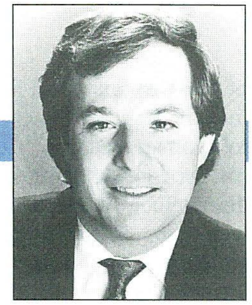
A Word to the Wise...Put It In Writing



By Steven Mitchell Sack

There is an important trend in sales and marketing (which has little to do with demographics, consumer attitudes or incentive trips) that is taking place in the courts. The number of lawsuits instituted by disgruntled ex-salespeople has increased dramatically over the past few years. So too, has the size of the average settlement and awards given to successful litigants.

Recent changes in the law throughout the U.S. have made it easier for the salesperson to sue — and win — a lawsuit against a former company. Salespeople have become more knowledgeable about the legal remedies available to them and are more inclined to enforce their rights. For example, the recent passage of sales representation protection statutes in more than 30 states guarantees prompt payment of commissions, and awards sales reps up to three times the commissions owed and attorney fees.

Such laws correct certain perceived inequities in the relationship between independent sales reps and their principals, demonstrating a greater awareness by salespeople and legislators.

Thus, avoiding litigation should be one of a sales executive's chief concerns. Lawsuits are time-consuming, expensive and often garner bad publicity. While you cannot entirely eliminate the risk of litigation, there are ways to increase the odds in your company's favor. The following points will help you steer clear of common problems associated with hiring company salespeople and independent reps.

Discriminatory questions

The art of selecting the right person for the job is a matter of concern for all sales executives. However, illegal questions are sometimes asked on employment applications or during interviews.

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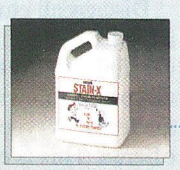

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Circle No. 317 on Inquiry Card — ISSA Booth #7334 of 1964, as amended, prohibits inquiries into an applicant's race, color, age, sex, religion and national origin. For example, female applicants are often asked discriminatory questions about child care (e.g., "Who will look after your child while you are working?") while the same questions are not asked of male applicants. In addition, inquiries pertaining to medical history, arrest records or even former drug use are illegal, because employers are required to consider applicants as they presently exist, not based on their past.

Remember too, that most states have their own laws protecting the rights of applicants, and severe consequences often occur when discriminatory questions are asked. An applicant merely has to file written charges against your company with the Equal Employment Opportunity Commission, Civil Liberties Union or Human Rights Commission in your state.

The charges are then investigated, formal inquiries and hearings may be conducted and penalties can be imposed, including job reinstatement, large fines and an award for attorney fees. Thus, it is essential that executives review their company's employment applications and prepare for the hiring interview in advance in order to avoid asking discriminatory questions and possibly basing a hiring decision on answers to such questions.

Guarantees

Avoid making earning claims you cannot guarantee. Some executives innocently make promises about potential earnings in an effort to woo high-caliber applicants. The Federal Trade Commission (FTC) considers such statements to be an unfair and deceptive trade practice when earnings are promised (e.g., "If you join our company, you will make $100,000 in commissions this year, because that's what our other salespeople make.") that exceed the the average net earnings of your other salespeople. That is why you should tell an applicant that he/she "*may* earn *up to* 'X' dollars this year," but avoid promising earnings unless you can guarantee the figure.

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Key points to cover when hiring a salesperson or independent rep

Compensation

1. Salary (usually given to company-employed salespeople)

What is the amount and when is it payable?

2. Draw (usually given to independent sales reps)

Is it applied against commission?

What is the amount and when is it payable?

The draw can be stopped by the company at any time without prior notice when commission earnings do not exceed draw.

The sales rep is personally liable for repayment when draw exceeds commission earnings, or the rep either resigns or is fired.

The company has the right to set off draw and reduce the amount of commission owed upon termination of the employment relationship.

3. Bonus (usually given to company-employed salespeople)

Is the bonus gratuitous or enforceable by contract?

What is the amount and when is it payable?

Specify that pro rata bonuses will not be given in the event the salesperson resigns or is fired prior to the date the bonus will be paid.

Avoid basing the bonus on a determination of profits, as this may give the salesperson the right to inspect your company's books and records.

4. Commission

Specify the commission rate and when it is payable.

Avoid guaranteed shipping arrangements.

