries, including the financial sector. Perhaps this is why the U.S. Chamber of Commerce has described *Dukes* as the "800-pound gorilla" of the Court's 2010-11 docket. The Supreme Court granted review of *Dukes* in December 2010, with argument scheduled for March 29, 2011.

In *Dukes*, the plaintiffs seek to represent a nationwide class of an estimated 1.5 million women across approximately 3,400 Wal-Mart stores. The United States District Court for the Northern District of California granted class certification in the case in 2004. It based its holding on the plaintiffs' theory that Wal-Mart fosters company-wide gender discrimination by giving store managers too much discretion to make pay and promotion decisions based upon subjective criteria. The plaintiffs bridged the gap between the subjective decision making and alleged discrimination by presenting four basic categories of evidence: (1) statistics aggregated at the regional and national level which they argue show statistically-relevant disparities; (2) testimony of a sociologist who asserts that Wal-Mart is "vulnerable" to gender bias (but could not say whether it affects 0.5% or 95% of all decisions); (3) anecdotes of 112 current and former Wal-Mart employees (*i.e*., less than 0.01% of the putative class); and (4) evidence of a uniform corporate culture (without regard to whether the culture is animus-neutral or actually opposed discrimination). The court noted that "[c]ourts have long recognized that the deliberate and routine use of excessive subjectivity is an 'employment practice' that is susceptible to being infected by discriminatory animus."

In April 2010, a Ninth Circuit en banc panel upheld the certification ruling, noting that "mere size does not make a case unmanageable." The dissenting opinion captured the stakes for all employers: "The door is now open to Title VII lawsuits targeting national and international companies, regardless of size and diversity, based on nothing more than general and conclusory allegations, a handful of anecdotes, and statistical disparities that bear little relation to the alleged discriminatory decisions."

While numerous parties have challenged the *Dukes* decision on multiple levels, the SIFMA *amicus* brief focuses on the potential impact to the financial services industry of finding commonality based on an employer's alleged use of "excessive subjectivity."

Although most financial services jobs are subject to various objective criteria, such as revenue generation statistics, other crucial qualities and characteristics that defy quantification often are as important as, or even outweigh, such objective factors. Investment bankers, personal bankers, loan officers, financial advisors, traders, and investment advisors all interact with public investors and/or corporate clients. Employees in those diverse jobs typically need a sophisticated and ever-changing skill set, not subject to ready evaluation by purely objective factors, to properly perform their jobs. Punishing employers for applying such nonquantitative criteria could be potentially hobbling for many employers in this sector.

There is nothing inherently unlawful in applying some subjective criteria to personnel decisions. Almost three decades ago, in *General Telephone Co. v. Falcon*, 457 U.S. 147 (1982), the Supreme Court noted that an employer cannot be subjected to class certification just because it applies some level of subjective criteria. The focus of the analysis must be on an identifiable discriminatory purpose, not the mere application of nonquantitative or subjective factors. Despite this guidance, the Ninth Circuit significantly lowered the burden of proof at the certification stage and undermined the exercise of discretionary, nondiscriminatory decision making. The Ninth Circuit decision allows plaintiffs to file broad class actions for plaintiffs in multiple facilities and geographic locations who are managed by different decision makers based on little to no evidence of a general company policy to discriminate. The resulting fear of broad class-wide liability based on so-called subjective factors is likely to inhibit employers from making essential, job-related discretionary assessments of employee performance and potential. This would arguably create a disincentive to the financial services industry in fulfilling its regulatory and compliance responsibilities in overseeing its workforce.

The *Dukes* case has naturally spurred tremendous interest among the plaintiffs' class action bar. A number of new high profile class action cases alleging gender discrimination in pay and promotion have been filed against major financial services firms, and many others are being threatened. These developments, coupled with the risk that the Supreme Court could affirm *Dukes*, highlight the importance for employers to be proactive in detecting and resolving discriminatory employment practices.

