

READY TO PUNCH A TIME CLOCK?

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Big full-service brokerage houses like Merrill Lynch, Morgan Stanley, UBS and Smith Barney have long tried to have it both ways: hiring brokers as employees in an effort to own the client relationships, while treating brokers like independent contractors when it comes to certain expenses. At least that's what some disgruntled brokers say. And that double standard, as brokers see it, is poised to come back to bite them.

Merrill Lynch has already been hit. The firm paid \$37 million in July to settle claims in California that it owes thousands of former Merrill brokers overtime pay and that it improperly deducted certain business costs from their commissions during the four years ending September 2004, when the lawsuit was filed. (The brokers stand to collect about \$10,000 each, the attorneys \$9 million.)

Now, class-action attorneys smell blood. **Mark Thierman**, a partner with Thierman Law Firm in Reno, Nev., and the lawyer representing the plaintiffs in the California case against Merrill Lynch, says two more cases have already been filed in California. One is against UBS and the other is against Smith Barney; more cases in Illinois, New Jersey and New York will be filed by September, he says. In all, there are as many as 20 lawsuits in the works, Thierman estimates.

Rinse, Repeat

Merrill insists that what happened in California will stay in California. That settlement “revolves around the idiosyncrasies of California law, not federal law,” says a Merrill Lynch spokesman. But employment lawyers differ. While the cases will be decided on a state-by-state basis, both state and federal law come into play, and there are plenty of other states where similar cases could be won, they say.

Chargebacks are governed by state case law, which differs widely from state to state. In Florida, for example, there is little precedent, so it could be a tough battle for brokers in the Sunshine State. In New York, on the other hand, case law indicates that firms can charge back against bonuses, but not commissions — for many, the bulk of their pay.

Overtime pay, meanwhile, is governed by both state law and federal law — specifically, the Federal Labor Standards Act, which was revised last year. Those revisions included changes to the overtime pay rules for “white collar” workers: today, administrative employees who earn more than \$455 a week in salary (not commissions), or double the state minimum wage (whichever is higher), are exempt from getting overtime pay. But this so-called administrative exemption specifically does not apply to employees whose “primary duty” is to sell financial products, according to the U.S. Department of Labor's Code of Federal Regulations regarding nonmanual labor.

The base salary — or “draw” — that Merrill pays its brokers didn't meet the California minimum wage requirement, so the question of whether the brokers could be considered administrative employees didn't need to be addressed. Depending on the minimum wage requirements and the draw paid to brokers in other states, that question could play a larger role.

"I think what's going to happen now is employers will be reviewing the administrative exemption and seeing whether there really is compliance with it," says Ken Stein, an attorney with Ford & Harrison. The Department of Labor might also be asked to clarify that exemption, he adds.

In the aftermath of the settlement, Merrill Lynch says it has "clarified" certain compensation policies concerning financial advisors in California. But the firm declines to say what kinds of clarifications it made. Labor lawyers say the most obvious remedy is to raise the base salary they pay their brokers, which might then make them eligible for the administrative exemption. There's no such thing as a waiver of your overtime rights, under federal or state law, attorneys say.

Settle, For Less

Merrill and other firms will probably continue to settle rather than let the cases go to trial, say employment attorneys. Thierman estimates that if a firm the size of Merrill were to lose such a case in state court, it could face maximum fines and penalties of over \$200 million. Even if the firms settle, it could add up to hundreds of millions of dollars in legal and settlement fees.

To get out of this situation, firms will have to change their payroll practices, or seek a legislative solution, says David Marshall, a partner at Edwards & Angell in the labor and employment group in New York. But it could take years to reverse the changes made last year to the Fair Labor Standards Act, he says.

The irony of all this is not lost on Marc Rapaport, a class-action labor lawyer with Schaffer Rapaport & Schmidt in New York. After all, brokers may work long hours, but they also take home a bundle of dough. "They changed [the Fair Labor Standards Act] in a way that was probably thought to be pro-employer," he says. "Sometimes the language in the law has unintended consequences. It's amazing how often this occurs," he says.

One Merrill broker, who says he routinely works 80 hours a week and is frustrated by the firm's practice of making brokers pay sales assistant salaries and other expenses, says he still won't join the lawsuit. "One, how do I prove the amount of time I worked? Two, let's say they give me \$5,000. What does that mean? I'm challenging my employer, and in spite of what they might say, I'll be penalized for it," he says.