SUPERIOR COURT
OF THE
STATE OF DELAWARE

T. Henley Graves
Resident Judge

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Date Submitted: August 28, 2003

RE: ***Patrick J. Montague and Gregory C. Carson v. Seacoast Realty, Inc., Celeste B. Valliant, and John O. Valliant***
C.A. No. 01C-10-021

Dear Counsel:

Patrick J. Montague and Gregory C. Carson ("Plaintiffs") filed a Motion for Summary Judgment against their employer Seacoast Realty, Inc., and its owners Celeste B. Valliant and John O. Valliant, (collectively, "Seacoast"). Seacoast contested the Motion and filed a Cross-Motion for Summary Judgment. This is the Court's decision.

Factual Background

Plaintiffs were engaged by Seacoast as real estate sales agents or associates. Plaintiffs signed a document entitled "Independent Contractor Agreement Between Seacoast Realty & Salesperson" ("Agreement"), which details the terms of Plaintiffs' association with Seacoast. Pursuant to this agreement, Plaintiffs' sole source of income is a percentage of the commission paid to Seacoast from the sale of real estate. The Agreement incorporates by reference a

"Commission Schedule," which sets forth the guidelines for determining what percentage of a given commission Plaintiffs are entitled to receive. This percentage is a function of the agent's year-to-date earnings and the type of sale.[1] The Commission Schedule is part of a larger document entitled, "Compensation Policy."

On October 25, 2000, Seacoast discharged Plaintiffs. At the time of termination, the two sales agents had facilitated sales for twelve properties that had yet to proceed to closing. Seacoast does not dispute that Montague and Carson had secured ready, willing, and able buyers for each of these properties before they were fired. "Ratified contracts" were in place but the sales had not yet proceeded to settlement.

Plaintiffs contend they are entitled to receive their full commissions for these pending transactions. Pursuant to the Commission Schedule, Montague was entitled to receive additional commissions at Level 12. Carson was entitled to receive additional commissions at Level 13. Seacoast relies upon a clause contained in Seacoast's "Compensation Policy" that permits Seacoast to pay terminated agents at a lower level (Level 1) for "pending" transactions. Accordingly, Plaintiffs allege that Montague received $20,773.99 less than he was entitled to be paid and Carson received $26,811.86 less than he had earned.[2]

Originally, Plaintiffs contended that they had been wrongfully terminated. They have since abandoned this claim. *Plaintiffs' Opening Br.* at 15 n. 8. Plaintiffs do, however, challenge

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[1] The type of sale depends upon whether Seacoast was the listing agent, the selling agent, or both.

[2] Seacoast agrees that initial calculations at the Level 1 rate were erroneous and that Montague is due another $1,590.87 and Carson is owed an additional $1,224.22.

the validity and applicability of the commission reduction clause contained in the Compensation Policy. Specifically, Plaintiffs present two arguments for consideration:

1. Does the Wage Payment and Collection Act prohibit the forfeiture of earned commissions?
2. In the alternative, did Seacoast's attempted forfeiture of Plaintiffs' earned commissions constitute a breach of contract and/or a breach of the covenant of good faith and fair dealing, including a claim that the commission reduction clause was punitive?

Seacoast has filed a Cross-Motion for Summary Judgment, alleging that it is entitled to summary judgment because: (1) Plaintiffs were independent contractors and therefore the Wage Payment and Collection Act does not apply, and (2) Plaintiffs' commissions were earned but not accrued when they were terminated, and thus, the terms of the Independent Contractor Agreement apply.

Motion for Summary Judgment

A. Standard of Review

This Court will grant summary judgment only when no material issues of fact exist, and the moving party bears the burden of establishing the non-existence of material issues of fact. *Moore v. Sizemore,* 405 A.2d 679, 680 (Del. 1979). Once the moving party has met its burden, the burden shifts to the non-moving party to establish the existence of material issues of fact. *Id.* at 681. Where the moving party produces an affidavit or other evidence sufficient under Superior Court Civil Rule 56 in support of its motion and the burden shifts, the non-moving party may not rest on its own pleadings, but must provide evidence showing a genuine issue of material fact for trial. Super. Ct. Civ. R. 56(e); *Celotex Corp. v. Catrett,* 477 U.S. 317, 322- 323 (1986). If, after

discovery, the non-moving party cannot make a sufficient showing of the existence of an essential element of his or her case, summary judgment must be granted. *Burkhart v. Davies,* 602 A.2d 56, 59 (Del. 1991), *cert. denied,* 504 U.S. 912 (1992); *Celotex Corp.*, *supra*. If, however, material issues of fact exist, or if the Court determines that it does not have sufficient facts to enable it to apply the law to the facts before it, summary judgment is inappropriate. *Ebersole v. Lowengrub,* 180 A.2d 467, 470 (Del. 1962).