New York Court Finds Class Action Waiver Provision Unenforceable

Many financial services firms include class action waiver provisions in their employee arbitration agreements, and those provisions have been effective in cutting off class and collective action wage and hour claims in many states. New York state and federal courts generally have held these class action waiver provisions to be valid and enforceable. However, a federal judge in the Southern District of New York just recently issued an opinion invalidating a class action waiver in an employee arbitration provision.

In *Sutherland v. Ernst & Young LLP*, No. 10 Civ. 3332, 2011 WL 838900 (S.D.N.Y. March 3, 2011), a "low level" accountant filed a class action alleging that Ernst and Young misclassified her and others similarly situated as exempt from overtime requirements under the Fair Labor Standards Act and New York state laws. Ernst & Young moved to dismiss or to stay the proceedings, and to compel arbitration of the plaintiff's claims on an individual basis in accordance with the class action waiver provision in its arbitration agreement.

Relying on *In re American Express Merchants' Litigation*, 554 F.3d 300 (2d. Cir. 2009), *aff'd*, 2011 WL 781698 (2d Cir. Mar. 8, 2011), the court held that the class action waiver is invalid because, under the totality of the circumstances, it prevents the plaintiff from vindicating her statutory rights. As a result, Ernst & Young would receive de facto immunity from liability for alleged violations of the labor laws. The court concluded that the plaintiff could not reasonably prosecute her claims on an individual basis because the expense of prosecution would dwarf her potential recovery (approximately $1,867 in overtime compensation) and she would be unable to retain an attorney to pursue her individual claim.

Although the court invalidated Ernst & Young's class action waiver, it concluded that it could not order Ernst & Young to submit to class arbitration because, under *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.*, 130 S.Ct. 1768 (2010), class arbitration may not be imposed on parties whose arbitration agreements are silent on the permissibility of class proceedings.

REGULATORY ROUNDUP

The Dodd-Frank Act SEC Whistleblower Program

The Dodd-Frank Act, enacted on July 21, 2010, provides powerful monetary incentives for whistleblowers to report securities law violations to the SEC and strong protections for doing so. The legislation provides that whistleblowers who provide the SEC with original information about violations of securities laws shall be awarded a share of between 10% and 30% of monetary sanctions ultimately imposed by the SEC that exceed $1 million.

The Dodd-Frank Act requires the SEC to establish a separate office within the Commission to administer and enforce the Act's whistleblower provisions. On February 18, 2011, the SEC named Sean McKessy, former Senior Counsel in the Division of Enforcement, as head of the new Whistleblower Office. It is unclear how soon the new office will get up and running, as prior to this announcement, the SEC had stated that, due to budgetary constraints, it would not be able to establish the office, but would instead handle Dodd-Frank whistleblower reports through its existing enforcement staff.

In the meantime, however, tips have been pouring in, and the SEC estimates that it will receive 30,000 Dodd-Frank whistleblower tips a year, and that half of those, or 15,000, will result in formal monetary claims by whistleblowers. The agency expects the first monetary awards to whistleblowers under the new program to be made in late 2011. We expect that many of these claims will be filed by employees working in the financial services industry.

SEC's Proposed Regulations

The SEC is required under the Dodd-Frank Act to issue final regulations implementing the Act's whistleblower provisions within 270 days (i.e., by April 17, 2011). The agency issued proposed regulations on November 3, 2010, with a comment period that was supposed to end on December 17, 2010. It appears that the SEC is still continuing to accept comments on its website past that deadline.

The proposed regulations clarify that whistleblowers will only be eligible for awards under the whistleblower program if they: (1) "voluntarily" provide information to the agency, that is, before a request is made by the government; (2) the information is "original," based on the individual's independent knowledge or analysis; and (3) the information leads to a successful enforcement action with a recovery of over $1 million.