Specify split commission policies, if applicable.

Specify all deductions from commissions, how and when they are computed; e.g. returns, freight charges, unauthorized price concessions given by the salesperson, billing and advertising discounts, collection charges, failure of the customer to pay.

Specify commission for large orders, special customers, off-price goods and reorders.

5. Expenses (usually for company-employed salespeople)

Specify the kind and amount of expenses that are reimbursable.

Specify the kind of documentation the salesperson must supply in order to receive reimbursement.

Territory

Are you giving exclusive or non-exclusive territorial rights? Define the particular territory and customers.

Be sure to discuss all house accounts and document these in writing.

What about products sold in one territory and shipped into another? Determine how this will affect your split-commission policy.

Can the salesperson sell in other territories not solicited by other salespeople, e.g. at trade shows?

If exclusive rights are not involved, ensure that the salesperson will not receive commission for orders not actually solicited by that individual.

Duties of the salesperson

Exercise best efforts in representing the company and its products or services.

Make no representations, warranties

Recognize that the law can also be violated when a sales manager exaggerates the amount of back-up support for a salesperson or promises exclusive sales territories which cannot be allotted.

Employment terms

Discuss all employment terms in advance. Sales managers must discuss carefully all the terms and responsibilities of the job with the applicant, no matter what type of sales job is being offered. This is essential to maintaining positive relations with your sales force and minimizing breach-of-contract and wrongful termination lawsuits.

The above list shows the key negotiating points to be discussed with applicants when hiring a company salesperson or an independent rep.

Document everything

Document your employment agreement in writing. Once you and the salesperson have agreed to key terms, it is important to confirm the deal. Legal disputes usually arise in this area because companies hire their salespeople on a handshake.

A handshake or an oral agreement indicates only that the parties came to some form of agreement; it does not or commitments binding the company without the company's prior consent.

The salesperson will:

• Be personally liable and required to reimburse the company in the event he exceeds this authority.

• Forward all field inquiries or complaints in the field to the company immediately.

• Must work full-time for the company without any sideline, and especially must not represent or form a competing business.

• Must personally solicit the product and cannot hire an associate to represent the company without prior written approval.

• Maintain minimum general and automobile liability coverage in excess of $X per occurrence.

• Attend sales meetings, both local and national.

• Call on accounts periodically, service accounts, and maintain accurate selling records and lead sheets.

• Assist in any collection efforts requested by the company.

• Promise to protect all trade secrets, customer lists and other forms of confidential information acquired while working for the company.

Length of employment relationship

State the date that employment is to begin, and whether or not employment is at will (the salesperson can be fired anytime) or for a definite term, say, two years?

If employment is at will, is notice required? If so, for how long must it be sent for the termination to be effective and how must it be sent (e.g., certified or regular mail)?

Never give assurances of job security if you are hiring a salesperson at will.

If employment is for a definite term, is the contract renewable under the same terms and conditions after the expiration of the original term? Must notice be sent to confirm?

Peg employment to a minimum sales quota, if applicable.

Termination of employment

Clarify when commissions stop; e.g., upon termination, upon shipment of order, upon shipment with a cut-off date to eliminate the problem of reorders.

Avoid severance compensation arrangements.

Specify when a final accounting will be made.

Limit the right of the salesperson to sue for commissions within a specified period.

Specify the prompt return of all samples, customer lists, orders, field information, with a penalty if not compiled with.

Include a restrictive covenant for additional protection in writing.

say what that agreement was. Failure to spell out important terms often leads to misunderstandings and disputes. Even when key terms are discussed, the same spoken words that are agreed upon have different meanings from the salesperson's and company's perspective. Written words limit this sort of misunderstanding.

There are other reasons why it is advantageous for companies to use written contracts. One is the arbitration clause. You can compel an ex-employee to resolve a dispute by arbitration rather than litigation if you include such a clause in your written contract, thus forcing the salesperson to sue you in the location of your choice (usually where your company is located) rather than some distant site.

