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NATIONAL SAFETY ASSOCIATES, INC.,  
Plaintiff,

v.

Case No. 93-CV-4178  
Administrative Agency  
Review: 30607

LABOR AND INDUSTRY REVIEW COMMISSION  
and  
WISCONSIN DEPARTMENT OF INDUSTRY,  
LABOR AND HUMAN RELATIONS,  
Defendant.

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DECISION AND ORDER

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This is an action for judicial review brought pursuant to secs. 108.10 and 102.23, Stats., of a decision issued September 30, 1993, by defendant Labor and Industry Review Commission ("LIRC"). In that decision it was determined that those individuals providing services for plaintiff National Safety Associates ("NSA") as distributors did not come within the employment exemption of sec. 108.02(15)(k)16, Stats., and thus were employees under sec. 108.02(12), Stats.

BACKGROUND<sup>1</sup>

On August 1, 1990, the Department of Industry, Labor and Human Relations issued an initial determination finding that NSA's sellers were employees and not independent contractors. This initial determination was affirmed following a hearing before an appeal tribunal. NSA then petitioned for commission review. On September 20, 1991, LIRC set aside the appeal tribunal decision and remanded the matter to the appeal tribunal for additional testimony

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<sup>1</sup>The following information is summarized from LIRC's September 30, 1993, decision.

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regarding NSA's method of compensating its distributors.

On September 30, 1993, LIRC issued a decision in which the appeal tribunal's December 28, 1990, decision was reinstated. LIRC's factual findings were as follows.

NSA manufactures and sells a line of water filters, air filters and water carbonation units for the home. It markets and sells these primarily through a direct sales organization rather than using retail outlets. This sales force is comprised of two classes, dealers and distributors. The first class consists of dealers. They are recruited by distributors and trained to make in-person sales calls to homeowners and small businesses to sell NSA's products. The distributors who recruit the dealers are responsible for placing all of the dealer's orders for merchandise with NSA. The dealers do not have any direct contact with NSA after they sign their initial contract. Dealer compensation is made up of two parts. The first is the dealer's retail margin which is the difference between the amount he pays the distributor for the product and the amount the consumer buys it for. The second is a rebate or after the fact discount on his purchase price from the distributor. This rebate is based on the prior month's purchase volume. Increased purchase volume translates into increased rebates.

The second class of sellers consists of direct distributors, car qualified direct distributors, sales coordinators, fifth dimension sales coordinators, and national marketing directors. During the period covered by the initial determination, most of

these sellers' income was made on the basis of "wholesale purchase volume to the down line." They receive a percentage of inventory sales made to dealers and other distributors below them. This compensation was not related to any sales to an ultimate consumer. Under NSA's buy back procedure and also under the 1990 Wisconsin consent decree, distributors were not required to give up any compensation when inventory was returned to NSA by the dealers.

#### DISCUSSION

Wisconsin's Unemployment Act, Section 108.02(15)(k)16, Stats., excludes from the definition of "employment" services provided

[b]y an individual whose remuneration consists solely of commissions, overrides, bonuses or differentials directly related to sales or other output derived from in-person sales to or solicitation of orders from ultimate consumers, primarily in the home.

If NSA's distributors come within this exclusion, NSA is not an employer under sec. 108.02(13)(a), Stats. Thus, the question before the Court is whether the above language is limited to commissions paid to direct sellers for retail sales or if it also encompasses wholesale sales made by NSA's distributors to its lower level dealers. This presents a question of law.

As described by the supreme court in Kelly Co., Inc. v. Marquardt, 172 Wis. 2d 234 (1992), there are three standards of review applied to the legal conclusions made by administrative agencies:

First, if the administrative agency's experience, technical competence, and specialized knowledge aid the agency in its interpretation and application of the statute, the agency determination is entitled to "great weight." Jicha, 169 Wis. 2d at 290-91; Sauk County, 165 Wis. 2d at 413. The second level of review is a mid-level standard that provides if the

agency decision is "very nearly " one of first impression it is entitled to "due weight" or "great bearing." Jicha, 169 Wis. 2d at 291; Sauk County, 165 Wis. 2d at 413-14. The third level or review is de novo and is applied when the case is clearly one of first impression for the agency and the agency lacks special expertise or experience in determining the question presented. Jicha, 169 Wis. 2d at 291; Sauk County, 165 Wis. 2d at 414.

Kelley, 172 Wis. 2d at 244-45.

LIRC does have long experience in applying sec. 108.02, Stats., and determining whether or not an individual is an employee or a general contractor. However, the case at hand involves the proper construction of subparagraph 16, and is an issue of first impression. Therefore the Court concludes that the appropriate standard of review to apply in this case is *de novo*.

The focus in this case is on the meaning of the phrase "or other output derived from." The Court agrees with LIRC and NSA that this phrase is ambiguous. LIRC, echoing its September 30, 1993, decision which stresses that the compensation earned must be based on sales to the ultimate consumer, contends that "other output" refers to sales leads, obtaining orders, or just soliciting rather than "completed sales to those who resell to consumers." (LIRC's Brief at 11). NSA defines "other output" as referring to sales of inventory to dealers and argues that LIRC's interpretation ignores subparagraph 16's allowing the output to be "derived from" sales.