There are several categories of individuals who would not be eligible for an award under the proposed regulations:

- Those with a pre-existing legal or contractual duty to report the information
- Attorneys who attempt to use information obtained from a client engagement to make whistleblower claims for themselves (unless disclosure is permitted by SEC or state bar rules)
- Independent public accountants who obtain information through a client audit
- Individuals who learn the information by violating federal or state criminal laws
- Individuals who learn the information from ineligible individuals
- People criminally convicted in connection with the conduct
- People who knowingly and willfully make misrepresentations in a whistleblower report or in subsequent dealings with the SEC or other authorities
- Foreign government officials
- Employees of certain agencies
- Internal compliance or management employees who are told about violations with the expectation that they will take appropriate steps to respond to the violations (and people they inform/question in the course of attempting to respond)

With regard to this last category, it is important to recognize that these compliance and management personnel (and others whom they may inform of the issue in the course of addressing it) can become eligible for an award under two circumstances: first, if the company does not disclose information that is required to be disclosed to the SEC within a “reasonable time”; and second, if the company acts in “bad faith.” The proposed regulations do not define “reasonable time” or “bad faith.” The SEC’s comments to the regulations suggest that a “reasonable time” is necessarily a “flexible concept” and must be determined on a case by case basis, and that “bad faith” might include hindering the company’s investigation or interfering with the preservation of evidence.

Even if an employee is ultimately not eligible for a whistleblower bounty under the SEC program, the employee remains covered by the Dodd-Frank Act’s anti-retaliation provisions, which provide for broad remedies for retaliation against whistleblowers who make reports to the SEC, including reinstatement, double-back-pay, and attorneys’ fees.

Recognizing that the Dodd-Frank Act’s bounty provisions provide a huge incentive for employees to immediately go to the SEC with concerns prior to reporting issues internally to their employers, the SEC’s proposed regulations attempt to counteract that with a 90-day look-back period. That is, an employee may report issues to the company first, and have the date of that internal report count as the operative date of providing original information as long as the employee then provides the information to the SEC within 90 days of the internal report. In addition, the proposed regulations state that the SEC may (but is not required to) consider higher awards for individuals who report issues internally prior to going to the agency.

As a practical matter, it is unlikely that merely permitting internal reporting will be sufficient to prevent employees from approaching the SEC directly with reports of actual or potential violations, given the massive incentives for whistleblowers to be the first in line to provide “original information.” Thus, unless the SEC adopts the approach suggested by many corporations and management-side attorneys, who, in their comments to the proposed regulations, urged the SEC to require internal reporting first, we can expect to see a dramatic rise in external whistleblowing by employees in search of six or seven-figure bounties.

Next Steps for Employers

In light of the strong monetary incentives provided to employees to report violations to the SEC, employers would be well served to review their internal whistleblower procedures and policies as soon as possible to ensure that they require internal reporting and the maximum opportunity to address compliance and regulatory concerns internally before employees provide information to the SEC. In addition, employers should consider whether to require at least annual certifications by certain categories of employees that they are not aware of violations or, if they are, that they have already reported them to the company through an appropriate channel.

NEW STATUTES

Amendment to New York Wage Law Adds Significant Administrative Responsibilities for Financial Services Employers

Beginning on April 12, 2011, financial services firms must provide all of their New York employees with annual written notice of their wages, and employers must then retain written acknowledgment confirming receipt of this notice. For financial service employers, distributing, and, more significantly, collecting written acknowledgments from every New York employee each year will be a significant administrative burden.

The amendments to the New York Labor Law were passed under the Wage Theft Prevention Act, which New York Governor Paterson signed into effect on December 13, 2010. Expanding on New York Law Section 195’s requirement to provide written wage notice to all newly hired employees, the statute now requires employers to provide all newly hired employees at the time of their hire and by February 1 of every year thereafter with written notice of their regular rate of pay, regular pay day, overtime rate of pay (if overtime eligible), basis of pay (e.g., whether the employee will be paid by the shift, hour, day, week, salary, piece, commission, or by another basis), any allowances (like tips) claimed as part of the minimum wage, the employer's main address and phone number and any other information that the commissioner of labor deems material and necessary. Employers must provide this notice in both English and the employee's primary language (if other than English). The New York Department of Labor will be, but has not yet, issued template notices that comply with these requirements, including a non-English version of the notice. If an employee identifies a primary language for which a template is not available, the employer will be allowed to provide an English-language notice.

