

LEGALLY SPEAKING

\$1 million award for fraudulent reduction of sales commissions



by Gerald M. Newman
ERA General Counsel

In the last issue of *The Representative*, we discussed an arbitration award of \$980,000, which a Florida sales representative, Electronic Assembly Supply Co., Inc. (EASCO), secured against its former principal, Nissei Sangyo America, Ltd. (NSA), on account of a fraudulent commission reduction. In this article, we will explain the primary arguments that EASCO used to persuade the arbitrators to find in its favor.

NSA had hired EASCO in January 1992 to serve as its professional sales representative in Florida, Puerto Rico and the Caribbean. EASCO steadily developed its territory, and by April 1994, it had become apparent that EASCO was about to secure a series of unusually large, multimillion dollar orders. NSA was concerned about the commission payments that would be due on these sales, so it requested that EASCO accept a commission reduction from 7 percent to 2 percent. EASCO refused.

Several months later, after it had actually received the pending orders, NSA, without prior discussion, sent EASCO a proposed contract modification, which would reduce the commission rate to 3 percent. NSA also withheld commissions due EASCO of approximately \$55,000.

Following telephone discussions, NSA promised that it would pay EASCO the past due commissions and also retain EASCO for another year as its sales representative if EASCO agreed to the rate reduction. NSA further promised that it would send EASCO a letter confirming the guaranteed retention if EASCO would sign and return the commission reduction letter. Based on these verbal promises, EASCO signed the letter. Instead of the 12-month contract guarantee and the back commission

payments, however, several days later NSA sent EASCO a letter of termination. Pursuant to a provision in the representation agreement, EASCO demanded arbitration with the American Arbitration Association. It sought the full 7 percent commission, plus attorneys' fees and punitive damages, under the Illinois Sales Representatives Act.

EASCO contended that the oral agreement to reduce its commissions was invalid, because it was fraudulently induced and because it lacked legal consideration (i.e., a benefit to EASCO). NSA raised three primary defenses. First, it claimed that the commission reduction was simply a response to competition and was therefore specifically allowed under the representation agreement. Second, it denied that it had ever promised to retain EASCO for an additional year and maintained that such a promise, if it had been made, would not be binding because it was not in writing. Third, it argued that only a court of law, as opposed to an arbitration panel, could award punitive damages.

EASCO met each of these arguments in turn. It disproved the "response to competition" defense through a careful analysis of NSA's internal accounting papers, which showed that, even with the full commission, NSA expected a greater-than-average profit on the pending sales. As to NSA's denial that it had promised to retain EASCO for at least 12 more months, EASCO's president testified that he had such a conversation and there would be no reason for EASCO to reduce its commission without a return benefit. Furthermore, although the representation agreement stated that it could only be modified in

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Leonard A. Nelson and Daniel E. Beederman, partners in Schoenberg, Fisher, Newman & Rosenberg, Ltd., co-authored this column.

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IN MEMORIAM

William C. "Bill" Hagaman

William C. "Bill" Hagaman, 62, of the Lindberg Company in Denver, passed away in July. He had been with the company since 1978. Donations in his memory can be made to Porter Care Hospice, 2465 S. Downing, #202, Denver, CO 80210.

MEMBER MOVES

- Andy Corrao has announced his retirement from Corrao Marsh Inc., in Fort Wayne, Ind. Although he will no longer be involved in the day-to-day operation of the company, he will continue to serve as chairman of the board and consultant. Steve Sliger joined the company earlier this year in an outside sales capacity.
- Rocky Mountain ERA headquarters has moved to new offices. The new address is: 6740 E. Hampden Ave., #306, Denver, CO 80224. Phone: (303) 756-5120; fax: (303) 756-5699.
- Scott Lindberg, president of the Lindberg Company, announced the appointment of Michael A. Mabbitt to the board of directors as vice president of sales. Mabbitt has been with the Lindberg Company, in Denver, since 1994.

- Bourns Inc., an ERA manufacturer member based in Riverside, Calif., promoted two sales managers to newly created positions in its sales organization. Patricia Moorman has been promoted to vice president, Bourns Worldwide Distributor Sales, and Graham Maggs has been promoted to manager, European Distributor Sales.

- James Griswold is the fifth Northport Engineering Inc., South Saint Paul, Minn., employee to complete Grayhill's correspondence course. The course covers basic electronics, switches and instruction on the application of the company's products. Grayhill is an ERA manufacturer member.

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writing, the controlling legal authority held that such restrictions are invalid. Finally, as to the arbitrators' power to award punitive damages, EASCO pointed to a series of decisions by the United States Supreme Court that expressly found that arbitrators have this authority.

Ultimately, the arbitrators restored the entire 7 percent commission to EASCO, and they awarded EASCO punitive damages and attorneys' fees. Although they did not state a basis for their decision, they probably concluded that NSA, when it promised to extend the representation agreement for another year, did not intend to keep its word. Such a finding would have supported EASCO's position that NSA had acted fraudulently, and it would also have justified the award of punitive damages.

Thus, although the usual rule is that an oral statement is insufficient to contradict a written agreement, the arbitrators found an exception. When the evidence shows that a party made a promise but never intended to keep its word, the promise may be considered fraudulent. In such a situation, that promise may be the basis for both compensatory (out-of-pocket) and punitive damages, notwithstanding the terms of the written document.

Editor's note: EASCO was represented by the law firm of Schoenberg, Fisher, Newman & Rosenberg, Ltd.

BETTER REPPING

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predict whether a person will work out. If you find you have made a mistake, the effect is somewhat minimized.

Whenever hiring, we made it clear that in 90 days, we would both review the progress. If satisfactory, the new employee would receive a raise. It was a rare exception for a new person not to remain and receive the raise. This reduced the negative effect on our principals if we made a mistake. It also helped ensure our financial investment.

In the next issue of *The Representor*, I will review more thoughts on the process of hiring the best people: the pitfalls, the questions and helping ensure the right decision.

These columns cover thoughts generated by more than 63 years in sales and marketing: 18 as a manufacturer, 28 as a rep and 17 doing seminars, sales training, teaching, management workshops, writing and publishing. And I am not through yet, although I have no plans to continue my career in the movies (and neither does the movie industry).

I want to cover areas such as selling, motivation, strategy, company public relations and consultants. Please give me your reaction to this plan. I am looking forward to being overwhelmed by hearing from my many wonderful friends. (Well, at least one or two.) Fax me at 310-472-4839, phone at 310-472-4039 or e-mail me at jackberman@aol.com.