

## OUTSIDE COUNSEL

BY HOWARD S. MEYERS

### *Recovering Unpaid Bonus Payments in Turbulent Times*

In light of the most recent layoffs affecting securities industry professionals on Wall Street, the question often arises as to whether such individuals are entitled to receive any bonus payments earned prior to their termination, even when they are employed “at will” and are not present on the date the bonus was intended to be paid.

This article will examine those circumstances where former employees have been successful in asserting claims for unpaid bonus payments subsequent to their termination. In addition, because an overwhelming number of disputes between securities industry professionals and their former firms are subject to mandatory arbitration, this article will examine various arbitration awards in this area as well.

#### **‘Discretionary’ Compensation**

Although, as a general rule, an employee has no enforceable right to receive bonus compensation if such compensation is “discretionary,”<sup>1</sup> the Appellate Division, First Department, recognized in *Weiner v. Deibold Group Inc.*, 568 NYS2d 959, 961 (1st Dept. 1991) that New York State has a “long-standing policy against the forfeiture of earned wages.” Accordingly, the issue of whether a bonus is merely “discretionary,” which does not have to be paid by the employer to the terminated employee, or “earned wages” not subject to forfeiture, is an issue of fact. See *Mirchel v. RMJ Securities Corp.*, 205 AD2d 388, 389, 613 NYS2d 876, 878 (1st Dept. 1994). Critical to this analysis is whether such a bonus constitutes “an integral part of the employee’s compensation package.” *Id.*

New York courts have recognized that, “[w]hen a bonus that is an integral part of a compensation package has already been earned by the time the employer decides not to pay it, the latter can no longer argue that such bonus is discretionary.” See *Sipkin v. Major League Baseball Advance Media*, 808 NYS2d



920 (1st Dept. 2005) citing *Harden v. Warner Amex Cable Communications*, 642 FSupp 1080, 1096, (S.D.N.Y. 1986). At that point, failure to pay the bonus constitutes a breach of the employment agreement. *Guggenheimer v. Bernstein Litowitz Berger & Grossmann LLP*, 810 NYS2d 880, 886 (N.Y. Sup. Ct., N.Y. County 2006). In addition, the fact that the precise amount of the bonus to be awarded was not specified does not make the agreement unenforceable. *Id.* Nor is a claim for an unpaid bonus barred by the fact that an individual was an “at will” employee. See *Sipkin v. Major League Baseball Advance Media*, 808 NYS2d 920; *Deutsche Bank Securities Inc. v. Kong*, No. 110536/06, 2008 N.Y. Misc. LEXIS 2408, at \*6 (N.Y. Sup. Ct., N.Y. County, April. 18, 2008).

On Wall Street, the compensation packages of many senior level securities industry professionals are comprised of both salary and bonus. Indeed, bonuses on Wall Street are an expected part of a senior employee’s total compensation and are often viewed as essential to maintaining a securities firm’s franchise and employees. The fact that this compensation obligation is usually paid at year-end, or within the first quarter of the following year, does not diminish its level of importance.

#### **Compensation Structure**

Where an employer creates a compensation structure that pays an employee a small portion of his annual compensation as a base salary during the year, but has traditionally paid the balance of the employee’s annual compensation as a so-

called “bonus,” the “bonus” may, in reality, be considered an integral part of the employees’ overall annual compensation.

For example, in *Mirchel v. RMJ Securities Corp.*, 613 NYS2d 876 (1st Dept. 1994), the plaintiff was employed by defendant RMJ as a government securities broker for nearly five years. Plaintiff alleged that prior to commencing his employment with RMJ the company’s president offered him a compensation package that included, among other things, a “base salary” and an “annual bonus” — “described as ‘substantial’ in proportion to the base salary.” *Id.* at 877. Consistent with such allegations, the court found that “throughout the term of his employment, plaintiff’s compensation included a substantial bonus....” *Id.* Following the plaintiff’s resignation from RMJ on Jan. 20, 1987 and the company’s failure and refusal to pay plaintiff his 1986 bonus, plaintiff commenced an action on several legal grounds, including breach of an implied contract and quantum meruit. RMJ moved for summary judgment dismissing plaintiff’s complaint, claiming “that its policy had always been to make bonus payments at its discretion, and then only if the employee continues to work for the company; that the employee bonus is paid as an inducement to continued satisfactory employment; and that in accordance with this policy, defendant will not make a bonus payment to a former employee.” *Id.* at 878.

