New Commission Agreements Law

Requires Review of Pay Plans

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A California law enacted in 2011 requires that by January 1 of this year, whenever an employer enters into a contract of employment with an employee who is paid on a commission, the contract must be in writing and must set forth the method by which the commission shall be computed and paid. This new law, A.B. 1396, further requires that the employer give a signed copy of the commission agreement to the employee and obtain a signed receipt for it as well.

This law applies to dealership pay plans for commission-paid employees and its impact is likely to be greater than merely requiring that dealers obtain signed receipts for pay plans. Plaintiffs' attorneys may soon focus on dealerships as potential targets for class action or Private Attorney General Act (PAGA) lawsuits for failing to have pay plans that comply with this law. Such scrutiny will not end at whether pay plans are compliant with A.B. 1396, however. Pay plans will additionally be reviewed for non-compliance with overtime and other wage and hour laws.

Compliance With A.B. 1396

Pay plans for commissioned employees hired after January 1 and pay plans for existing employees that are changed this year must comply with this new law. A "commission" covered by this law is defined as a payment for services rendered in the sale of the employer's goods or services that is based "proportionately" on the amount or value of the sale.. Clearly, employees who are paid a commission on sales they personally make are covered by this law. The law suggests that employees who are paid a percentage of store or department profits are covered too, as it applies where an employee is paid "a fixed percentage of sales or profits as compensation for work to be performed."

A.B. 1396 requires that a pay plan describe how a commission is to be computed and paid. While the courts have yet to interpret this law, it will likely be read to require the following:

(1) Where an employee is paid a percentage of profit on a deal, a clear and complete explanation should be provided of how that profit, or commissionable gross, is to be calculated. First, all sources of revenue to be taken into account must be specified. Will dealer holdback be included in the gross? Second, all "packs" and internal costs assessed on a deal must be disclosed.

(2) If chargebacks will be assessed against future commissions this must be disclosed as well.

(3) The pay plan must be clear regarding when the commission is deemed earned, so that the employee's entitlement to commissions upon termination of employment may be determined. Is the sale complete when the vehicle is delivered, or at some other point in the transaction? Dealers have some flexibility regarding how much of a commission will be paid for sales not yet completed when the employee terminates, but the terms must be clearly explained.

(4) If a draw is paid, the pay plan should state when the draws will be reconciled against commission. If the draw will carry forward if not exceeded by commissions, this should be stated as well.

(5) The pay plan must disclose the day of the month when commissions will be paid.

While not required by law, pay plans should additionally contain employment-at-will language. Finally, the signed receipt for the pay plan which this law requires should be kept in the employee's personnel file.

Compliance With Wage and Hour Laws

All employees must be paid at least minimum wage (plus overtime if applicable) for all hours worked. Therefore, all salespersons must record their hours and a calculation must be done each pay period to ensure that the employee's draw or commissions are sufficient to meet minimum wage.

To be exempt from overtime, a commissioned employee in a dealership may fall under the inside commission sales exemption. To qualify, (1) an employee must earn more

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than 1-1/2 times minimum wage (i.e., at least $12.01) for all hours worked, and (2) more than half of the employee's compensation must be in the form of commissions. The first test must be met for each pay period. This means that if a salary or draw is paid on one of two paydays per month, it must exceed 1-1/2 times minimum wage for all hours worked during the half of the month that it covers. Likewise, commissions paid on the other payday must also exceed 1-1/2 times minimum wage for all hours worked during the other half of the month.

The second test (i.e., more than half of pay being commissions) may be met on a monthly basis, but for the purposes of this test, a narrow definition of "commission" applies: (1) payment for services rendered in the sale of the employer's property or services, and (2) based proportionately upon the amount or value thereof.

The executive exemption may cover managers who supervise two or more employees and who spend more than half their working time performing management duties. To qualify for this exemption, however, a manager must be paid a salary or guarantee amounting to at least twice the minimum wage ($16.00) for a 40 hour week, which is at least $640.00 per week or $2,773.33 per month.

If a commissioned employee does not qualify for one of these exemptions in a pay period, overtime must be paid. It is calculated by dividing all compensation earned (commissions plus salary if applicable) by the number of hours worked. This produces the "regular rate" of pay for that period. One-half of the regular rate must then be paid in addition for all hours of overtime worked.

Finally, even if inside salespersons are exempt from overtime they still must receive meal and rest breaks, and these should be documented.

All Pay Plans Should Be Reviewed

Dealers should review their pay plans for commissioned employees now to determine if they comply with A.B. 1396 and applicable wage and hour laws. If they do not, they should be changed promptly to avoid significant future liability. OCADA

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