When construing an ambiguous statute, the Court finds guidance in a statute's context and its legislative history. Subparagraph 16 was enacted by the Wisconsin legislature in 1983 in response to the supreme court's holding in Princess House, Inc. v. DILHR, 111

Wis. 2d 46 (1983). Princess House was a manufacturer and direct seller of household products, principally glassware. Its products were sold through dealers who generally used a party sales plan. Although each Princess House product had a suggested retail price, dealers could charge whatever price they wished. Each dealer entered into a written contract with Princess House which provided that Princess House would sell its products to the dealers for resale. The contract specifically provided that the dealers were not employees. Individual dealers could recruit other dealers and thereby become unit organizers. Their compensation was then calculated as a percentage of the sales made by the recruits. Usually the dealers would write orders for drop shipments direct to their customers' homes, but they also purchased products to use as samples and inventory. The supreme court applied the tests in sec. 108.02(3)(b), Stats., and found that Princess House dealers were not subject to Princess House's control, but held that they were employees because their businesses as dealers could not be sustained absent the relationship with Princess House.

NSA argues that the facts of this case are analogous to those in Princess House. Like Princess House, NSA is a direct seller. The companies have similar sales structures and compensate their sellers on a commission or percentage basis. The difference between NSA and Princess House is that NSA calculates its distributors' compensation based on their wholesale sales to the dealers below whereas the Princess House area organizers received a percentage based on the retail sales made by subordinate sellers.

NSA stresses that subparagraph 16 was passed in order to overrule the Princess House decision and asserts that the Legislature obviously intended to exclude direct sellers from the definition of employee. According to NSA, it would contravene the intent of the amended statute to hinge the exclusion on how sellers are compensated.<sup>2</sup>

NSA also points to the federal direct sellers law, 26 U.S.C. § 3508<sup>3</sup>, which excludes those who sell to individuals who will then

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<sup>2</sup>NSA states that it calculates distributors' compensation based on sales of product to dealers as a manner of practical convenience. It does not monitor what is sold by dealers as that would require additional record keeping.

<sup>3</sup>§ 3508. Treatment of real estate agents and direct sellers.  
(a) General rule. For purposes of this title, in the case of services performed as a qualified real estate agent or as a direct seller

(1) the individual performing such services shall not be treated as an employee, and (2) the person for whom such services are performed shall not be treated as an employer.

(b) Definitions. For purposes of this section, (2) Direct seller. The term 'direct seller' means any person if --

(A) such person

(i) is engaged in the trade or business of selling (or soliciting the sale of) consumer products to any buyer on a buy-sell basis, a deposit-commission basis, or any similar basis which the Secretary prescribes by regulations, for resale (by the buyer or any other person) in the home or otherwise than in a permanent retail establishment, or

(ii) is engaged in the trade or business of selling (or soliciting the sale of) consumer products in the home or otherwise than in a permanent retail establishment,

(B) substantially all the remuneration (whether or not paid in cash) for the performance of the services described in subparagraph (A) is directly related to sales or other output (including the performance of services) rather than to the number of hours worked, and

(C) the services performed by the person are performed pursuant to a written contract between such person and the person for whom the services are performed and such contract provides that the person will not be treated as an employee

resell product to the ultimate consumer. Legislative history reveals that the Legislature was aware of § 3508 when it drafted subparagraph 16. Both NSA and LIRC believe that the words "other output" and "solicitation" were taken directly from the federal statute. Indeed, NSA essentially views the subparagraph 16 as a "Readers Digest" version of the federal statute.

However, while LIRC acknowledges that NSA's distributors are not employees under § 3508, its conclusion is the precise opposite of NSA's. For LIRC the fact that subparagraph 16 does not contain the federal language excluding individuals "selling ... consumer products to any buyer ... for resale (by the buyer or any other person) in the home or otherwise," demonstrates that the Wisconsin Legislature rejected extending the exclusion to those who make wholesale sales to lower level direct sellers.

The Court is persuaded that sec. 108.02(15)(k)16, Stats., does exclude NSA's distributors. First, interpreting "or other output derived from in-person sales ... or solicitation" as referring to sales leads or mere solicitation but not sales of inventory is unreasonably restrictive. LIRC's construction basically drops "other output" from the statute. Although LIRC contends that because subparagraph 16 operates as an exemption from unemployment compensation tax it should be narrowly construed, the supreme court has previously rejected a strict construction of an exception to the unemployment compensation law's definition of "employee." Gelencser v. Industrial Commission, 31 Wis. 2d 62, 65 (1966).

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with respect to such services for Federal tax purposes.

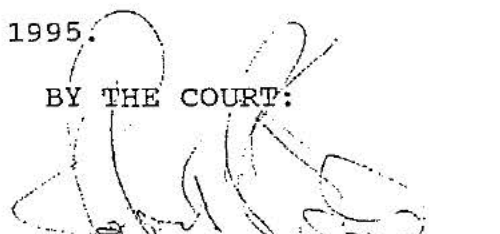
Second, NSA's organization is not so different from the selling method used by Princess House. As noted above, both are direct sellers where lower level dealers are recruited by upper levels. It is conceded that the Legislature enacted subparagraph 16 in order to overrule the Princess House decision. The Court concludes that if the Legislature's intent is to be followed, the emphasis should be on the fact that Princess House was a direct seller; depriving NSA of the exclusion because its compensation is based on wholesale sales to dealers rather than retail sales by dealers is inappropriate. Moreover, the Court agrees with NSA that the Legislature's use of § 3508 language is indicative of an effort to bring Wisconsin law in line with the federal law.

ACCORDINGLY,

For the reasons stated above, the September 30, 1993, decision of the Labor and Industry Review Commission is hereby REVERSED.

Dated this 23rd day of February, 1995.

BY THE COURT:



Hon. Robert R. Pekowsky  
Circuit Judge, Branch 5

cc: Atty. Robert A. Christensen  
Atty. Peter W. Zeeh