In rejecting RMJ’s contention and sustaining the plaintiff’s claim, the Appellate Division, First Department stated:

Similarly, an implied contractual relationship may be established by conduct of the parties, as well as by express agreement. The course of dealing between the parties evinces an implied promise that annual or semiannual bonus payments constitute a part of plaintiff’s compensation. That the amount of each annual bonus was determined at the end of the year does not bar recovery under an implied contract. Nor can a bonus be withheld because, as here, the employee did not work until the date the bonus was to have been paid.

*Id.* at 878 (citations omitted); accord, *Radio*

**Howard S. Meyers** is a partner at Meyers & Heim and a visiting professor of law at New York Law School and associate director of that school’s Center on Business Law & Policy.

*Today Inc. v. Westwood One Inc.*, 684 F.Supp. 68, 71 (S.D.N.Y. 1988) (under New York Law, implied contracts are “based on the conduct of the parties, from which a fact finder may fairly infer the existence and terms of a contract”); see also *Deutsche Bank Securities Inc. v. Kong*, No. 110536/06, 2008 N.Y. Misc. LEXIS 2408, at \*6 (“[p]arties’ course of conduct [is] sufficient to support a cause of action for a bonus for past year’s work based on an ‘implied promise’ that annual bonus payments constituted an integral part of [investment banker’s] compensation”).

### ‘Express’ Promises

Similarly, in *Giuntoli v. Garvin Guybutler Corp.*, 726 F.Supp. 494 (S.D.N.Y. 1989), the U.S. District Court for the Southern District of New York also found a former employee to state a contract claim for wrongful denial of bonus payments. There, plaintiff alleged that her employer had breached an oral employment agreement by refusing, among other things, to pay her bonus. *Id.* at 507. The employer argued that the plaintiff had not sufficiently alleged that the employer had made an “express promise with respect to bonus compensation.” *Id.* Based on plaintiff’s allegations, inter alia, that upon commencing employment, she had been promised a semi-annual bonus based on profitability and the “course of dealing between the parties” demonstrated her entitlement to a bonus, the court denied the employer’s motion to dismiss, holding that adequate evidence in fact existed that semi-annual “bonus payments constituted a term of plaintiff’s employment.” *Id.* at 507-08. The court noted “[b]onus history thus may be used to determine an appropriate bonus amount.” *Id.* at 508.

Even where the parties have agreed that the payment of a bonus is purely discretionary, an employer must act reasonably when refusing to pay such a bonus. Indeed, under New York law, every contract contains an implied covenant of good faith and fair dealing. See *Travellers International A.G. v. Trans World Airlines Inc.*, 41 F.3d 1570, 1575 (2d Cir. 1994). Even where a contract confers discretion on one of the parties, courts have recognized that such discretion is “subject to an obligation that it be exercised in good faith.” *Id.* See also, *Dalton v. Educational Testing Service*, 639 N.Y.S.2d 977, 979 (1995). Thus, courts have held that “where the contract contemplates the exercise of discretion, this pledge includes a provision not to act arbitrarily or irrationally in exercising that discretion.” *Id.*; *Tagare v. NYNEX Network Systems Co.*, 994 F.Supp. 149, 159 (S.D.N.Y. 1997).

For example, in *Rothman v. KPMG Peat Marwick & Co.*, Index No. 601756/98 (March 4, 1999) (N.Y. Sup. Ct., N.Y. County), Justice Carol F. Huff denied the defendant’s motion for summary judgment based upon the company’s claim that its payment of “bonuses” was purely discretionary. The court held that KPMG did not have blanket discretion to refuse to pay

the plaintiff an annual bonus even though the employment agreement between the parties stated that KPMG had such discretion. Instead, such discretion had to be employed taking into account the various criteria which the firm represented would be part of the compensation process.

