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## **Commission Pay for Employees: Structuring Agreements and Defending Claims Absent a Contract**

Leveraging Plaintiff and Defense Theories in Unpaid Commission Claims

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Today's faculty features:

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# Commission Pay for Employees: Structuring Agreements and Defending Claims Absent a Contract

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# How and When Commission is Earned

- Commissions earned at point of sale
- Commissions earned at time of customer payment (all payments made or some payments made)
- Commissions earned when employer recognizes revenue in its internal billing system
- Commissions earned when credited to employee
- Commissions subject to clawbacks
- Windfall provisions (McCormick v. Level 3 Comm'ns, LLC, 261 F.Supp.2d 476, 480 (E.D. Va. 2003))

# State Laws on Commissions

In Virginia, the Department of Labor and Industry has taken the position that if the salesperson had done all or substantially all that is necessary to close the sale, then the commission has been earned.

In California, commissions are treated as a form of “wages” which are protected under the Labor Code Section 221. If an employee has done all the work necessary to make the sale and the revenue is received by the employer, then a court may reject attempts to impose additional conditions that are unrelated to the sale or beyond the employee's control. Harris v. Investor's Business Daily, Inc., (2006) 138 Cal. App. 4<sup>th</sup> 28, 40-41; cf Fudali v. Pivotal Corp., 310 F.Supp.2d 22, 25-28 (D.D.C. 2004) citing D.C. Code § 32-101 et seq. (stating that commissions are not treated as wages in the District of Columbia).

# State Laws on Commissions

In New York, a commission is considered a wage under Section 190(1) of the Labor Law. A commission is considered earned either at the moment stated in the contract or, if no written or implied agreement exists, at the time of “the employee’s production of a ready, willing and able purchaser of the services.” Pachter v. Bernard Hodes Grp, Inc., 10 N.Y.3d 609 (2008).

In Texas, commissions are considered wages under the Labor Code. The Labor Code and the Texas Payday Law specify that commissions are earned when the employee has met the required conditions agreed to in writing, orally or by practice.

# What constitutes a contract?

Written agreement with employee

Employee handbook, written policies, training

Oral agreement

Business practices/past dealings



# Changing the Terms of Commissions

Changes may be made to terms of a commission but changed terms must be agreed to by employee. Remaining in the employment may signify agreement to new terms.

Where there is no written agreement or policy or changes are not made in writing, courts are more likely to construe terms in favor of employee.

Employees are generally entitled to the old plan until the effective date of the change. Changes are not retroactive.

# Examples of Commissioned Employees

Car dealership sales

Retail sales

Pharmaceutical sales

Telesales: selling goods and services, such as magazine subscriptions, over telephone or Internet

Maintenance and repair technicians

Financial services: financial advisor/stockbroker

Computer software sales

# Commissions Earned: Sample Language

- Sales will only be credited and commissions earned and paid, after approval by the CEO & CFO.
- Commissions are deemed Earned Commissions when the Company has received and accepted in writing a signed, valid and unconditional acknowledged purchase order prior to the quarter end.

# Commissions Earned: Sample Language

- Commissions are deemed earned when delivery of products to customer has occurred or services have been fully provided.
- Commissions are deemed earned when the company recognizes and declares revenue in the company's quarterly reports.

# Commissions Earned: Sample Language

Commissions are deemed earned when the risk of loss and title has transferred to the customer and collection on the account is not in doubt.

# Allowable Deductions

In general, deductions are more likely to be permitted when:  
employee expressly agrees to deduction and deduction is taken from draws, not earned commissions.

## California:

Deductions cannot be “unpredictable” or “taken without regard to whether the losses were due to factors beyond the employee’s control.” This includes business losses. See Hudgins v. Neiman Marcus Grp, Inc.

Returns may be deducted where such policy is agreed to by the employee. Compare DeLeon v. Verizon Wireless, 207 Cal.App.4<sup>th</sup> 800 (2012) with Harris v. Investor’s Business Daily, Inc., 41 Cal.Rptr.3d 108 (2006).

# Allowable Deductions

## New York:

Deductions may be taken from draws as agreed between employee and employer.

Deductions may be taken from earned commissions only as permitted by Labor Law Section 193 for items such as insurance, health benefits, charitable contributions, union dues.

## Texas:

Deductions from wages, including earned commissions, must be authorized in writing.

# Draws

Advance on commission payment. Draws are common where commission may take some time to vest or where the amount of future commissions is uncertain.

