iGLOBAL LAW™
GLOBAL LABOUR LAW

iGlobal Strategic Guidance Series 2: Employee Compliance

(2) Commission and incentive plans

Many US-based multinationals take a global one-size-fits-all approach to their annual or quarterly commission and incentive plans. Their aim, understandably, is to keep things simple. However, this approach can result in the business having to make significant additional payments to its overseas employees under local country rules, particularly on terminations of employment.

We outline some of the main pitfalls and points to consider and suggest a best practice approach to structuring your worldwide commission and incentive plans.

A global approach?

The typical global incentive plan of a US corporation will be drafted by US legal, governed by the laws of the state in which the company is based and distributed in essentially the same form to both the domestic and international senior workforce. For American employees, the plan will likely function as intended: plans are often discretionary and designed to give employers maximum flexibility. But will that approach work for those employed overseas?

In some jurisdictions, all employment terms and conditions are automatically governed by local law for employees working in that country. This can apply to documents that state they are not contractual, like a bonus or commission plan where the plan itself says it is wholly discretionary and non-contractual. Where local law automatically creates a contractual right to participate in a bonus or commission scheme it is very hard, and often impossible, for companies to apply discretion, or even to amend or revoke incentive entitlements in the future.

In addition, many jurisdictions, particularly those in western Europe, have developed sophisticated and usually very pro-employee case law on bonus and commission payments and workers' entitlements. This can mean that much of the plan's written rules are not the rules that will actually apply.

Impact of local rules

Examples of these kinds of overriding local rules include:

- Obligation to pay employees 100% bonus during sick leave (example: Netherlands)
- Entitlement to 100% commission when on garden leave during notice (example: Germany)
- Obligation to pay employees pro rata for bonus or commission where they only part-complete the financial year or quarter (numerous jurisdictions);
- Obligation to pay employees extra money in lieu of commission when they take vacation, so that they are no worse off by taking vacation than if they had worked the time (example: United Kingdom)
- Being unable to withhold bonus or commission where an employee is involved in an unrelated disciplinary matter or subsequently needs to be performance managed (example: Spain)
- Obligation to make payments by a specific time in order to avoid breach of contract claims (example: Italy)
- Denial of provisions that allow employers to withhold payment where an employee leaves their job after the end of the reference period but before the payment date (example: France)
- Certain rules on leave of absence common in US plans could be deemed discriminatory towards those who are disabled or on maternity leave in some countries (numerous jurisdictions)
- Issuing a plan late, i.e. after the start of the applicable financial year or quarter, may entitle the employee to 100% bonus or commission for the period when he/she did not have a plan – as employees cannot be expected to perform to targets they have not been set
- Changing the plan and the targets during the year may be possible in a lot of jurisdictions, but many do not allow the change to have retrospective effect because the employees have already provided performance based on the previous plan rules (numerous jurisdictions)
- Clawing back overpayments can be extremely hard, resulting either in costly litigation where it is possible at all or the intervention of local labour laws which prohibit it entirely (many jurisdictions)
- Obligation (depending on the wording of the documents) to pay employees continuing commission for a period of time if they have been materially involved in winning a client (example: Switzerland)

Contractual rights

Contractual rights can further complicate matters where the employer wants to change the structure of an incentive plan, particularly where that change is negative for the employee.

For instance, where an employee is moved to another customer account and it is harder to earn as much commission on the new account; or if the local employer subsidiary's business declines, reducing the budget to offer such generous commission entitlements; or, conversely, a product has become far easier to sell because it has reached the maturity stage of its life cycle and commission needs to be reined in.

Failure to foresee and plan for these issues beforehand can make it difficult to legally amend the structure of a plan, in some jurisdictions, without the employee's express consent. Getting consent will not be easy if the employee is likely to be financially worse off.

Possible workarounds

While it may add administrative burden and some upfront cost, employers can achieve significant longer term cost savings if they issue a new plan each year (and for some businesses even each quarter) and then keep those plans under review on a jurisdiction-by-jurisdiction basis so as to maximise business flexibility.

Many jurisdictions allow for some flexibility in the plan to deal with the issues raised above but this often involves amending the plan with very specific wording for that jurisdiction, requiring a more localised document.

