FROM THE ARCHIVES: New Year's Resolution? Review Your Sales Pay Plan

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Many dealerships give little thought to their sales pay plans. After all, they're simple and straightforward, right? X% of the front gross and Y% of the back end gross, plus whatever bonuses you choose to give. About as simple as you can get.

Unfortunately, an increasing number of dealerships are finding out that their pay plans are a lot more complicated than they thought, particularly when they are examined in a courtroom by jurors who know nothing about the car business. A case from New York provides a good example of how complicated a sales pay plan can be.

Case In Point
In this case, a group of salespeople sued their dealership group, claiming they were paid below minimum wage and had unlawful deductions taken from their commissions. Eventually, a total of 89 salespeople from all six dealerships joined the lawsuit.

The sales pay plan at issue was straightforward enough: 20% of the front gross and 10% of the back gross, less a $275 pack on new cars and a $950 pack on used cars; and $50 mini on a new car sold at a loss, $100 mini on a used car. The dealership group also paid $20 per day as shift pay. Like most salespeople, they worked 45 to 55 hours a week, a fact the dealership group admitted.

Minimum Wage: Strike One
The court ruled on the minimum wage claim quickly and easily – and in favor of the employees. The facts showed that when salespeople made no sales in a particular week, the dealerships only paid them $20 per day, far less than the required minimum wage. The court rejected the dealership group's argument that the salespeople's annual earnings – $40,000 to $50,000 – were more than sufficient to cover minimum wage on an annual basis.

This attempted "annual salary pitch" was dismissed as a red herring. After all, the law is clear: with a weekly pay plan, the salespeople must be paid at least the minimum wage for all hours worked each week, regardless of earnings in previous or subsequent weeks.

Deductions: Strike Two
The court then turned to the commission claim. The salespeople claimed that the dealership group had manipulated their commissions in a number of different ways by adding additional "packs" and

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including extra “costs” to the vehicle and the transaction. Specifically, each of the dealerships made a deduction for “auction expenses” to which the salespeople had not agreed.

They also argued that the dealerships inflated the actual cost of these charges by having some work performed by “sham subsidiaries.” They claimed, for example, that the actual costs of etching, tire and wheel protection, and extended warranties were inflated when deducted from their commissions, further reducing their compensation. Finally, they claimed that the dealer group made improper deductions from their commissions by fining them for personnel infractions (using improper forms, tardiness, other disciplinary matters), damage done to vehicles, and mechanical problems.

The court started by examining the written documents explaining the commission calculation and found that they permitted the employer to make deductions for commission packs, transportation expenses, open Repair Orders, and gasoline costs. However, the court found that there was no language authorizing the deduction for “auction expenses.” Therefore, that deduction was found to be improper and unlawful.

The dealership group defended the deduction, claiming that they had been taking it for years without complaint, meaning that the salespeople had, in effect, agreed to it. Not so, said the court: “A failure to complain does not render that conduct permissible in light of the clear contractual language to the contrary. Silent suffering of a contractual breach certainly does not excuse the dealership’s failure to live up to its contractual obligations.”

The court then addressed the “chargeback” deductions for disciplinary matters and similar infractions, and also found them improper. The court noted that none of these deductions were spelled out in the pay documents, and were not part of any established company policy.

Willful Violations: Strike Three

All these mistakes were compounded when the court determined that the dealer group’s violations were “willful,” entitling the salespeople to double the amount improperly withheld. Under federal law, proof of willfulness is fairly easy: the salespeople only had to prove that the dealership group was aware of the existence of the federal Fair Labor Standards Act.

In this case, that finding was not hard to reach. The court noted that the dealer group had undergone two state wage-hour investigations in recent years and had been cited for wage violations on both occasions, but had never changed its pay practices.

Resolution Of The Case: It Wasn’t Pretty

So how did it all turn out? The case finally settled in December 2015, six years after it was originally filed. The soft costs associated with six years of litigation were staggering: a number of company employees, including owners, were subjected to stressful and time-consuming depositions; the dealerships had to produce hundreds of thousands of documents in discovery; the plaintiffs’ attorneys spent days at the dealerships examining thousands of deal files; and management was

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forced to attend numerous court hearings, meetings with their attorneys, and at least two mediation sessions.

The hard costs were even worse. The dealership group settled the minimum wage claims for $423,569.92. It also agreed to settle the commission claims by creating a fund of $5,500,000. About a third of the fund will go to the plaintiffs' attorneys, while the rest will cover unpaid commissions, settlement costs, and other costs associated with the case.

Plus, the group had been paying its own attorneys – two different attorneys, one representing the owners and the other representing the General Manager, who had also been named in the lawsuit – for the six years of litigation.

To add insult to injury, the lawsuit inspired a separate "copycat" lawsuit filed by another former salesperson making the same claims. That separate case took over two years to resolve and finally settled for $150,000.

Lessons To Be Learned

So what can we learn from this case? You should resolve to start the new year by reviewing your pay plan to make sure you don't fall victim to the same troubles. Here are six practical steps you can take right away:

1. Remember that a sales pay plan is a legally binding document, enforceable in court. You should take great care in drafting it to be sure that it states exactly how your salespeople will be paid.
2. More importantly, you must ensure your salespeople are paid exactly in accordance with the plan. If you want to make an additional deduction in the commission calculation, for example, or make any other modification, you must revise and reissue the pay plan.
3. You can calculate the commission any way you want, but you must clearly disclose any particular deductions that will be made from commissions.
4. If you justify any part of your pay plan simply because you've been paying your people that way for years without complaint, that's no guarantee you won't be sued tomorrow. Pay plan claims are treated as contract claims, which often have a six-year statute of limitations. Review them to make sure they are compliant even if you've heard no complaints.
5. Similarly, claiming that "all dealerships do it this way" is not likely to impress a judge. Arguing that a certain part of your plan is "industry practice" is unlikely to get you off the hook in court. Review your plan with an eye toward the law, not toward the dealership down the street.
6. Make sure you review your company policy to make sure it doesn't conflict with the pay plan or the law. Unilateral policies (allowing for deductions for fines or damage to vehicle, for example) are unlikely to trump the terms of a pay plan, and could violate state or federal law.

Conclusion: Don't Scrap Your Pay Plan

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The irony of this and many other sales pay plan lawsuits is that the dealership could have lawfully paid its salespeople exactly as it wanted if it had just properly drafted its sales pay plan. For example, a dealership could lawfully deduct the cost of the dealer's dog groomer from sales commissions so long as this is clearly spelled out in the pay plan.

Perhaps this is one reason why so many dealership pay plans are purposefully vague – some dealers do not want to be up front with their employees about what is actually being deducted when calculating their commissions. Of course, as this case made clear, if you are not up front and your pay plan is not transparent, there may be a significant price to pay.

We've heard reports of some dealers who are so frustrated with legal concerns that they decide they are going to do away with written sales pay plans altogether to protect themselves from liability and preserve their flexibility. Don't do that; that's just jumping out of the frying pan and into the fire. Your pay plan will still be just as legally binding as a written one, but now it will be an oral contract. It is far more difficult for a dealership to prove the terms of such a contract, and your chances of winning in court will be greatly reduced.

For years, Fisher Phillips has helped dealerships across the country draft sales pay plans that comply with both federal and state laws, and also include proper commission-deduction disclosures. If you would like to have us review your current sales pay plan to determine if it will pass legal muster, we would be happy to do so.

Just contact your Fisher Phillips attorney, or call any of our offices and ask for a member of our Automotive Dealership Practice Group. They will be happy to help.

For more information, contact the author at JDonovan@fisherphillips.com or 404.240.4236.

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