



## One Minute Memo<sup>®</sup>

# Commission Wages Based Upon the Number of Products or Services Sold May Be Exempt From California Overtime Pay Requirements

Section 3(D) of various California Wage Orders provides an exemption from the daily and weekly overtime requirements for employees who earn at least one and one-half times the minimum wage and whose pay is mostly in the form of “commissions.”

On May 20, 2011, in *Areso v. CarMax, Inc. et al.*, the California Court of Appeal held that compensation based proportionately on the number of products or services sold constituted “commissions” for purposes of qualifying for the commissioned sales exemption.

## Case Background

CarMax sells used vehicles, warranty plans, used vehicle appraisals, and vehicle accessories. Former CarMax employee Leena Areso filed a class action complaint against CarMax, alleging it failed to pay overtime wages and violated other provisions of the California Labor Code.

CarMax classified Areso as a “commissioned exempt salesperson.” Her primary job was selling CarMax products and services. Areso received a minimum guaranteed base pay, but was not paid overtime. She also received wages pursuant to CarMax’s “National Pay Plan,” which provided for a uniform dollar payment for each sale of a vehicle, lease, appraisal purchase, or extended service plan. She also earned ten percent of the purchase price of any accessory sold. In 2005, CarMax implemented a “California Pay Plan.” Under this plan, Areso earned wages pursuant to a formula which accounted for the number of products and services sold, but that resulted in a uniform payment per product or service sold.

Areso sued CarMax for unpaid overtime compensation. CarMax contended Areso was exempt from overtime pursuant to the “commissioned sales exemption” in Industrial Welfare Commission Wage Order No. 7. Section 3(D) of the Wage Order exempts employees whose “earnings exceed one and one-half (1 1/2) times the minimum wage [and] if more than half of that employee’s compensation represents commissions.” The Wage Order does not define the term “commissions.” Areso argued that her payments under the National Pay Plan and the California Pay Plan could not qualify as “commissions” because they were not based on a percentage of the value or price of the product or service sold.

The trial court granted CarMax summary adjudication on the ground that payments under both the National Pay Plan and the California Pay Plan were in fact “commissions.”

## The Appeal

The Court of Appeal affirmed, finding that wages based proportionately on the *amount or number* of property or services sold by an employee constitute commission wages.

The court rejected Areso's argument that wages must be based proportionately upon the *value* of the property or services sold to be considered "commission wages." Instead, as an issue of first impression, the court held that section 204.1 of the Labor Code, which creates an exception for automobile dealers allowing them to pay commission wages only monthly, expressly allows wages based on the amount or number of items sold to be considered commission wages.

Based on this interpretation of section 204.1, the court also rejected Areso's claim that *Keyes Motors Inc. v. Division of Labor Standards Enforcement* (1987) 197 Cal.App.3d 557 and *Ramirez v. Yosemite Water* (1999) 20 Cal.4th 785 limited the definition of "commission" to one that was calculated as a percentage of the selling price. The court concluded that the section 204.1 definition of commission is much broader than a straight percentage of selling price and held that the "percentage" language in *Keyes* was dictum. The court held that a "commission" can be proportionate to the amount – or units – of sales, independent of the price paid by the customer.

CarMax's payment plans, which provided for uniform payments based on the number (i.e., amount) of items or services sold, constituted commission wages within the meaning of section 204.1 for purposes of the commissioned sales exemption.

## What Areso Means For Employers

For purposes of assessing whether an employee satisfies the commissioned sales exemption, wages paid based proportionately upon the number of products or services sold by an employee should qualify as "commissions" even if the commission is not based on the revenue derived from these sales. Although the application of Labor Code section 204.1 appears to be limited to vehicle dealers, the Supreme Court in *Ramirez* held that the definition of section 204.1 applies generally, not just to vehicle dealers, so the reasoning of this case also should apply to employees of other businesses.

Employers also should keep in mind that the federal Fair Labor Standards Act has a similar exemption, but it applies only to employees employed by a retail or service establishment. Therefore, it is possible that a commissioned employee could be exempt from daily and weekly overtime requirements under California law, but not be exempt from weekly overtime requirements under the FLSA. (The FLSA has no daily overtime requirement.)

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