Draws are not considered wages since they are not yet earned. There must be express agreement that a payment is a draw, not an earned commission

Total payments received must meet minimum wage and overtime requirements for non-exempt employees.



# Draws

Reconciliation/recoverable draw: recoupment of a portion of a draw against future commissions by the amount that the advance exceeded commissions earned.

Reconciliation may be permitted where the employee expressly agrees in advance. New York law also requires that the agreement specify the frequency of calculation.

# Draws: Sample Language

Employee will also be entitled to receive a nonrecoverable draw of \$\_\_\_\_\_ per month for the first three months of employment and a recoverable draw of \$\_\_\_\_\_ per month for the following three months of employment. If employment terminates during the time period of the recoverable draw, employee will be responsible to reimburse the company the amount of the recoverable draw that was received.

Donovan v. Kentwood Development Co., Inc., 549 F.Supp. 480, (D.Md. 1982)(discussing impact of draws and FLSA exemptions)

# Minimum Wage and Overtime

All non-exempt employees are entitled to minimum wage and overtime premiums.

Business expenses must be reimbursed to the extent that they cause an employee's wage to drop below the required minimum wage or overtime compensation.

Accurate record-keeping is key for all employees.

Risks of misclassification: class actions, tax liability for underpayment of employment taxes.

# Is Your Worker Really an Independent Contractor?

Independent contractors are not employees and are therefore exempt from minimum wage, overtime requirements.

Factors include:

Employer's control over worker's day-to-day tasks: how a task is performed, set hours, training.

Who provides tools and supplies

Payment by job or by time worked

Continuing relationship versus isolated job(s)

Whether task performed is the principle business of the employer

Whether worker can work for other employers, makes services available to the general public.

Significant investment, opportunity for profit or loss by worker.

# Common Exemptions for Commissioned Employees

Certain employees are exempt from minimum wage and/or overtime requirements.

Outside salespeople: primary duty is making sales or obtaining contracts AND employee is customarily working away from the employer's offices.

Commissioned salespeople: exempt from overtime only.  
Employee works at a retail or service business AND wages exceed 1.5 times minimum wage AND more than half of earnings consist of commissions/draws.

Highly compensated employee: total compensation exceeds \$100,000 per year including at least \$455 per week in salary AND employee performs office or non-manual work AND employee regularly performs an administrative, executive or professional duty

# Other Possible Exemptions

**Administrative:** employee who performs office work directly related to management or general business operations of employer and exercises discretion and independent judgment

**Executive:** employee with primary duty of management of employer or a department therein who regularly directs two or more other employees and has authority in hiring or firing

**Learned Professional:** employee who performs work requiring advanced knowledge and study

**IT:** computer systems analyst, programmer, engineer who designs, tests, or modifies computer programs or specifications

**Creative:** employee whose duties require inventions, imagination, originality or talent

# Calculating Hours Worked

“Work” is exertion required or controlled by employer and pursued primarily for the benefit of employer. Common test is “integral and indispensable” to employer’s business.

Any waiting, changing or travel time that takes place after the first “principal activity” and before the last “principal activity” of the day is compensable work.

Remote work issues – paperwork, checking email, preliminary research, waiting time may be compensable.

Tracking time is necessary – watch for off-the-clock work.

Generally simple commuting time and de minimis additional time are not compensable.

# Commissioned Employee Wage Issues

Car sales: To qualify as “retail or service establishment” for commissioned sales exemption, at least 75% of the dealership’s business cannot come from re-sale.

Retail: Compensation based on store’s total sales vis company’s expectations found to be bonus, not true commission.

Telesales: complicated “points” system that used value of sales and other factors not true commission in Harris.

Maintenance technicians: continuous workday can include time waiting in company vain for jobs.

Financial Services: banking and investment companies lack “retail concept” so stockbrokers may not be exempt as commissioned sales people, although other exemptions may apply.



# Termination

- Terminated before payment is received
- Commission denied when termination occurs before payment is received
- Commission denied when termination occurs before payment is committed

# Termination: Sample Language

If your employment with the company is terminated for any reason, whether voluntarily or involuntarily, and whether with or without cause, you will not be paid for any sales not already credited prior to the date of termination.

