

Treble Damages and Other Dragons

Slaying the Sales Representative Commission Case

By Daniel N. Sharkey and Brent W. Warner



Imagine the following cocktail party conversation:

Manny: “What do you do?”

Sally: “I’m a sales rep.”

Manny: “Interesting. I’m in manufacturing.”

Sally: “Who are your customers?”

Manny: “ABC is our biggest customer, but we really would like to get into XYZ.”

Sally: “That’s a funny coincidence. I know the head of purchasing at XYZ.”

Manny: “Really? We should talk about whether you should rep us. I have nothing at XYZ now, so it couldn’t hurt.”

Sally: “I’ll call you next week to discuss your products and see what I can do.”

Now imagine the same two people several years later, this time in the manufacturer’s conference room:

Manny: “We have to let you go. You said your standard commission was 5 percent and we never questioned it, but we just can’t afford to pay you that much off the top anymore. We’re barely keeping our heads above water with XYZ.”

Sally: “Let *me* go? I got you into XYZ. Without me, you’d have 95 percent of nothing.”

Manny: “We’re here in the plant working every day to meet XYZ’s crazy quality standards, redesigning to its specification changes, and trying to meet its up-and-down release schedules. We haven’t even *seen* you in months—you’re out playing golf while we’re in here sweating.”

Sally: “Until I brought you XYZ, this plant was half empty. This is the thanks I get? You owe me commissions on the life of those parts. You’ll be hearing from my lawyer.”

This colloquy illustrates the tension at the heart of one of the most common types of commercial litigation: the sales representative commission dispute.

Michigan’s Sales Representative Commission Act

The Sales Representative Commission Act, enacted in 1992,¹ applies to principals and their sales representatives.² A *principal* is any entity that “produces, imports, sells or distributes a product” in Michigan or “[c]ontracts with a sales representative to solicit

orders for or sell a product” in Michigan.³ A *sales representative* is “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.”⁴ For simplicity, this article will refer to sales representatives as “reps.”

The purpose of the act is to ensure that reps are fully paid commissions earned under their agreements with principals, whether written or verbal.⁵ Under the act, all commissions due at termination of an agreement and those that become due must be paid to reps within 45 days after the date on which the commission became due.⁶

So far, simple enough, but here’s where things get dangerous for principals: the act imposes significant penalties on principals for failing to pay commissions when due. A principal found “to have intentionally failed to pay the commission when due” is liable to the rep not only for the unpaid commission, but also an additional penalty equal to the lesser of “2 times the amount of [unpaid] commissions” up to \$100,000.⁷ To meet the act’s requirement of an “intentional” failure to pay, which triggers the treble damages, a rep need not prove that a principal acted in bad faith; it need only demonstrate that the principal made a conscious decision not to pay a commission when it was owed.⁸ In that sense, the act is akin to a strict liability statute with treble damages—a scary combination for principals. In addition, if a rep files suit against a principal for commissions owed and prevails “on all the allegations of the complaint,” the principal will owe the rep its attorney fees and court costs.⁹

The terms of the contract between the principal and the rep determine when a commission is due.¹⁰ “If the time when the commission is due cannot be determined by a contract...the past practices between the parties shall control...”¹¹

Principals and reps cannot contract their way around the act’s penalty provision. The act makes clear that “[a] provision in a contract between a principal and a sales representative purporting to waive any right under this section is void.”¹² Because the act imposes heavy penalties on a principal that fails to pay commissions due, before termination a principal should review the terms of the parties’ agreement and determine what, if any, commissions are due as of termination and will become due after termination.

What does your sales representative agreement require?

As a threshold issue, the principal must understand the scope of commissions owed to the rep. Is the rep entitled to commissions on all sales from all the *customers* it procures for the principal, or is the rep entitled only to commissions on the individual *sales orders* in which the rep played an active role?¹³ In *Dietrich v Bell, Incorporated*,¹⁴ the Sixth Circuit recently highlighted the

importance of clearly distinguishing between *customer* procurement and *sales* procurement agreements:

[Principal] Bell incentivized [rep] Dietrich to procure new business contracts and did not incentivize him to sell anything to customers who had been with Bell for more than two years. This language would compel a salesperson to bring new accounts to his employer, which is the crux of the customer procurement model. In contrast, a sales procurement contract would typically incentivize sales without regard to the age of the customer relationship, as long as the salesperson was responsible for procuring the individual sale.

Where a manufacturer establishes a commission incentive program to reward procuring new accounts, pays the sales representative for only a limited time after the customer procurement as the award for procuring that account, and does not require the representative to personally book every sale, it creates a customer procurement arrangement.¹⁵

This distinction is crucial for principals that engage outside reps. They should clearly define whether the agreement is a *customer* procurement contract or a *sales* procurement contract and describe precisely any commissions that will be paid after termination.

Duration of the commissions after termination is another oft-litigated issue. From a principal’s perspective, a well-drafted rep agreement will limit the period in which a rep can recover post-termination commissions, either measured by time or conditioning them on the occurrence of an event that must take place before termination. For example, a provision limiting post-termination commissions may state that a rep is entitled only to commissions

FAST FACTS

If a principal fails to pay a sales representative, the Sales Representative Commission Act provides for treble damages up to \$100,000 and mandatory attorney fees.