Critically, employers must obtain from the employee a signed and dated written acknowledgment confirming receipt of this notice, which must be retained for six years. While there is no guidance from the New York Department of Labor, the "signed and dated written acknowledgment" language in the text of the statute suggests that electronic acceptance of this mandatory notice will not satisfy the statutory requirements.

Failing to provide a newly-hired employee the required wage notice can result in damages of $50 for each workweek during which the violation occurred, but not to exceed $2,500. The New York Department of Labor can also obtain $50 per week if an employer fails to provide all appropriate wage notices now required under Section 195.

In addition to the notice and recordkeeping amendments, New York Wage Theft Prevention Act also expands the information that employers must provide to employees on their pay stubs, increases the time that employers must maintain payroll records from three to six years, and increases liquidated damages from 25% to 100% of any unpaid wages.

CROSS-BORDER DEVELOPMENTS

Post-Employment Restrictive Covenants: Cross-Border Disputes

Financial services firms with employees located in various states and countries often experience significant difficulty implementing and enforcing uniform post-employment restrictive covenants across employee populations. Given the significant differences in the laws governing restrictive covenants in various jurisdictions, choice of law and choice of forum issues often become the most critical issues in cross-border restrictive covenant disputes. For example, California and New York courts often reach completely differently decisions based on the same set of facts. It is common for an employer to file a lawsuit in one forum to enforce a restrictive covenant, while the former employee files a parallel declaratory judgment action in another forum seeking to have the restrictive covenant declared unenforceable.

A recent decision by a New York court in *Marsh USA Inc. v. Hamby et al.*, 2010 N.Y. Misc. LEXIS 3439 (N.Y. Sup. Ct. July 22, 2010) provides an excellent example of such a cross-border dispute involving New York and California, and provides some hope for New York-based financial services seeking to enforce post-employment restrictive covenants against employees located in California. In Marsh, the plaintiff Marsh USA Inc. ("Marsh") brought an action in New York State Supreme Court against one of its competitors, Dewitt Stern Group, Inc. ("Dewitt"), and two of its former employees who had joined Dewitt, alleging that the former employees had breached their noncompetition agreements and that Dewitt and the two former employees had misappropriated trade secrets. At all relevant times the two former Marsh employees had worked for Marsh in California, had resided in California, and went to work for Dewitt in California. However, the noncompetition agreements had New York choice of law and venue provisions.

Dewitt and the two employees filed a declaratory judgment action in California state court, arguing that California law should apply to the agreements and that the noncompetition agreements were unenforceable under California law. The California court rejected this argument and granted Marsh's motion to quash and stay the California action, allowing the action to proceed in New York. Meanwhile, the New York court denied Dewitt's motion to dismiss on *forum non conveniens* grounds, and held that the New York choice of law and venue provisions were enforceable because: (1) both Marsh and Dewitt had a global presence and maintained their principal places of business in New York; and (2) the two former employees were sophisticated individuals who were compensated for signing the noncompetition agreements. This decision demonstrates that, in a cross-border dispute, choice of law, conflict of law, and choice of forum provisions may be some of the most critical provisions of an agreement and should be carefully considered by employers when implementing such agreements.

The New FSA Code on Remuneration Comes into Effect in the UK

On January 1, 2011, the Financial Services Authority ("FSA") Remuneration Code (the "Code") came into force in the UK. The Code sets out rules and associated guidance regarding remuneration within a wide variety of organizations. In July 2010, the European Union agreed to amendments to the Capital Requirements Directive 2006/48-9/EC ("CRD 3"). CRD 3 requires Member States to introduce stricter controls on remuneration for specified employees and "risk takers" within specified credit institutions and investment firms from January 1, 2011.

As a result of CRD 3, the provisions set out in the Financial Services Act 2010 ("FS Act") and the Principles for Sound Compensation Practices (as published by the Financial Stability Board), the FSA have revised and expanded the previous Remuneration Code and have published this revised Code which came into force on January 1, 2011.

According to the FSA, the Code now applies to over 2,500 FSA-authorized firms. It covers 12 core principles including governance, performance management and composition of remuneration committees. In publishing the Code, the FSA has recognized that remuneration policies, practices and procedures were a contributory factor in the recent financial crisis, but were not the dominant factor.