In the event that parties file cross-motions for summary judgment, "the parties implicitly concede the absence of material factual disputes and acknowledge the sufficiency of the record to support their respective motions." *Browning-Ferris v. Rockford Enters*., 642 A.2d 820, 823 (Del. Super. 1993).

B. Applicability of the Wage Payment & Collection Act

The Wage Payment and Collection Act ("the Act") requires terminated workers to be paid promptly, regardless of fault or just cause, and assesses penalties against employers who unreasonably fail to do so. The relevant statute reads:

> (a) Whenever an employee quits, resigns, is discharged, suspended or laid off, the wages earned by the employee shall become due and payable by the employer on the next regularly scheduled payday(s) either through the usual pay channels or by mail, if requested by the employee, as if the employment had not been suspended or terminated.
> (b) If an employer, without any reasonable grounds for dispute, fails to pay an employee wages, as required under this chapter, the employer shall, in addition, be liable to the employee for liquidated damages in the amount of 10 percent of the unpaid wages for each day, except Sunday and legal holidays, upon which such failure continues after the day upon which payment is required or in an amount equal to the unpaid wages, whichever is smaller, except that, for the purpose of such liquidated damages, such failure to pay shall not be deemed to continue after the date of the filing of a petition of bankruptcy with respect to the employer if the employer is adjudicated bankrupt thereupon. An employer who is unable to prepare the payroll due to a labor dispute, power failure, blizzard or like weather

> catastrophe, epidemic, fire or explosion shall not be deemed to have violated this chapter.

19 *Del. C.* § 1103.

In order for the Act to apply, the person seeking relief must be an "employee" as defined by 19 *Del. C.* § 1101(a)(4). That is, an employee must be a person "suffered or permitted to work by an employer under a contract of employment . . . ." *Id.* As the Supreme Court has noted, "[t]hat definition is of little help . . . ; apparently, the Legislative intent was to leave it to the Courts to decide, in any given case, whether a person is or is not an employee." *Fairfield Builders, Inc. v. Vattilana*, 302 A.2d 58, 60 (Del. 1973).

The question of the existence of an employer-employee relationship is an issue of law that turns on the facts and circumstances of the particular case, with no single element being decisive. *Gooden v. Mitchell*, 21 A.2d 197 (Del. Super. 1941). For purposes of applying the Act, however, two cases have provided guidance by condensing the Supreme Court's discussion in *Fairfield* into a three-part analysis, focusing on: "(1) whether the employer retained control over the means and methods of doing the work; (2) whether the person was taxed like an employee; and (3) whether other benefits consistent with a standard employment contract were provided." *Kutney v. Saggese*, 2002 WL 1463092 (Del. Super.) at *1; *Rypac Packaging Mach. Inc. v. Coakley*, 2000 WL 567895 (Del. Ch.) at *13.

Plaintiffs contend first, that the independent contractor analysis embodied in the Second Restatement of Agency is the proper methodology the Court should use in considering Plaintiffs' status; and second, that case law from other jurisdictions finding real estate agents to be employees is persuasive.

First, the Delaware courts have embraced the Restatement test, while distilling it differently under various circumstances. The test has been simplified to consist of four considerations in the workers' compensation statute context. *See Loden v. Getty Oil Co.*, 316 A.2d 214, 216 (Del. Super.), *aff'd* 326 A.2d 868 (Del. 1974). Likewise, the courts have chosen to focus their analysis on the factors enumerated in *Kutney* in the wage collection context.

Second, while some of the cases cited by Plaintiffs are intriguing, it is not necessary to look for guidance from other jurisdictions. The Court's decision in this case turns on the analysis set forth in *Fairfield*, *Kutney*, and *Rypac*.[3]

The parties agree that there is no dispute as to the material facts concerning the Plaintiffs' relationship with Seacoast. The Court concludes that Plaintiffs are independent contractors as a matter of law.

In the first instance, it is significant to examine the terms of the contract governing Seacoast's association with Plaintiffs. Although the formal contract may not indicate the relationship which existed in actual practice between the parties, "it should be examined and given its proper weight." *Loden v. Getty Oil Co.*, 316 A.2d at 217. Plaintiffs' contract with Seacoast states the parties "agree that [Plaintiffs are] independent contractor[s] and not [] partner[s] or employee[s] of [Seacoast]." *Agreement* at p. 3 ¶ 7. In addition, a paragraph, set

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[3] Seacoast argues that the *Kutney* and *Rypac* decisions have served to eliminate all considerations in an independent contractor analysis that do not fall within the three criteria set forth therein. I disagree. The Court in *Kutney* specifically referenced case law in different areas when considering the plaintiff's employment status. For example, the court noted that whether a worker provides his own instrumentalities is a factor to consider when determining whether one is an independent contractor. The case cited for that proposition was based on master-servant law and accompanying tort liability. While the *Kutney* criteria embrace the factors set out in the Restatement of Agency, the Court may take other considerations into account.

apart from the rest of the contract and separately acknowledged by way of signature, specifies that Plaintiffs shall not be treated as employees for Federal Tax purposes. *Id*. at p. 4.

