IT'S COMP-LICATED: TRICKY COMPENSATION ISSUES FOR EMPLOYERS

I. RISKS AND REWARDS WHEN UTILIZING INCENTIVE COMPENSATION

A. Rewards.

1. Motivation.

2. Increased sales or productivity.

3. Loyalty.

4. Increased employee job satisfaction.

5. Teamwork.

6. Increased investment in employer's success.

7. Retention of key employees.

B. Risks.

1. Setting effective metrics.

   a. Incentive compensation must be sufficient so as to motivate employees to increase productivity or meet objective goals.

   b. However, the bonus or compensation cannot be disproportionately large so as to completely offset the gains from the employee's performance.

2. Incentive compensation can promote the wrong behaviors.

   a. Employees can begin to put their own interests ahead of the interests of the employer.

b. Moreover, incentive compensation based on sales performance can lead to employees pushing ethical boundaries (i.e., Wells Fargo sales scandal, 2008 subprime mortgage crisis).

c. Employees may be more apt to engage in risky behavior with the possibility of a large monetary award.

3. Fairness.

a. Often times, the most talented employees are given the most difficult tasks, while weaker employees are given more mundane, rudimentary tasks which are easier to accomplish.

b. Not all employees are eligible to participate in incentive compensation programs.

c. Can cause resentment amongst team members.

4. Lack of clear, objective measures.

a. Objective measures are necessary to give clarity as to when employees are going to be rewarded.

b. Using subjective measures (i.e., improve communication skills, increase efficiency, be more of a team player) will likely lead to a dispute between the employer and the employee over whether or not an incentive compensation award has been earned.

c. Lack of clarity in metrics will likely lead to disputes between employers and employees over awards of incentive compensation.

d. If metrics are confusing, employees will be less likely to "buy in" and the plan will be ineffective.

5. Communicating expectations and monitoring progress.

a. Employers should communicate not only the "what" but more importantly the "why" and the "how" of the incentive compensation plan. Emphasis on the "why" will lead to employee investment in the employer's success.

b. Employers should have an effective tracking system so employees know where they stand in relation to their performance goals.

6. Incentive compensation may not lead to increased performance.

a. Some research shows that certain employees are motivated by things like competence, autonomy and connection with teammates. Offering financial rewards to such employees may not stimulate the behavior sought by the employer.

b. Employers may want to consider doing informal surveys of their employees to see if incentive compensation will promote the behaviors they desire.

II. MICHIGAN'S EQUAL PAY STANDARDS AND STATUTES

A. Elliott-Larsen Civil Rights Act (MCL Sec. 37.2202).

1. Employer is prohibited from discriminating against an individual with respect to compensation because of religion, race, color, national origin, age, sex, height, weight or marital status.

B. Workforce Opportunity Wage Act (MCL Sec. 408.423).

1. An employer having employees subject to this act shall not discriminate between employees within an establishment on the basis of sex by paying wages to employees in the establishment at a rate less than the rate at which the employer pays wages to employees of the opposite sex for equal work on jobs, the performance of which requires equal skill, effort, and responsibility and that is performed under similar working conditions, except if the payment is made under one or more of the following: (a) a seniority system; (b) a merit system, (c) a system that measures earnings by quantity or quality of production; or (d) a differential based on a factor other than sex.

C. The Michigan Penal Code (MCL Sec. 750.556).

1. Any employer of labor in this state, employing both males and females, who shall discriminate in any way in the payment of wages as between sexes who are similarly employed, shall be guilty of a misdemeanor. No female shall be assigned any task disproportionate to her strength, nor shall she be employed in any place detrimental to her morals, her health or her potential capacity for motherhood. Any difference in wage rates based upon a factor other than sex shall not violate this section.

III. <u>AVOIDING CLAIMS UNDER MICHIGAN SALES REPRESENTATIVE COMMISSION ACT ("SRCA")</u>

A. Michigan Sales Representative Commission Act (MCL Sec. 600.2961).

1. Principal - A person who does either of the following: (a) manufactures, produces, imports, sells or distributes a product

in this state; or (b) contracts with a sales representative to solicit orders for or sell a product in this state.

2. Sales representative - A person who contracts with or is employed by a principal for the solicitation of orders or sale of goods and is paid, in whole or in part, by commission. Sales representative does not include a person who places an order or sale for a product on his or her own account for resale by that sales representative.

3. Commission - Compensation accruing to a sales representative for payment by a principal, the rate of which is expressed as a percentage of the amount of orders or sales or as a percentage of the dollar amount of profits.

B. When are commissions due and payable?

1. If there is a contract, then the terms of the contract will dictate when commissions will be paid.

2. If there is no contract, the past practices between the principal and sales representative shall control or, if there are no past practices, the custom and usage prevalent in this state for the business that is the subject of the relationship between the parties.

3. All commissions that are due at the time of termination of a contract between a sales representative and principal shall be paid within 45 days after the date of termination. Commissions that become due after the termination date shall be paid within 45 days after the date on which the commissions became due.

C. What if principal fails to pay commissions?

1. Principal is liable for both of the following:

a. Actual damages caused by the failure to pay the commissions when due; and

b. If the principal is found to have intentionally failed to pay the commission when due, an amount equal to two times the amount of commissions due but not paid as required by this section or $100,000.00, whichever is less.

2. What constitutes "intentional" failure to pay a commission?

a. Does not require a showing of bad faith.

b. Only requires a showing that principal purposefully withheld the payment of a commission.

3. Attorneys' Fees.

a. If a sales representative brings a cause of action pursuant to this section, the court shall award to the prevailing party reasonable attorneys' fees and court costs.

D. Waiver of Rights.

1. A provision in a contract between a principal and a sales representative purporting to waive the sales representative's rights under the act is void.

E. Oral agreements to pay commissions are also covered under the statute.

F. Can a principal set-off amounts owed by the sales representative against the commissions owed?

1. *Peters v. Gunnell*, 253 Mich App 211; 655 NW2d 382 (2002).

2. Principal must pursue amounts owed by sales representative by way of a separate action and cannot offset those amounts against commissions owed to the sales representative.

G. The “Procuring Cause Doctrine”.

1. An agent is entitled to commissions, even if he or she did not personally complete the sale, if his or her efforts were the procuring cause of the sale.

2. Applies only where the parties have not addressed the subject of post-termination commissions, and seeks to ensure that the manufacturer does not unfairly benefit from the opportunistic termination of a sales representative after he or she has procured a sale but before the sale is consummated.

H. Steps for employers to protect themselves from claims under the SRCA.

1. Avoid oral or “back of the napkin” agreements with sales representatives. Always have a written agreement that clearly sets forth the rights and responsibilities of both the employer and the sales representatives.

2. Things to consider in putting together a sales representative agreement:

a. What are the sale representative’s duties?

b. When are commissions earned and when they should be paid?

c. Is the sales representative compensated for completed customer “sales” or for customer “procurement”?

d. What constitutes grounds for termination of the agreement?

e. What happens after the sales representative is terminated by the employer?

f. Should the sales representative be subject to non-competition and non-solicitation provisions?