Which Institutions Are Covered by the Code?

The Code, as required by CRD 3, will apply to all banks, building societies and firms which are subject to the provisions of the Capital Adequacy Directive ("CAD"). This includes most hedge fund managers, all UCITS firms, plus some firms which engage in corporate finance, venture capital, the provision of financial advice, brokers, several multilateral trading facilities and others.

The Code also applies to the UK branches of firms whose home states are outside the EEA. Interestingly, the Code will not apply to UK branches of firms whose home states are within an EU Member State, as the firm's own home state should have implemented the provisions of CRD 3 accordingly.

Which Individuals Are Covered?

Technically, all employees of a firm which is subject to the Code are covered, as the firm is required to ensure that its remuneration policies and procedures provide for effective risk management. However, the Code will primarily affect two categories of employee:

1. Code Staff (a concept introduced by the Code for the first time); and
2. Employees engaged in control functions.

Code Staff are those employees who perform a significant influence function for the firm. This includes senior managers, all staff whose total remuneration takes them into the same bracket as senior management and risk takers whose professional activities have a material impact on the firm's risk profile.

The Code contains a non-exhaustive list of the key positions which it considers to fall within the definition of 'risk takers.' Examples include: Heads of business lines including commodities, equities, structured finance, and fixed income. The FSA also expects firms to compile a list of Code Staff ahead of the bonus allocation period, so that firms can notify staff who may be potentially subject to the Code's rules.

It is important to note that where a member of staff is classified as Code Staff for part of a performance year, the firm should treat that member of staff as Code Staff for the entirety of that year.

Individuals who earn less than £500,000 ***and*** who receive variable remuneration which is not more than 33% of their total remuneration are generally considered by the FSA to fall outside the Code Staff definition for certain purposes such as deferral and performance adjustment, guaranteed bonuses and the 50% rule regarding variable remuneration. This is called the *de minimis* threshold. Accordingly, if a member of Code Staff ***either*** receives variable remuneration amounting to more than 33% of their total remuneration ***or*** their total remuneration is more than £500,000, they will not satisfy the *de minimis* threshold and will be caught by the full Code Staff requirements.

The FSA have indicated that staff who fall below the *de minimis* threshold may still be categorized as Code Staff. As the Committee of European Banking Supervisors ("CEBS") guidelines state, firms should be aware of cases where staff do not receive a high level of remuneration, but still have a material impact on the firm's risk profile on account of their particular job function or responsibilities. CEBS cautions firms against categorically dismissing low earners as non risk takers.

Consultants and other individuals who provide services to a firm may also be classified as Code Staff despite not being direct employees. It is for this reason that firms should consider whether any consultants or special advisers should be identified as Code Staff, for example, because their remuneration is equivalent to the levels of remuneration paid to senior management, or because their roles could materially impact the firm's risk profile.

What Are the Remuneration Requirements?

Many of the evidential provisions and guidance under the previous remuneration code have been replaced by new rules in the Code. Therefore, firms need to ensure that they review the Code thoroughly, including those firms which were already subject to the Code.

The requirements and principles set out in the Code build on those contained in the previous code. The central tenet of the Code remains the general requirement that firms' remuneration policies must be consistent with and promote effective risk management and not expose them to excessive risk.

Firms need to establish whether, for each member of Code Staff, there is a suitable balance between the employee's fixed pay and variable compensation. Firms should set a maximum ratio of variable to fixed pay for different categories of Code Staff.

Subject to proportionality for Code Staff whose remuneration exceeds the *de minimis* threshold, firms need to take steps to ensure that:

- At least 40% of variable remuneration paid to Code Staff is deferred over at least three to five years, with awards vesting no faster than on a pro-rata basis (and the first vesting no earlier than one year after the award). Where the amount of variable remuneration is particularly high (generally £500,000), at least 60% should be deferred.