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### Arbitration Panels

Arbitration panels have also found employees who have been terminated, are entitled to full or pro rata bonuses, rejecting claims by employers that year-end “bonuses” are purely discretionary or that an employee must be employed by the firm at year-end or when bonuses are ultimately distributed in order to be entitled to receipt of what is, in reality, earned wages.

For example, in *Halikias v. Warburg Dillon Read LLC f/k/a UBS Securities, LLC*, NYSE Arbitration No. 1998-007299 (Dec. 10, 1999), an arbitration panel awarded the claimant, a junior level trader for the firm, \$1,442,406, rejecting the firm’s defense that “bonuses” were discretionary. Moreover, in *Schwartz v. Warburg Dillon Read LLC f/k/a UBS Securities, LLC*, NYSE Arbitration No. 1998-007500 (June 19, 2000), an arbitration panel awarded the claimant \$2 million and \$144,000 in attorney’s fees, and in rendering its decision, the panel considered, inter alia, “industry custom and practice concerning compensation and the payment of so-called discretionary bonuses and the inherent obligation of fair dealing and good faith implicit in all such arrangements.”

See also, *Schuman v. CS First Boston Corp.*, NYSE Arbitration No. 1995-004808 (July 9, 1996) (Vice president and analyst/trader terminated as part of a reduction in force awarded \$147,000 in unpaid compensation, \$32,400 in attorney’s fees and \$2,415 in costs, with First Boston further ordered to bear all forum fees); *Kaul v. CS First Boston Corp.*, NYSE Arbitration

No. 1995-004815 (May 16, 1996) (Director and trader terminated as part of a reduction in force awarded \$225,000 bonus/severance pay); *Salomon Brothers v. Dumas*, NYSE Arbitration No. 1991-001250 (Aug. 12, 1992) (Managing director who resigned awarded \$902,000, which included \$700,000 bonus for four months services prior to his resignation); *Gordon v. Kidder Peabody & Co.*, NYSE Arbitration No. 1995-004635 (Dec. 6, 1995) (following closing down of the firm and his resulting termination, vice president in mortgage research awarded a \$300,000 bonus for 1994, which constituted a 40 percent increase in bonus amount offered to him by firm in his separation package, notwithstanding firm’s claim that it had a discretionary bonus policy and lost \$1.18 billion dollars in 1994); *Ehling v. Morgan Stanley & Co.*, NYSE Arbitration No. 1997-006273 (March 4, 1998) (arbitrators rejected firm’s claim that bonuses are purely discretionary and awarded salesperson \$180,000); and *Katz v. Adams Cohen Securities*, NASD Arbitration No. 94-04892 (Jan. 18, 1996) (two investment bankers who resigned in November 1993 to start own business awarded \$298,677, a clear rejection of firm’s claim that bonuses were purely discretionary and that employees in any event had to be employed on date of bonus distribution to then be eligible to receive payment).

### Conclusion

In evaluating whether a terminated employee is entitled to recover unpaid bonus payments from his prior employer, the practitioner should determine whether such a bonus was earned at the time of the employee’s termination and constituted an integral part of the employee’s compensation package. Furthermore, in conducting this analysis, the practitioner should examine, inter alia, industry custom and the course of dealing between the parties. In circumstances where the parties agreed that the payment of a bonus would be made at the employer’s discretion, the practitioner should determine whether such discretion was exercised in good faith. After careful analysis of these and other factors, can the practitioner properly advise his client as to whether he is entitled to receive unpaid bonus payments.

1. See *Namad v. Salomon Inc.*, 537 N.Y.S.2d 807 (1st Dept. 1989), aff’d 545 N.Y.S.2d 79 (1989).

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## MEYERS & HEIM LLP

HOWARD S. MEYERS  
ATTORNEY AT LAW  
CERTIFIED PUBLIC ACCOUNTANT

444 MADISON AVENUE, 30TH FLOOR • NEW YORK, NY 10022  
PHONE: 212.355.7188 • FAX: 212.355.7190  
EMAIL: HMEYERS@MEYERSANDHEIM.COM