Fudali v. Pivotal Corp., 623 F.Supp.2d 1, 8 (D.C. 2007)(discussing termination language in commission plan)

# Claims Against Employer

- Breach of Contract (Republican Nat. Comm. v. Taylor, 299 F. 3d 887, 892 (D.C. Cir. 2002))
- Promissory Estoppel (not recognized in some jurisdictions, like Virginia)
- Breach of Covenant of Good Faith and Fair Dealing (Kelly v. Skytel Comm'n Inc., 32 Fed. Appx. 283, 284-87 (9<sup>th</sup> Cir. 2002); McCollum v. Xcare.net, Inc., 212 F.Supp.2d 1142, 1150-54 (N.D.CA. 2002))
- Breach of Implied Contract (Wood v. Symantec, 872 F.Supp.2d 476 (E.D.Va. 2012))

# Claims Against Employer

- Unpaid wages: minimum wage, overtime, expenses. Off-the-clock claims common for commissioned employees.
- Potential class action
- Tax liability for misclassified employees

# Plaintiff: Written Discovery Strategies

- Litigation hold letter
- All communications related to payment from customer
- Company financial information related to customer payments
- Confirm payments from customer and how employer booked the deal
- Detailed 30(b)(6) notice
- Interrogatories related to payments, agreements, third party contracts, etc.
- Admissions related to commission plan

# Electronic Discovery

Meet and confer to agree on framework:

- Search terms, custodians
- Strategy to prepare and analyze documents
- Preliminary or representative search to estimate size of production

Talk with client to learn abbreviations, acronyms, slang to include in search.

# Deposing Employer & Corporate Representatives

- Gain admissions on timing of payment from customer
- Gain admissions from corporate representative regarding earned commissions.
- Gain admissions on terms of payment
- Gain admissions regarding how else others in company are paid

# Deposing Employer & Corporate Representatives

- Any prior investigations or reports of unpaid wages?
- Gain admissions on employer's understanding of commission, overtime, wage calculations.
- How are workers classified as independent or exempt?
- Ask about affirmative defenses asserted in answer.



# Deposing Co-Workers

- Single plaintiff versus class considerations
- Co-workers may support you but if still employed do not want to jeopardize current employment
- Do not be adversarial
- Confirm works performed
- Confirm payments made to co-workers
- Confirm manner in which co-workers understand how commissions, wages, overtime are calculated
- Keep it simple

# Experts to Calculate Damages

- Complex Commission Calculations may require the use of a forensic accountant or other expert
  - Net present value
  - Currency exchanges
  - OEM royalties
  - Licensing/Maintenance fees
  - Non-standard terms
- Management, manipulation, interpretation of large amounts of data may require expert
- In class context, judge may limit damages to amounts provable by records

# Special Concerns

- Protecting client from defense strategies re: performance issues
- Subpoenas to former employers
- Subpoenas to other third parties
- If government is a third party then generally no right to subpoena
- Class concerns: class representative should be a standard, typical employee, not necessarily the one with the biggest claim.

# Defense Theories & Techniques: Defeating Class Certification

A thousand different stories: differences between class members based on duties, method of compensation.

Class representative: not adequate or typical.

Offer of Judgment: Sole plaintiff in FLSA action who received Offer of Judgment that satisfied individual claim and attorneys' fees not permitted to pursue action as class because Offer rendered case moot. See Genesis Healthcare v. Symczyk, 569 U.S. \_\_\_ (2013).

# Defense Theories & Techniques: Protecting Trade Secrets in Litigation

- Before discovery is propounded you want to enter into a protective order to protect employer's proprietary information
- Discovery will inevitably lead to the disclosure of company's financial information and proprietary business information like purchase orders, third party contracts and payments for services or payments for goods
- Enforcing employment nondisclosure agreements
- Parties should work together to avoid filing documents under seal. This is a hassle for courts.

Sibley v. Sprint Nextel Corp., 254 F.R.D. 662, 666-69 (D. Kan. 2008)(discussing use of protective order for employee wage and employment records as well as confidential business records).

# Defense Theories & Techniques: Defending Against Claims

- Employer adhered to express agreements
- Workers correctly classified
- Minimal or speculative damages
- In class context, dismissing plaintiffs who do not respond to discovery or otherwise limiting class.
- Statute of limitations – minimize exposure before reclassification
- Potential counterclaims – but beware retaliation

# Defense Theories & Techniques: Deposing the Employee

- Commission disputes with previous employers
- Employee's performance
- Request documents from employee deponent
- Grueling depositions can be useful but can also backfire

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THANK YOU



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