Turning to a consideration of the *Kutney* criteria, the issue that requires the greatest discussion is that of control. *See Fairfield*, 304 A.2d at 60-61 ("Most importantly, [defendant] retained no power of control over the means and methods of doing the work . . . ."). Plaintiffs allege that Seacoast had such control over their means and methods of conducting a sale that Plaintiffs were employees as contemplated by the Act. In support of this theory, they cite to the following:

1. On Friday mornings, Seacoast real estate sales agents were encouraged to attend the weekly sales meeting. At this meeting, new listings are introduced and tours of the properties encouraged. The meeting is an important one to attend, if one desires to acquire commissions from new sales. Ms. Valliant cited Carson's failure to attend the meetings as a sign of an "underlying problem."
2. Sales agents send out mailings in an effort to facilitate sales and boost revenue. All mailings were subject to Ms. Valliant's approval.
3. Seacoast asks that sales agents take turns covering the office, in order to handle walk-ins, model homes, and cold calls, among other issues. Seacoast sets up a schedule and assigns hours to the sales agents. If a sales agent is unable to work, he is responsible for ensuring that another agent will cover for him.
4. Seacoast forbids sales agents from negotiating commissions on its behalf.
5. Seacoast has several rules that its agents must follow concerning office maintenance and an agent's physical appearance.

The facts that support a finding that Seacoast does not control the means and methods of Plaintiffs' work may be summarized as follows:

1. All licensing, registration, and membership fees associated with the realty organizations with which Plaintiffs were required to be affiliated were borne by Plaintiffs.
2. Plaintiffs were not required to work a minimum number of hours, nor were they required to work a set schedule. Plaintiffs were not required to attend the weekly meetings, nor were they required to work pursuant to the office schedule if they were able to find a replacement.
3. Plaintiffs bore all costs associated with transportation, computer use, and cellular phone use.

Seacoast does not dispute that it imposed rules and regulations by which Plaintiffs were expected to conduct business. However, Seacoast argues that these restrictions were either maintenance-related, rules required to enable the business to run efficiently, or conditions otherwise imposed on real estate sales agents by law. The Court agrees.

Plaintiffs were engaged in the business of selling real property. The requirements for completing a sale are, simply put, a seller with a property, a buyer, and a licensed agent. As both parties concede, Delaware law strictly regulates the realty business. Requiring that its agents conform to the conditions detailed in the law cannot be imputed as Seacoast acting to control its agents.

Further, providing an office that serves as a communication center through which listings are made available to agents does not rise to the level of control. *See Kutney*, 2002 WL 1463092 at *2 ("Even if employees handled scheduling for [p]laintiff, staff support does not constitute

supervision or oversight, and does not establish that an employer has retained control over an employee, unless the supervisor dictates the schedule."). Similarly, maintaining a general sense of order in requiring office time of agents merely serves to facilitate business. No specific hours or cumulative time was required of Plaintiffs. Plaintiffs were responsible for providing their own means of transportation to a home site for a showing. Similarly, Plaintiffs were required to use their own cell phones and their own computers to facilitate a sale. They were not reimbursed for

these expenses. In sum, Seacoast's rules and regulations serve only to simplify the process by which a sale is executed.

The second consideration under *Rypac* is whether Plaintiffs were taxed like employees. Clearly, they were not. Indeed, a separate paragraph set apart on the last page of the Agreement and requiring the agent's acknowledgment reads, in pertinent part: "It is understood that the Salesperson shall not be treated as an employee with respect to the services performed hereunder for Federal Tax purposes." Both Plaintiffs took advantage of the situation and deducted substantial business expenses from their tax returns.

The third determinant is whether other benefits consistent with a standard employment contract were provided. No evidence has been introduced to indicate that Plaintiffs received sick leave, vacation time, retirement or medical benefits, or any other conventional benefit.

In addition to the above, the Court notes that real estate salespersons are excluded from the definition of "employee" under Delaware workers' compensation laws. 19 *Del. C.* § 2316(a). While this fact is not controlling, the purpose of workers' compensation laws is to protect the employee, *Barnard v. State*, 642 A.2d 808, 820 (Del. Super. 1992), and the exclusion of realtors from this broad protection is noteworthy.