- At least 50% of variable remuneration (whether paid upfront or deferred) is paid in a non-cash form, specifically in an appropriate balance of non-cash instruments, that is:

  - Share (or equivalent ownership interests, for non-corporate firms), share-linked instruments or equivalent non-cash instruments (that is, rights that will deliver value at some point in the future, based on the value at that time of a specified ownership interest, such as phantom share options or share appreciation rights); and

  - (at least for some firms) bonds which are convertible into equity if regulatory capital needs to be increased.

- Measures are in place that allow the firm to adjust awarded but unvested variable remuneration, in particular where there is evidence of employee misbehavior or material error, or the firm suffers a material financial downturn or there is a material failure in risk management.

- Guaranteed bonuses are only paid in exceptional circumstances in the context of hiring new staff and are limited to an employee's first year of employment.

Firms should also evaluate their current remuneration structures to assess whether there is anything that could encourage Code Staff to take risks in order to maximize the amount of variable compensation being paid to them.

Application

Any new contractual term that contravenes the prohibition on guaranteed bonuses or the rules on deferral will be void and the firm must take reasonable steps to recover any payment made under it ("voiding and recovery"). Whilst this rule is extremely onerous, it only applies to contracts of employment concluded after the new Code came into effect, or to contracts of employment subsequently amended so as to contravene the Code. In addition, the FSA is adopting what it calls a "proportionate approach" to the implementation of the Code in relation to voiding and recovery, according to the size and nature of the firm - with less onerous standards applying to the lower tier firms and the strictest standards applying to those firms which were already subject to the previous Code. For the lower tier firm at least, the rules on voiding and recovery will not apply until January 2012.

All other provisions of the Code apply to remuneration awarded or paid after January 1, 2011, even if it is due under a contract of employment entered into before that date. Therefore the FSA is expecting firms to review all contracts of employment for Code Staff and take reasonable steps to amend them to ensure they comply with the Code. In making such contractual amendments, firms need to be aware that without an express power to amend or without employee consent, this could give rise to significant breach of contract claims. We are yet to see any litigation in this regard but when it comes (which it will), it will be interesting to see how the Courts balance the public policy requirements of the Code against individual contractual rights.

Employment Litigation in Japan Is Expected to Expand

Employment litigation in Japan has continued to expand greatly over the past five years, mainly due to the economic recession and the introduction of labor tribunals in April 2006. The number of labor tribunal cases has been continuing to increase, reaching almost 3,500 cases in 2009.

Labor tribunal cases have been booming in Japan due largely to the popularity of its faster average processing time (2.5 months), as opposed to the 12.3 month processing time for full merits trials. In addition, labor tribunal cases have become extreme popular because they offer more flexibility to the parties, as the labor tribunals have more flexibility in deciding their cases. For example, in cases of unlawful dismissal, labor tribunals often award severance payments, whereas decisions at full merits trials always result in reinstatement.

In only ten percent of the labor tribunal cases, opposition proceedings are filed against decisions and moved to full merits trials. Thus, ninety percent of the cases are concluded in labor tribunals. However, this does not mean that full merits trials are decreasing; rather they are remaining static at the core of litigation. The vast majority of subject matters handled in labor tribunal cases are related to dismissals, making up fifty percent of all cases, followed by cases concerning unpaid wages, including overtime payment and compensation of employees such as retirement allowances, which comprise thirty-seven percent of all cases.

We expect that in the coming years there will be a major shift in litigation in Japan from overpaid interest litigation between individuals and financial services firms, which accounted for fifty percent of all cases in district courts in Japan in 2008, to unpaid overtime litigation. Due to a recent change in Japanese law, this overpaid interest litigation is expected to end soon. There are many lawyers in Japan who specialize in representing individuals in overpaid interest litigation, because these cases have been profitable and are fairly straightforward for lawyers. As result of this, the vast majority of those "business" lawyers are expected to migrate to unpaid overtime litigation, which is considered to be quite similar in structure for lawyers representing individuals. Assuming that those "business" lawyers are to encourage employees and ex-employees to sue their employers for unpaid overtime wages, the number of unpaid overtime litigation will increase drastically in the near future.

In conclusion, due to the increase of employment litigation in Japan, careful consideration of employment agreements and work rules together with appropriate payment of overtime wages would help reduce the risk of contentious employment matters in Japan

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