

L a b o r & E m p l o y m e n t
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2008NEW YORK COURT OF APPEALS OUTLINES
PROTECTIONS AFFORDED TO EXECUTIVES UNDER
THE NEW YORK LABOR LAW

After more than a decade of disagreement between New York's state and federal courts on whether executives are covered by Article 6 of the New York Labor Law, a resolution is at hand. On certification from the Court of Appeals for the Second Circuit, the New York Court of Appeals held that executives are "employees" who are protected by section 193 of the Labor Law. *Pachter v. Bernard Hodes Group*, 2008 N.Y. Slip Op. 05300 (June 10, 2008) Section 193 forbids employers from deducting unauthorized sums from employees' earned "wages." The Court also declared that where executives are compensated on a commission basis, whether and when those commissions are considered earned "wages" and not subject to deductions under the Labor Law is regulated by the agreement of the parties. That agreement may be express or implied, or, in the absence of any agreement on the question, by default common law.

Background

Between 1992 and 2003, Elaine Pachter was employed as a vice-president with Bernard Hodes Groups, Inc., a recruitment marketing and staffing services company. Pachter chose to be compensated on a commission basis, which allowed her to earn significantly more money

annually than she would have earned in salary. Pachter's commission earnings were calculated using a formula that credited Pachter with a fixed percentage of the amounts she billed to clients, minus specified business costs associated with those clients. The deductions included finance charges for late payments, uncollectible debts and travel and entertainment expenses. Pachter received a monthly commission statement that enumerated her gross commission – the fixed percentage – and all business expenses attributed to her activities. The expenses were deducted from her gross commission to yield her net compensation for that period. Pachter knew of and consented to Hodes' use of this compensation scheme throughout her employment.

After leaving her employment in 2003, Pachter sued Hodes in federal court, asserting that Hodes was prohibited by Labor Law section 193 from deducting business expenses from her gross commissions. The district court ruled in favor of Pachter, holding that executives are covered "employees" under Article 6 of the the Labor Law, and therefore, the adjustments made by Hodes were illegal deductions from wages under section 193.

On appeal, the Second Circuit Court of Appeals observed that federal and state courts repeatedly had

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reached conflicting conclusions on these issues. It therefore certified two questions of law to the New York Court of Appeals: (1) whether an executive is entitled to the protections extended to employees under Article 6 of the Labor Law, and, (2) if so, when, in the absence of a written agreement between an employer and employees, is a commission “earned” and becomes a “wage” subject to the prohibition against deductions under section 193 of the Labor Law.

New York Court of Appeals’ Decision

Answering the first question based on the wording and format of the statute, the New York Court of Appeals found that the definition of an “employee” in Labor Law section 190 – “any person employed for hire by an employer in any employment” – must have been intended to embrace executives. Addressing the second question, the Court held that the legality of Hodes’ adjustments to Pachter’s gross commission depended on when the commission was “earned,” becoming a “wage” subject to the restrictions in section 193. As the Labor Law does not provide an answer the Court looked to the common law rule that a broker’s commission is earned when he produces a person “ready and willing to enter into a contract upon his employer’s terms.” The Court also looked to contract law rules under which “parties to a transaction are free to depart from the common law by entering into a different arrangement.”

Applying these principles, the Court found that, while there was no written contract, evidence of the parties’ prior course of dealings led to an implied contract under which the final computation of Pachter’s commissions, before they could be earned, required Hodes to adjust for specified business costs. Thus, nothing in Article 6 precluded the compensation scheme agreed upon by Hodes and Pachter.

The Significance of the Decision

While bringing welcome clarity, the extension of the protections of Article 6 to executives cannot help but encourage more executives to bring claims for unlawful deductions. On the other hand, employers should welcome the assurance of the Court of Appeals that their contractual arrangements with executives and others paid on a commission basis ordinarily will be enforced. The opinion is clearly warning employers to make sure commission plans and agreements are in order. Its direction, that common law rules will dictate when gross commissions become non-forfeitable wages if no express or implied contract reserves the right to make adjustments after the period closes, will mean some employers will be unable to make fair adjustments lawfully. Under *Pachter*, that result is completely avoidable – if employers will help themselves. ♦

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