Channel Partners Magazine September 2011

Sidestepping Quota Quicksand

By: Neil Ende

As a telecom attorney, there are many terms in agent agreements that get under my skin. Among the most disturbing are terms that impose unilateral obligations on an agent where: the agent's performance is entirely dependent on – or at least within the control of – the providing party or the providing party has no corresponding obligations.

These terms often take the form of quotas or minimum commitments. Even worse, most of these terms allow the providing party to entirely stop paying compensation if the quota or commitment is not reached, regardless of the amount of the miss or the cause.

Now, I've heard all the arguments and justifications that are presented for quotas: they are necessary to ensure that the agent continues to work or that the relationship makes economic sense. In my opinion, they are largely bunk and, in any event, the penalties generally are so punitive that the claimed justifications do not justify the existence of the quota.

So, what is an agent to do? First, just say no. When you are pressured, say no again and again and again. Despite what you are told, agent agreements are modified every day and our clients rarely sign agreements with quotas and they never sign agreements that contain a unilateral quota obligation. You have much more negotiating power than you think, so you should not be shy about demanding fair and balanced agreements. If you cannot achieve a fair agreement, especially on a core issue like quotas, it is generally a sign that the relationship is not a good one and that you should cut your losses now and move on.

If you feel the need to agree to some form of quota, there are steps you can and must take to limit your risk and exposure. First and foremost, you should never accept a unilateral quota obligation. Unilateral quota obligations are applied only to the agent without any corresponding obligations being imposed on the provider. Thus, while a unilateral quota obligation requires the agent to meet a dollar sales commitment, no corresponding obligation is imposed on the provider to ensure that the agent has a sellable product. Most of these agreements allow the provider to increase the rates at which the services are provided — even to the point at which they are non-competitive — while leaving the agent's sales quota intact. Most agreements also are silent, at best, regarding how or when services will be provisioned, the quality of the services or the customer service.

Unlike unilateral quota obligations, bilateral quota terms properly recognize that agents can only sell services that meet accepted quality standards, are competitively priced, are provisioned in a timely manner and that are supported by quality customer service. Bilateral quota terms also properly recognize that you cannot sell — and thus should not be committed to sell — any specific quantity of services that do not meet each of these requirements. Any agreed penalty should only be available where the failure to meet a quota is not due to any conduct or failure to act by a provider and is the result only of conduct or a failure to act by the agent.

In addition, any quota obligation does not need to continue for the entire term of the agreement. In many cases, a quota can apply until the agent meets some reasonable revenue level, at which point the quota no longer applies even if the revenue falls below that level. These terms can be crafted to meet the provider's desire to ensure that the agent is committed while limiting the scope and duration of the quota in a manner that is fair to the agent.

Moreover, if your agreement has a quota obligation, extreme care is required with respect to the penalty for non-performance. In many cases, the penalty for non-performance — regardless of how minimal — is the complete loss of commissions. This means that if you have a $10,000 commitment, if you only sell $9,900, you lose the entire commission. In our opinion, this penalty is much too extreme and, in fact, creates an incentive for providers to impose conditions that make it impossible for agents to meet their quotas.

At a minimum, there needs be some proportionality between the underperformance and the loss of commission revenues; i.e., the loss of commissions should be proportional to the underperformance. Further, in addition to the bilateral obligations discussed above, the agreement should measure performance over at least a series of months and provide a period of cure to avoid the imposition of any penalty where the underperformance is associated with one or a small number of billing periods.

Extreme care also is required to ensure that a quota obligation does not negate the evergreen terms of your agreement. A properly drafted evergreen term must contain specific language guaranteeing the payment of commissions on all revenues generated from customers brought by the agent, including on all revenues following the termination of the agreement for cause. Termination allows the provider to refuse to take new business; it should never allow the provider to stop paying commissions on revenues generated from customers brought by the agent. In this context, to avoid negating a properly drawn evergreen term, any penalty for a failure to meet a quota cannot be the basis for a refusal to pay commissions on evergreen revenues.

The simple truth is that, as benign as they may seem, quotas are fraught with risk. By agreeing to a unilateral quota, you are placing your livelihood in the hands of a provider who may, at best, be unwilling or unable to run his/her business in a manner consistent with your best interest and, at worst, may utilize the quota arrangement as the means to retain your commissions. Protect yourself by avoiding quotas in their entirety where possible or, where you must agree to a quota, by insisting that the quota be subject to bilateral obligations that minimize your risk to uncontrollable factors and that maximize your opportunity to meet your commitments.

Neil S. Ende is the founder of and managing partner in Technology Law Group, a Washington, DC-based telecommunications law firm specializing in transactional, litigation, regulatory and intellectual property (trademark and copyright) issues faced by telecommunications and technology companies. Mr. Ende can be reached by phone at +1 202 895 1707 and by email at nende@tlgdc.com.