Parties cannot opt out of the penalty provision by contract, but they can contract when commissions are due and how long post-termination commissions will be paid.

To minimize disputes, the parties should document their agreement regarding scope and duration of the commissions the sales representative will receive.

To meet the act's requirement of an "intentional" failure to pay, which triggers the treble damages, a rep need not prove that a principal acted in bad faith; it need only demonstrate that the principal made a conscious decision not to pay a commission when it was owed.

on sales that occur within 60 days of its termination. Or, a provision may condition post-termination commissions on sales arising out of release or shipment orders received and accepted by the principal before termination. Most reps, however, attempt to negotiate for "life of the part"—meaning that if the rep obtains the initial order of a part from a customer, the rep will be entitled to commissions as long as that part is sold to that customer. It is much less expensive to define and negotiate the duration of the commissions at the inception of the relationship than to litigate it later.

What if the agreement doesn't address post-termination commissions?— The procuring cause doctrine

While precisely defining rights and obligations is a wonderful concept, in our experience, the parties often fail to do so. An optimistic haze tends to pervade the honeymoon phase of rep relationships. The agreements are based on trust and handshakes and are often documented only on proverbial napkins, if at all; many are exclusively verbal agreements. These informal agreements rarely address post-termination commissions. In the absence of such definition by agreement, the procuring cause doctrine applies.¹⁶

The procuring cause doctrine states that a rep is entitled to a commission if he can show that his efforts were the procuring cause. This doctrine's roots stem from the 1958 case *Reed v Kurdziel*,¹⁷ in which the Michigan Supreme Court explained its purpose as "preventing a principal from unfairly taking the benefit" of the rep's services without compensation and imposing on the principal liability to the rep "for commissions for sales upon which the agent or broker was the procuring cause, notwithstanding

the sales made have been consummated by the principal himself or some other agent."¹⁸ The Court also explained that the doctrine includes post-termination commissions: "In Michigan the rule goes further to provide if the authority of the agent has been cancelled by the principal, the agent would nevertheless be permitted to recover the commission if the agent was the procuring cause."¹⁹ A half-century after the doctrine was established in *Reed*, however, no bright-line test has been established to determine if a rep is the procuring cause of a sale.

"Michigan cases...interpret the concept of 'procuring cause' quite narrowly."²⁰ To show that he is the procuring cause of a sale, the rep must have done more than simply introduce the customer to the principal.²¹ The rep must show that he was the "chief means, by which [a] sale was finally effected."²²

In 1990, in *Roberts Associates, Incorporated v Blazer International Corporation*,²³ which is often cited by subsequent decisions, the U.S. District Court for the Eastern District of Michigan held that obtaining the initial purchase order does not suffice to be deemed the procuring cause of subsequent sales if those sales resulted from additional servicing or negotiation not performed by the rep:

If subsequent purchase orders are submitted by a customer which involve no additional servicing or negotiation, then the salesman securing the original account may well be entitled to commissions on those sales. Of course, in the usual case each subsequent order will require some further customer services and under those circumstances the agent securing the previous order will have no claim for additional commissions.²⁴

In the generation since *Roberts*, the Sixth Circuit²⁵ and Michigan state courts²⁶ have reaffirmed its core holding: that if further sales or reorders resulted from additional negotiation or servicing not involving the rep, he is not entitled to a commission on those sales.

At least in the automotive context, purchase orders by themselves rarely guarantee principal manufacturers any future sales. Most purchase orders do not promise a specific quantity or even the buyer's requirements of products from the seller. And even if the customer agrees to purchase its requirements of products, the order's terms and conditions often allow the customer to terminate if the supplier's prices are no longer competitive. As a result, after the initial purchase order is issued, orders do not always continue to flow in on their own; additional negotiations are often required. To the extent that the rep was not involved in subsequent negotiations with the customer, the principal may have an argument that the rep's right to commissions ceased.²⁷

Conclusion and specific recommendations

- On the front end, ensure that the rep agreement (1) is reduced to writing, (2) details the rep's duties, (3) states whether the contract is a sales or customer procurement agreement, and (4) precisely addresses payment of post-termination commissions.

- If dealing with a rep who is located outside of Michigan or will be selling outside of Michigan, principals should consider a choice-of-law provision applying the rep's home state law if the law is less punitive toward principals.²⁸
- When severing relationships, rather than simply terminating, principals should, if possible, attempt to negotiate with reps a severance agreement detailing what, if any, post-termination commissions will be paid.
- A principal that is terminating a rep for breach should document and communicate that fact to the rep. A rep terminated for breach may not be able to recover under the procuring cause doctrine, or the principal may be able to assert a "first breach" defense to a claim for post-termination commissions.²⁹
- In defending post-termination commissions claims, outline a chronology of the business on which the rep seeks commissions, and analyze whether sales occurring under a purchase order initially obtained by the rep would have not occurred but for someone else's efforts with respect to servicing the account and maintaining the relationship with the principal's customer. ■



Daniel N. Sharkey is a co-founder of Brooks Wilkins Sharkey & Turco PLLC in Birmingham. He is past chair of the Commercial Litigation Committee of the SBM Business Law Section and has significant experience in automotive supply chain disputes, UCC issues, and sales rep commission disputes. Previously, he was a trial counsel in the U.S. Army Judge Advocate General's Corps, and a special assistant U.S. attorney.