Seacoast's Motion for Summary Judgment is granted as to Plaintiffs' claims under the Act.

C. The Commission Reduction is a Forfeiture Clause and Unenforceable

Plaintiffs contend that Seacoast's forfeiture of their earned commissions constitutes a breach of contract and/or a breach of the covenant of good faith and fair dealing. Plaintiffs also contend that the commission reduction is in reality a forfeiture clause which is unenforceable as

against public policy. Since the Court finds the Compensation Policy's Termination Policy punitive and therefore void as against public policy, only that dispositive issue shall be discussed herein.

The clause at issue is as follows:

> If an Associate's Independent Contractor's Agreement is terminated by either party, any pending transactions would be at Level 1 and other referral fees, etc., would be at management's discretion. The Company may assume the responsibility for all follow-up on pending Sales Agreements and may deduct a percentage at management's discretion.

Compensation Policy, Section XII.

The question of whether a clause represents liquidated damages or is a penalty is a question of law. *S.H. Deliveries, Inc v. Tristate Courier & Carriage*, 1997 WL 817883 (Del. Super. 1997). The presumption in dealing with damages clauses is to interpret them as liquidated damages, which are valid and enforceable on its terms, when the purposes of the clause is to compensate the nonbreaching party or to ensure performance. *Id., Unifirst Corporation v. Borris*, 1999 WL 1847348 (Del.Com.Pl. 1999). On the other hand, when the clause is intended only to punish the defaulting party, the clause is void as against public policy and recovery will be limited to actual damages. *S.H. Deliveries, Inc v. Tristate Courier & Carriage*, 1997 WL 817883 at *2 (Del. Super. 1997).

In determining if a clause is a penalty or for liquidated damages, Delaware applies a two-part test. *Id.* A provision will be found to represent liquidated damages when:

> (1) the damages which the parties might reasonably anticipate are difficult to ascertain (at the time of contracting) because of their indefiniteness or uncertainty, and (2) the amount stipulated is either a reasonable estimate of the damages which would probably be caused by the breach or is reasonably proportionate to the damages which have been caused by the breach.

Id. at *2. Additionally, some courts have added a third part to this test, "that the parties must have intended the provision to serve as a liquidated damages provision and not a penalty." *Unifirst Corporation v. Borris*, 1999 WL 1847348 at *5 (Del.Com.Pl. 1999). In this case, the commission reduction triggers upon termination of the agent, regardless of whether it was the agent's decision to leave or the broker's decision to end the relationship.

The Court finds that the first sentence in Section XII, which drops the terminated agents down to Level 1, in and of itself would likely be valid as a liquidated damage clause had a reason for the reduction been enunciated. First, the damages incurred by the Defendant due to an agent's termination would be uncertain or, at the least, difficult to determine with accuracy at the time of their initial engagement. Following a termination, the broker must step in to make sure that whatever is necessary to get the sale to final settlement is in fact done. This protects the interests of the broker as well as the interest of the public, i.e. the buyer and the seller. The time and energy to "ride herd" on any closing problems would not be known or certain. Second, an agent's termination while working for the Defendant could have had a variety of ill effects, including the loss of a sale or sales.

However, when combined with the second sentence of Section XII, the result changes character and becomes punitive. The second sentence allows Seacoast to deduct from an agent's already reduced commission (by way of the first sentence) any out of pocket expenses incurred by Seacoast, regardless of whether the agents see pending sales through to closing. This sentence provides for actual damages to the Defendant in case of unknown expenses, the costs of resolving unsold properties and other similar damages resulting from an agent's termination and

failure to get the sale to settlement. You can't have it both ways.

The second sentence removes any reasonable purpose for the first sentence, and taking both sentences together, the Court finds the result to be excessive and punitive. Defendants argued that there was no reduction in plaintiffs' compensation due to the second sentence, i.e. reduction by actual damages. The Court finds that is irrelevant because they could have, and to interpret the two sentences in isolation of the other wouldn't make sense.

D. Conclusion

In conclusion, the Court holds that the agents are not employees but independent contractors. Further, the Court holds that the commission reduction combined with the ability to dip into the reduced compensation to pay actual expenses or damages is punitive and unenforceable. Plaintiffs are entitled to their commissions, without being reduced to Level 1. Interest, at the legal rate, should be paid beginning on the date of settlement for each transaction.

Per our office conference, this should dispose of the necessity of a trial. Please submit an order incorporating the judgement; or if it's paid, then submit a stipulation of dismissal within thirty days. Thank you.

IT IS SO ORDERED.

Very Truly Yours,

T. Henley Graves

oc: Prothonotary's Office