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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))

# 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.

# 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)

# Plaintiff Theories and Techniques

# 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))

# Plaintiff: Written Discovery Strategies

- Admissions related to commission plan
- Interrogatories related to payments, agreements, third party contracts, etc.
- Company financial information related to customer payments
- All communications related to payment from customer
- Confirm payments from customer and how employer booked the deal

# 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
- Gain admissions on employer's understanding of commission, overtime, wage calculations
- Inquire into investigations

# Deposing Co-Workers

- 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

# 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

# Deductions Generally

Deductions are more likely to be permitted when:

employee expressly agrees to deduction and deduction is taken from draws, not earned commissions.

# Allowable deductions

## **California:**

Deductions can't be “unpredictable” or “taken without regard to whether the losses were due to factors beyond the employee’s control.”

Returns may be deducted where the policy is agreed to by the employee.

# Allowable Deductions

## **New York:**

May be taken from draws as agreed between employee and employer.

May be taken from earned commissions only under Labor Law Section 193 for certain items.

Regarding accidental overpayment of wages, certain steps must be taken.

## **Texas:**

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

## Draws: Generally

Advance on commission payment.

Draws are common where commission may take some time.

Draws are not considered wages.

Why?

There must be express agreement.

Total payments received must meet certain requirements.

## Draws: Specifics

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: Tips

Draft plans which *clearly and unequivocally* explain that commissions will not be earned until the occurrence of a specific event.

Articulate that any monies paid prior to the earning of commissions are *advances against commissions* that can be subject to charge-back;

Clearly explain *the terms and conditions of charge-backs*;

Ongoing work up to the vesting of a commission.

## 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: Generally

Federal and state law provide an interlocking set of rules governing wages and overtime.

The FLSA requires employers to pay an overtime premium of one and a half times the employee's regular rate for all hours worked in excess of 40 within a workweek and to also pay at least the minimum wage for all hours worked.

However, the FLSA establishes certain exceptions to these requirements. If the employee does not fit within an exception, then the employer must comply with the FLSA.

# Minimum Wage and Overtime: Exemptions

Employees covered by "white collar" exemptions include executives, administrators, and professionals.

To qualify, the employee must be paid a salary of at least \$455 per week (pending new anticipated federal regulations).

If this salary test is met, the employee must also satisfy a duties test.

Some commission-paid employees will satisfy these duties test.

A commission paid sales manager who supervises two or more employees might fall under the executive exception.

A salesperson who advises the client on the proper product to purchase might be an administrative employee.

# Commissioned Employees: Exemptions

Outside salespeople. making sales or obtaining contracts AND customarily working away from the office.

Commissioned salespeople (overtime only). 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 threshold AND employee performs office or non-manual work AND employee regularly performs an administrative, executive or professional duty

## State Exemptions

California. The salary must be at least \$3,466.67/month (\$41,600.00/year) and exempt duties must constitute more than 50% of the employee's time.

Colorado. It has very specialized state tests for exemptions.

Connecticut. The minimum salary level requirement is \$475.00. Also, the state does not permit exempt employees to be subject to disciplinary deductions for violations of workplace conduct rules.

## State Exemptions

In addition to FLSA restrictions, states are permitted to (and often have) wage hour laws more restrictive than the FLSA.

So... an exemption under the FLSA will not necessarily constitute an exemption under state overtime and minimum wage laws.

# Commissions: Non-Exempt Employees

For non-exempt commissioned employees, the next step is to determine which work activities constitute compensable work activities. The definition of compensable work is broad.

Under both the FLSA and many state laws compensable work time includes:

“all time spent in physical or mental exertion ... controlled or required by the employer ... primarily for the benefit of the employer’s business.”

All time during which employees are “suffered or permitted to work,” as well as time during which

# Commissions: Non-Exempt Employees

## **Calculate the Correct Rate of Pay.**

Where commissioned employees are entitled to overtime, the last step is to apply the correct overtime calculation.

The key is to determine the regular rate of pay, generally calculated by dividing an employee's total non-overtime compensation by the total number of hours worked.

The methodology may differ depending upon the specifics of the compensation system, especially where salaries are involved. Four common scenarios

# Commissions: Non-Exempt Employees

Four main calculations:

1. Commissions Only.
2. Commissions Plus Hourly Rate of Pay.
3. Commissions Plus Salary Intended to Cover 40 Hours of Work.
4. Commissions Plus Salary Intended to Cover More Than 40 Hours of Work.

## Documenting changes

**California.** Written commission agreement law Labor Code 2571.

Employers paying commissions must:

1. have a written contract with the employee regarding commissions that is signed by the employer;
2. include in the contract the method for calculating and paying the commissions; and
3. require the employee to sign a “receipt” retained by the employer.

## Plan changes - generally

Changes may be made to terms of a commission but changed terms must be agreed to by employee.

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.

# Defenses

- State of Frauds (Fox News host Geraldo Rivera)
- Statute of Limitations
- Parol Evidence
- Minimal or speculative damages
- Unclean Hands
- Offset
- Release
- Ambiguity (judgment call)
- Avoidance of Class Certification (2017 Oracle Commission Lawsuit)
- Counterclaims (as leverage)

# Protecting Trade Secrets

- Prior to litigation, clearly mark confidential information
- During litigation, enter into a protective order to protect employer's proprietary information
  - Two-tier levels of disclosure (CI and CI-Attorney's Eyes Only)
  - Special provisions under the state uniform trade secret statutes and the Federal Defend Trade Secrets Act
- Be prepared to produce and protect company's financial information supporting the commission amount
- Counterclaims for trade secret misappropriation?
  - State statute
  - Federal Defend Trade Secrets Act

# Deposing Employees

- History of commission disputes
- Employee's performance
- Employee's ulterior motives
- Inconsistent positions
- Facts establishing defenses
- Evidence supporting counterclaims
- Early deposition to lock them in

# Interaction with Federal and State Statutes

Fair Labor & Standards Act

State Payday Statutes

Texas: Final Paycheck

Special State Commission Agreement Rules

California: Must be in Writing

National Labor Relations Board

Non-Competition and Non-Solicitation

Federal Defend Trade Secrets Act

Anti-SLAPP Statutes

# THANK YOU



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