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ERA General Counsel

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## LEGALLY SPEAKING

# Five reps settle claim against International Rectifier Corporation

Five sales rep organizations filed suit against International Rectifier Corporation (IR) for commissions owed and promises made (and subsequently broken) following IR's termination of the reps in the spring of 1999. The five rep plaintiffs had served IR for terms ranging from eight to 23 years.

The controversy started in May 1997, when, according to plaintiffs, in violation of the terms in its written sales reps contracts, IR decided to unilaterally reduce the commissions to be paid to its independent sales reps by approximately 40 percent. Not surprisingly, IR's decision caused substantial discontent among the sales reps, particularly given the substantial loss of income they faced as a result of IR's actions. This discontent raised serious concerns in the IR camp that they might lose a large number of their sales reps. Consequently, IR senior executives and the sales rep council entered negotiations in June 1997, continuing through August. As a result of these negotiations and meetings, IR proposed that a new sales rep contract be entered into, which incorporated the reduced commissions, but as a quid pro quo, provided extended probation terms and greatly enhanced post-termination commissions to the sales reps in the event of termination for reasons other than cause. It is believed that IR was willing to make these substantial concessions because it would not affect IR's current cash flow, and at the time the proposal and subsequent agreement were made, IR had no intention of terminating the reps, thus there would be no adverse financial consequences to IR.

Because of the importance of the contract changes, on September 18, 1997, a meeting was held between IR and the owners of rep firms near IR's headquarters in El Segundo, Calif. During the owners' meeting, senior IR executives explained the new contract terms and passed out copies of the new

terms to the rep firm owners.

In general, IR promised that with respect to post-termination commissions for terminations due to reasons other than cause or non-performance, a sales rep who had been with IR for more than three years (which included each of the five rep plaintiffs) would receive "one year's full commission or one month's commission for every year, whichever is greater."

The sales reps understood this to mean that if they were terminated for reasons other than cause or non-performance, they would receive post-termination commissions as outlined in IR's presentation based upon the average monthly commissions they had earned prior to termination. Thus, if a sales rep was terminated and had been paid commissions of \$480,000 over the previous year (or an average of \$40,000 a month), if the sales rep had been with IR for 20 years, that sales rep would be entitled to post-termination commissions of \$800,000 under the terms of the new agreement promised by IR at the September 1997 meeting.

Because IR agreed to the extended probation period and the enhanced post-termination benefits, the sales reps agreed to the reduction in commissions requested by IR. As a result, IR promised to send out revised sales rep contracts that incorporated the new terms that had been agreed upon. Unfortunately, despite numerous requests by the sales reps (including the rep plaintiffs), new contracts with the terms agreed upon during the September 1997 meeting were never sent. In fact, IR delayed the new contract for more than 15 months. During that period of time, IR hired a new vice president of sales, who sent out a new contract that did not include any of the enhanced post-termination commission terms that IR had agreed to previously. A memo from the new VP of

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sales that accompanied the new contract stated, "Promises that were made some time ago, based upon the current market, are unfortunately just not going to be manageable for IR at this point in time." In the memo, IR admitted that it had made promises to the reps and had failed to comply with the September 1997 agreement.

Not long after that memo, IR sent terminations L.D. Lowery (Broomall, Penn.), M-Squared, Inc. (Raleigh, N.C.), NRG, Ltd. (Bridgeport, Conn.), and R-Theta Sales (Mississauga, Ontario, Canada). Several months later, IR notified Kinetic Sales, Inc. (Sanford, Flor.) that it would not be renewing IR's contract when it expired on April 15, 1999. The notices provided no basis for termination, and IR never claimed that any plaintiff was terminated for cause or non-performance.

As a result of IR's actions, the plaintiffs filed four separate lawsuits in Philadelphia, Penn., Raleigh, N.C., Hartford, Conn., and Orlando, Flor. (because R-Theta is a Canadian corporation, its claim was filed in the Philadelphia action). The underlying claim of each of the five rep plaintiffs was based on IR's unilateral reduction in commissions and failure to pay the enhanced post-termination commissions. It was the plaintiffs' position that IR was liable to them for either the enhanced commissions upon termination agreed upon during the September 1997 meeting, or the full amount of commissions payable under the sales rep contracts prior to IR's reduction of commissions, which began in July 1997. The rep plaintiffs urged the court that IR could not have it both ways; it was not entitled to the benefit of the reduced commissions without paying the enhanced post-termination commissions, or IR was liable to the plaintiffs for the full amount of commissions at the contract rate being paid prior to July 1997. From a practical standpoint, for most of the rep plaintiffs, the commissions payable under each scenario were approximately the same.

The plaintiffs also made a claim under the California Salesman Protection Act, as well as claims for fraud, misrepresentation, violation of various state business practice acts, etc.

IR's defense: It had the right to unilaterally reduce commissions without the consent or approval of the reps, notwithstanding that in the past, each and every commission change was accompanied by a written supplement to the contract; IR did not make any promises to the reps during the September 1997 meeting, but merely put a number of proposals on the table for discussion and negotiation, including the concept of enhanced post-termination commissions; and if there was a promise for post-termination commissions, it only related to "shippable backlog" and was not to be computed on an average of commissions paid during the previous year. The plaintiffs contended that using shippable backlog as a standard was meaningless since most of the backlog was shipped within 90 days, far less than the 23 months of average post-termination commissions for a company like Kinetic Sales (which was an IR rep for 23 years).

After an enormous amount of discovery, exchange of thousands of pages of documents, depositions in Chicago, California, Florida, Connecticut, North Carolina and Pennsylvania, and several mediation attempts, the Pennsylvania case went to trial on February 23, 2001. After less than two days of hearings, upon the recommendation of the trial judge, IR entered into a "global" settlement agreement with all of the five rep plaintiffs. Under the agreement, the terms and amount of the settlement must be maintained in confidence.

In retrospect, the rep plaintiffs on the rep councils should have put more pressure on IR to submit the new contracts with the enhanced post-termination provisions. They probably did not want to pressure IR, out of concern for the relationship, and assumed that IR would do the right thing. IR should not have unilaterally reduced the reps' commissions and then misrepresent to the reps that they would be receiving new contracts with the extended probation period and the enhanced post-termination commissions.

The five rep plaintiffs were represented by Gerald M. Newman and the law firm of Schoenberg, Fisher, Newman & Rosenberg, Ltd. (Chicago, Ill.), and by David A. Axelrod.