Some jurisdictions allow local employees to operate under incentive plans governed by a foreign law without local law automatically taking precedence. Therefore, it may be possible to adjust existing company documentation or practices to increase the chance of US law continuing to govern the commission arrangement.

However, there are many pitfalls to be aware of and the traps vary by country. Examples that could result in local law applying regardless of what the plan actually says include any reference to it in the local law employment contract or in an offer letter issued by the local subsidiary, or if payments under the plan are made to the employee via the local subsidiary rather than the US parent company which issued the plan.

Any ambiguity will usually be interpreted by local courts against the employer and in favour of the employee: the majority of Latin American and Continental European courts are very pro-employee, as are those in Japan, India, China and Russia.

Commercial considerations

- **Taking a one-size-fits-all approach.** This might involve trying to impose a US drafted plan consistently worldwide or alternatively basing your global plan on the most employee friendly and regulated jurisdiction in your network. Both have drawbacks and are likely to cost you more. In the former case you may inadvertently take on costs that could have been avoided at local level (as discussed above) and in the latter case you may voluntarily sign up to pay more than the local rules actually require. For example, while Brazilian labour law imposes many restrictions on an employer's right to be flexible in structuring its incentive plans, Singapore or Hong Kong do not. If you take the latter approach, you should consider carving out these jurisdictions whose laws are less restrictive so as to get maximum benefit from the less regulated environment.

- **Cultural impact of comparative entitlements.** Local labour laws may mean that in two identical scenarios an employee in one country may qualify for a payment, while an equivalent employee in a different jurisdiction may not. For example, a carefully drafted plan stipulating that an employee only receives their calendar year 2017 payment if still employed (and not under notice) at the payment date in 2018 may be upheld in Singapore but be void in France such that the employee remains fully entitled.

- **Should employees around the globe be entitled to the same commission for equivalent performance?** Typically (although not always) those jurisdictions that offer more business flexibility are also the countries where employees are required to pay less (or even no) tax on their awards. A gross commission award of US$50,000 may see a salesperson in Germany declare approximately half of the figure to income tax and other charges, whereas a colleague working in Dubai would keep the entire amount. Factor in the cost of living in a given location as well and the same US Dollar award in gross terms may provide very different levels of incentive to your workforce around the globe.

  On the other hand, employees in the higher tax jurisdictions in Latin America or Europe typically enjoy much better employment protection than their colleagues in the USA, Hong Kong or Singapore. This will impact on compensation received on termination, including in some cases on commission payments.

Suggested best practice approach

- Map at high level the relevant rules on commission/incentive entitlements, flexibility, timings and documentation for your countries of operation.
- Prepare a global plan template building the basic framework for your incentive scheme covering timetables, qualifying employee grades, calculation mechanisms and entitlements.
- Decide whether as a matter of policy you wish to maximise global consistency or minimise local cost and risk.
- If your preference is to minimise local cost, make the necessary scheme adaptations at local level to achieve maximum flexibility and cost/risk control in accordance with that country's rules. One option is to keep the plan consistent globally and then have a localised section on the key provisions specific to that jurisdiction.
- If your preference is to keep the plan global, you could simply add the general caveat that the plan operates subject to local laws but understand in advance the risks of this approach.
- As an alternative, you can adopt a hybrid approach where the plan is implemented consistently in those jurisdictions where it can work under US law or where local laws are not restrictive and make local adjustments in countries where it is wise to do so in order to minimise your liabilities.

iGlobal Law
71 Queen Victoria Street
London
EC4V 4AY

T: +44 (0) 20 7406 1639
E: info@igloballaw.com
www.igloballaw.com

We would welcome your feedback:
Please contact Karen Mosley
karen.mosley@igloballaw.com

Global labour and compliance law solutions for multi-national employers

This publication is for general information only and does not seek to give legal advice or to be an exhaustive statement of the law. Specific advice should always be sought for individual cases. iGlobal and iGlobal Law are the trading names of WB Global Limited which is a private limited company registered in England and Wales with number 8181382 at registered address 71 Queen Victoria Street London EC4V 4AY and is authorised and registered by the Solicitors Regulation Authority. This reflects the law as at the date of publication, December 2017. Produced by PWM