Brent W. Warner is a member of Brooks Wilkins Sharkey & Turco PLLC. He has significant experience in automotive supply chain disputes, sales rep commission disputes, and drafting and negotiating supply and sales representative agreements.

ENDNOTES

1. MCL 600.2961. The Sales Representative Commission Act, while short enough to fit on a single page, has been criticized as less than clear. See, e.g., *Henes v Continental Biomass Industries, Inc*, 86 F Supp 2d 721, 728-729 (ED Mich, 2000) (calling it "one of the most haphazardly and inartfully drafted pieces of legislation that it has ever been called upon to review").
2. MCL 600.2961(1)(d) and (e).
3. MCL 600.2961(1)(d)(i)-(ii).
4. MCL 600.2961(1)(e).
5. *Linsell v Applied Handling, Inc*, 266 Mich App 1, 14; 697 NW2d 913 (2005) ("the Legislature included heavy penalties against violating principals to ensure that sales representatives in Michigan are paid the full commissions to which they are entitled"); *Kuzin v A&J Precision Tool Co, Inc*, unpublished opinion per curiam of the Court of Appeals, issued March 30, 2001 (Docket No. 217895) (the Sales Representative Commission Act does not require that the rep agreements be in writing).
6. MCL 600.2961(4).
7. MCL 600.2961(5).
8. *Waring v Total Mfg Systems, Inc*, unpublished opinion per curiam of the Court of Appeals, issued April 7, 2007 (Docket No. 261497) at *4.
9. MCL 600.2961(1)(c) and (6); see also *Peters v Gunnell, Inc*, 253 Mich App 211, 223; 655 NW2d 582 (2002) (a party cannot be a prevailing party "unless that party is found to have prevailed fully on each and every aspect of the claim or defense asserted under the SRCA.").
10. MCL 600.2961(2).
11. MCL 600.2961(3).
12. MCL 600.2961(8).
13. See generally *Lilley v BTM Corp*, 958 F2d 746, 751 (CA 6, 1992) ("Whether an agent is entitled to commissions on a customer procurement or sales procurement basis is determined by the contract..."); *Plam, Inc v Ind Tube Corp*, unpublished opinion of the U.S. District Court for the Eastern District of Michigan, issued November 15, 2006 (Docket No. 06-11015) (finding that an agreement requiring that the principal pay 3 percent to 5 percent on sales to new customers procured was a customer procurement agreement).
14. *Dietrich v Bell, Inc*, 554 Fed Appx 418 (CA 6, 2014).
15. *Id.* at 422-423.
16. *KBD & Assoc, Inc v Great Lakes Foam Technologies, Inc*, 295 Mich App 666, 673; 816 NW2d 464 (2012).
17. *Reed v Kurdziel*, 352 Mich 287, 294; 89 NW2d 479 (1958).
18. *Id.* at 294.
19. *Id.* at 294-295.
20. *Roberts Assoc, Inc v Blazer Int'l Corp*, 741 F Supp 650, 654 (1990), citing *Powers & Co v American Society of Tool Engineers*, 345 Mich 392; 75 NW2d 824 (1956).
21. See *William Kehoe Assoc v Indiana Tube Corp*, 891 F2d 293 (CA 6, 1989) ("[i]t is the acquisition of orders, not the acquisition of the customer that is protected by the 'procuring cause' doctrine").
22. *Kuzin*, n 5 *supra* at *4.
23. *Roberts*, n 20 *supra*.
24. *Id.* at 655.
25. See *Jack Peddie and Assoc, Inc v Whitmore Mfg Co*, unpublished opinion of the U.S. Court of Appeals, issued December 2, 1992 (Docket No. 92-1005) at *7 (the only exception to *Roberts* "is where reorders submitted by a customer involve no additional servicing or negotiation").
26. See, e.g., *Steinke & Assoc, Inc v Loudon Steel, Inc*, unpublished opinion of the Court of Appeals, issued March 16, 2006 (Docket No. 263362) (the rep was not entitled to post-termination commissions even though "additional work" and post-termination sales "spawned from the original purchase order," because the rep failed to show that it performed any work with respect to those particular sales).
27. Exclusive agency agreements are an exception to this rule. *Roberts*, n 20 *supra* at 654.
28. Before entering into a rep agreement, the principal should determine which state law will control and whether it includes penalties similar to the Sales Representative Commission Act. Many neighboring states now have similar laws in place to penalize a principal who fails to pay a rep commissions owed. See, e.g., Illinois (820 ILCS § 120), Indiana (IC § 24-4-7), Ohio (ORC § 1335.11), and Wisconsin (Wisc. Stat. § 134.93).
29. See *KBD*, n 16 *supra* at 676 (the customer banning the rep from its premises "could be considered a substantial breach of contract, in which case defendant would not be required to continue performing under the contract").