This will make it cheaper and less burdensome for your company to defend itself in a lawsuit. In addition, since many

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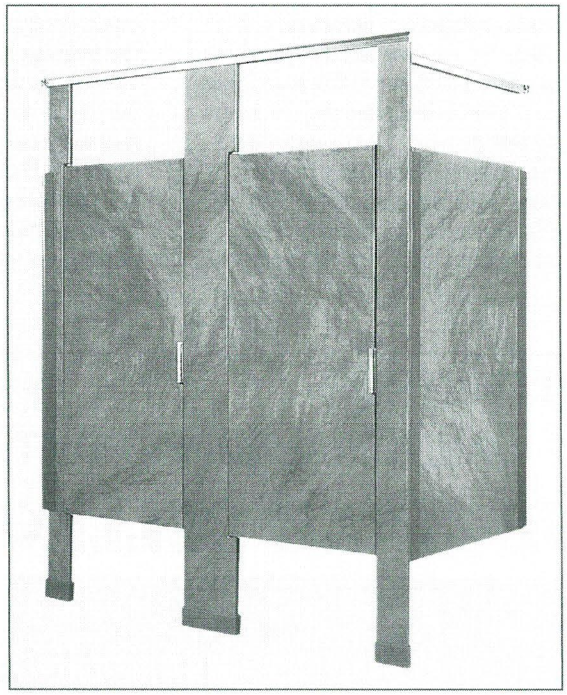

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attorneys believe that juries tend to favor individuals over companies, it is often best for the case to be decided by a no-nonsense arbitrator rather than a jury.

Arbitration eliminates the salesperson's most powerful weapon in commission disputes: the right to view your company's private books and records. Because of arbitration's streamlined features, the salesperson's attorney will probably not be able to obtain private records until the day of the hearing and may only be able to view those records that the company wishes to reveal. This, of course, differs markedly from pre-trial inspection and discovery procedures that allow attorneys to examine company books relevant to the proceeding.

Another advantage of a written contract involves the use of a restrictive covenant. Such a clause can restrain the salesperson from working for a competitor, starting a competing business, using company customer lists or confidential information for his own advantage, or calling upon your customers within a particular geographic territory or time period after he has stopped working for you.

Without a written contract, you cannot obtain an injunction to stop a former employee from working for a competitor. However, by inserting a restrictive covenant of reasonable geographic scope and duration into the contract, such a tactic can be pursued if someone joins a competitor.

Although a written contract cannot guarantee that you will be satisfied with your sales staff's performance, it will provide the company with additional remedies in the event of non-performance. Most companies are learning that they can still fire a salesperson without notice (which was the main reason why companies previously hired on a handshake), but can protect themselves better with clearly-drafted contracts.

For example, by specifying in writing that commissions cease upon termination of employment for any reason, the salesperson cannot claim post-termination compensation for re-orders or services rendered. This is a valuable point that should never be overlooked.

Properly execute contracts

When employment contracts are issued, be sure that all changes are noted by both you and the salesperson. If your company uses a standard employment contract, be sure all blanks are filled in. If additions are necessary, include them in a space provided or attach them to the contract itself.

Then, note on the contract that the addenda have been accepted by both parties. This prevents questions from arising if addenda are lost or separated because it's difficult to prove that they ever existed without specific mention of them in the contract itself.

Steven Mitchell Sack is a prominent labor & employment attorney with a private law practice in New York City. He is a Phi Beta Kappa graduate of SUNY-Stony Brook and Boston College Law School and is the author of 14 legal books for the American public. He can be reached at (212) 702-9000 if you have any questions or need assistance.

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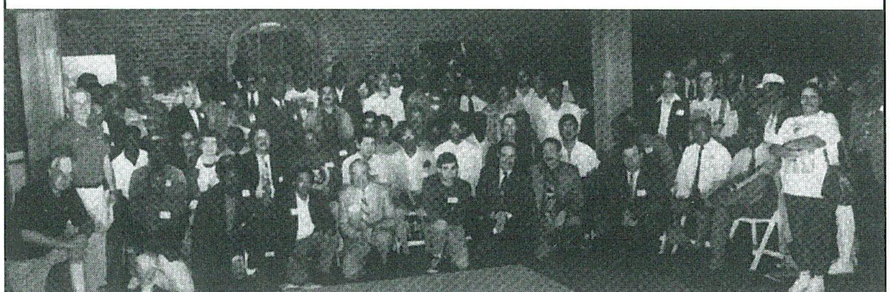

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