

California Supreme Court Affirms Employer's Right to Offer Voluntary Equity Plan

November 5, 2009

In a decision strengthening the right of employers and employees to negotiate the terms of employees' compensation, the California Supreme Court in *Schachter v. Citigroup, Inc.*, No. S161385 (November 2, 2009), affirmed summary judgment against an employee who claimed that his incentive compensation plan violated the California Labor Code.

Citigroup offered a voluntary employee incentive compensation plan under which employees could elect to receive a percentage of their compensation in the form of shares of restricted company stock at a reduced price. During a two-year restriction period, the employee was granted the right to vote the shares of restricted stock and received dividends on the shares, though the restricted shares were not included in the employee's gross income for tax purposes. At the end of the two-year restriction period, title to the shares vested fully with the employee. If the employee's employment ended before the end of the two-year period, however, he or she forfeited the restricted stock.

In this case, the employee, financial consultant David B. Schachter, elected to participate in the plan and elected to receive a percentage of his compensation in the form of restricted stock. Schachter voluntarily terminated his employment with Citigroup prior to the vesting date of his restricted stock, thereby forfeiting his right to the stock. Schachter then filed a putative class action against Citigroup, alleging that the plan's forfeiture provision violated sections 201 and 202 of the California Labor Code, which require the prompt payment of all earned wages when an employee is terminated or resigns, as well as California Labor Code section 221, which prohibits an employer from returning wages to an employee. Schachter argued that he "diverted" cash compensation to purchase the restricted stock shares, and that this diverted cash constituted earned wages that should have been paid to him in cash upon his resignation. The trial court granted the employer's motion for summary judgment and the California Court of Appeal affirmed.

In affirming the court of appeal's decision, the California Supreme Court confirmed that "straight-time wages (above the minimum wage) are a matter of private contract between the employer and the employee." The court concluded that by agreeing to have a portion of his compensation paid in the form of restricted stock, Schachter "essentially renegotiated the terms of his compensation with the company" and accepted that the restricted stock would have "limited and conditional present value," vesting only if he remained an employee of the company for two years.

Contrary to Schachter's assertion that the restricted stock constituted "earned wages" that should have been paid to him in cash when his employment ended, the court held that Schachter earned exactly what

he bargained for—his wages paid in the form of some cash compensation and some restricted stock, with conditions that he had to meet (two years of continued employment) before he received full ownership of the stock.

Implications for Employers

The California Supreme Court has affirmed that employers and employees may agree to prospectively alter terms of the employee's employment including, but not limited to, the employee's wages. More specifically, for California employers presently offering or considering incentive compensation plans, *Schachter* clarifies that employers can offer such plans conditioned upon future events, such as an employee's continued employment. Indeed, the court held that "[o]nly when an employee satisfies the condition(s) precedent to receiving incentive compensation, which often includes remaining employed for a particular period of time, can that employee be said to have earned the incentive compensation (thereby necessitating payment upon resignation or termination)." By rejecting *Schachter's* contention that his unvested restricted stock constituted wages he had already earned, the court has signaled that parties have significant latitude in defining and structuring employees' compensation and, moreover, that both employer and employee will be bound by the compensation agreements they reach.

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