STATE OF CALIFORNIA GRAY DAVIS, Governor

DEPARTMENT OF INDUSTRIAL RELATIONS
DIVISION OF LABOR STANDARDS ENFORCEMENT
Santa Rosa Legal Section
50 D Street, Suite 360
Santa Rosa, CA 95404
(707) 576-6788

H. THOMAS CADELL, *Of Counsel*

June 13, 2002

Stuart MacLeod
525 Manhattan Ave., #B
Hermosa Beach, CA 90254

Re: **Commission Calculations**

Dear Mr. MacLeod:

Anne Stevason, Acting Chief Counsel of the Division, has asked me to respond on behalf of the Division of Labor Standards Enforcement to your letter of April 8, 2002.

In your letter you inquire regarding your employer's policy which provides:

> "Salespersons will be paid commissions on a monthly basis within thirty days from the last day of the month in which the commissions are earned. Commissions are earned on a monthly basis subject to the following guidelines:[¶]a) Each month 50% of the total of any invoice which has been transferred from 'Accounts Receivable' to the 'Reserve for Bad-Debts' account during the month will be deducted from the respective salesperson's commissions account.[¶]An invoice will be transferred to the 'Reserve for Bad-Debts' account at such time that the invoice has been unpaid for ninety days from the date of the invoice.[¶]If, and at such time, that an invoice which has been transferred to the Reserve for Bad-Debts' account is subsequently paid in full, fifty-percent of the total invoice amount of that invoice will then be credited to the salesperson's 'accrued commissions payable' account.[¶]b) Thereafter, the salesperson will receive a credit to his or her commissions account for invoices that are paid during a month pursuant to the following:[¶]Commissions will be credited to a salesperson's commissions account only after an invoice is paid in full.[¶]Commissions shall be equal to a percentage (determined by the officers of the company) of the gross profit earned on the sale, i.e., the difference between the sales price of the coffee sold and the cost of the coffee, including freight-in, determined on a FIFO (First-in, First-out) basis. [¶]Monthly commissions shall be deemed earned only after the total amount from paragraph a) is deducted from the amount in paragraph b), above. If the amount in paragraph a) exceeds the amount in paragraph b) the salesperson will have a negative balance on his or her commissions account until the next month.[¶]Upon termination of employment, salespersons shall be paid only those commissions earned within 30 days of the salespersons' termination date."

You state that your commission is 15% of the gross profit of the sale you have made. Your concern is that you are held liable for 50% of the entire invoice if that invoice is not paid. We would like to address that concern as well as other concerns we have with the commission plan.

It would be permissible for an employer to have a commission policy which provided that in the event that an account was not paid, the commissions paid on that account would be recovered from future commissions paid to the salesperson. However, to debit the salesperson for the cost incurred by the employer as a result of the default in payment is not allowed in California. In the case of *Quillian v. Lion Oil* (1979) 96 Cal.App.3d 156; 157 Cal.Rptr. 740, the court cited to established California law which recognized that "the employees, through the company's policy of deducting losses, were in effect made insurers of the employer's merchandise, and the commissions earned by the employees which were subject to the deduction, served the same purpose as an employee's "bond" exacted by the employer to cover shortages." (Citing *Kerr's Catering Service v. Department of Industrial Relations* (1962) 57 Cal.2d 319, 19 Cal.Rptr. 492, 369 P.2d 20) The *Quillian* court noted that "Deductions were made, therefore, for losses beyond the employees' control." Again, in the case of *Hudgins v. Neiman Marcus* (1995) 34 Cal.App.4th 1109, the California courts reached the same conclusion holding that "employees may not be made the insurers of business losses suffered by the employer".

Thus, based on the facts you present and the case law in California, it is the opinion of the Division of Labor Standards Enforcement that the California courts would find the deduction by the employer of 50% of the cost of the goods sold from earned commissions is illegal. (See Labor Code §§ 221, 224)

In addition, the provision in the commission policy which purports to limit the commissions earned by an salesperson to those earned within 30 days of the salesperson's termination may be, on its face, illegal as well. In the case of *Ellis v. McKinnon Broadcasting Co.* (1993) 18 Cal.App.4th 1796, the California court held a forfeiture clause in a written employment contract providing that upon termination, salesman shall only be entitled to commissions on fees collected through final date of actual employment was substantively unconscionable, even if salesman knew or should have known of the provision. The court found that the clause enured to the benefit of the employer, the party with superior bargaining power which inserted it in a standard form employment contract. The court found that the clause was void as a result of the provisions of California Civil Code § 1670.5 coupled with the historical protections afforded wages in this state.

The California courts have long held that commissions must be paid to salespersons who are the procuring cause of the sale regardless of the termination of the employment. (See *Watson v. Wood Dimension* (1989) 209 Cal.App.3d 1359; *Zinn v. Ex-Cell-O Corp.*

(1944) 24 Cal.2d 290; *Willison v. Turner Resilient Floors* (1949) 89 Cal.App.2d 589, holding that "He who shakes the tree is the one to gather the fruit")

We hope this adequately addresses the concerns you raised in your letter of April 8, 2002. Please excuse the delay in responding which is the result of many requests for opinions.

Yours truly,

H. THOMAS CADELL, JR.
Attorney for the Labor Commissioner

c.c. Arthur Lujan, State Labor Commissioner
Tom Grogan, Chief Deputy Labor Commissioner
Anne Stevason, Acting Chief Counsel
Assistant Labor Commissioners
Regional Managers