New York legislature takes aim at dealership pay plans

By Ari Karen and Aaron Jacoby, Venable LLP

(Editor's note: The following article by attorneys Ari Karen and Aaron Jacoby relates to a change in New York state law and affects car dealers in that state. However, we know from experience, that once pay plan regulations take hold in one jurisdiction, they spread quickly to others. A word to the wise.)

New York's franchised car dealers are among the first to face new laws requiring written pay plans for commission based employees. The new legislation presents an opportunity for dealers to review and revise their pay plan practices. However, dealers that either rely upon verbal commission payment terms or poorly drafted pay plans will face increased litigation risk.

New York Labor Code Section 191(c) was recently amended to require a written commission agreement specifying numerous components of the commission. In the absence of a written pay plan, or if a pay plan creates confusion or ambiguity, the employee's recollection of the material payment terms is given presumptive effect; i.e. whatever the employee "recalls" goes.

Challenge for dealer/owners

Several challenges are presented by the requirement of a clearly written plan. First, dealers must define common industry terms to avoid misinterpretation. A number of recent cases involve claims that even the most common of industry terms, like "Front End" and "Back End," are ambiguous when it comes to pay plans, finding that the terms were manipulated by dealers to cheat employees. In fact, common industry terms are not always commonly understood and it may be difficult for an expert to explain the nuances with precision – particularly since one dealer's "Back End" is another's front or split.

Since judges have no innate understanding of auto industry terms, they may be inclined to find that any agreement that fails to include a clear definitions section is ambiguous. That may result in a verdict for the plaintiff. Dealers can overcome this challenge by adding a simple definitions section to the employee's written pay plan.

No chargebacks

Another significant challenge for New York car dealers is raised by a recent case, *Pachter v. Bernard Hodes Group Inc.*, which prohibits dealers from taking deductions from an employee's earned commission. In other words, once a commission is calculated, a dealership cannot deduct or charge back for any reason. Moreover, any elements of a sale that are excluded from the commission calculation must be carefully itemized. The *Pachter*

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case need not mean the end of legitimate deductions or charge backs, though it certainly means doing so with caution and a well thought out process.

Dealers may wish to craft a draw against commission system that will allow employees to receive pay while awaiting the calculation of the final commission, inclusive of any charge backs or deductions set forth in the pay plans.

The emphasis is now being placed on when commission is "earned." Absent a specific provision in an agreement clearly defining the timing of the final calculation, courts will deem the commission earned at the earliest possible time, such as when a sale has been originated by an employee – even if substantially more is required to "close the deal."

Remember that once an employee "earns" commission in New York, they have obtained an inalienable right to payment without deduction or charge-back. Accordingly, defining the timing of the commission calculation as "earned" at the latest possible point, is critical to maintaining control over the vesting rights in the commission payment.

Dealers should note that, regardless of any timing provision, commission agreements that require the employee to be employed on the date commission is paid, or that contain provisions forfeiting commissions, are invalid and unenforceable, and expose the dealer to significant penalties and liability.

In cases where employees are paid exclusively on commission, dealers must be clear as to which employees are entitled to minimum wage, how much must be paid in guaranteed compensation and, if relevant, how to recoup the cost of minimum wage through non-commissioned sales. As with many of the other issues raised here, form is as important as substance. Drafting the agreements correctly can mean the difference between prevention and liability.

Lesson for dealers: Take action to audit and revise pay plans

Every dealership can easily avoid pay plan nightmares. Drafting a proper pay plan template is the answer to these new challenges. Including additional provisions, such as a definitions section and immediate commission dispute resolution, can greatly minimize commission based claims. Dealers should seek counsel to audit and review existing pay plans to ensure that all necessary provisions are in writing and comply with these new laws. ❖

Ari Karen, Esq. and Aaron Jacoby, Esq. co-authored this article. Aaron Jacoby is a partner and chair of the auto industry practice with Venable LLP. Ari Karen is a labor and employment partner with Venable LLP. Mr. Karen can be reached at (202) 344-4649 or by e-mail at **akaren@venable.com**. *Mr. Jacoby can be reached at (310) 229-9940 or by e-mail at* **ajacoby@venable.com**.