

## **COMPENSATION CONUNDRUMS AND COMPLICATIONS**

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Compensation for services provided has always been a touchy subject. In 2009, much ado was made over the money paid to bankers and stockbrokers. In 2010, there was uproar about what corporate executives earned. This year, scandals rocked cities like Bell, California, where public officials were being paid outsized salaries out of tax revenues. And, lest we forget, every year there is a great amount of editorial vitriol sprayed across newspapers and the Internet regarding the size of the contracts given to professional athletes. (Though, let's be honest – wouldn't you like to be paid millions of dollars each year to play in the professional athletic league of your choice?)

Are you aware that there is a compensation problem in the rental property market? Consider, if you will, the following hypothetical:

Sam is an employee of Property Management Company ("PMC"). PMC fee-manages several residential rental communities throughout the valley and has permanent on-site employees at each one. Sam reports to an on-site community manager ("CM"), but neither Sam nor the CM hold real estate salesperson licenses. PMC has a designated broker who supervises the operations of the company.

PMC pays all of its on-site employees except for the CM an hourly wage; the CM is salaried. Sam is one of PMC's most efficient and productive leasing agents and generates many new leases at the community. To encourage and reward productivity like Sam's, PMC pays its leasing agents a bonus for each new lease; through that program Sam receives a significant addition to each biweekly paycheck. Property managers, meanwhile, receives a nice bonus for each month that delinquency rates at their communities are below a certain level. Thanks in no small part to Sam's effort in signing leases with responsible individuals, CM's community has continuously exceeded expectations and delinquency is very low – and thus CM has been regularly receiving a month-end bonus.

Did you spot the problem in this scenario? I'll give you a hint – it's not that one employee is salaried and the other is hourly.

Under Arizona law, no one may be involved in contracts for the leasing of real property without that person possessing a real estate license (salesperson or broker). A.R.S. § 32-2122. There are exceptions to this requirement, however, and the crucial exemption for residential property management is A.R.S. § 32-2121(A)(6). That statute provides that the licensing requirement is waived for "natural persons who are acting as residential leasing agents or on-site managers of residential rental property," so long as they work at "no more than one location during the period of the agents' or on-site managers' regular workday."

The problem is actually the method and manner in which compensation is being paid. Let's return to Sam and CM, the hypothetical leasing agent and the theoretical property manager from the scenario above. Aside from the wages, PMC is paying a "bonus" to Sam for

each lease executed and a “bonus” to CM for each month the community has low delinquency. Which “bonus” is a legal bonus and which one is illegal special compensation?

Is it the “bonus” being paid to CM? The extra moneys paid to CM are derived from a low rent delinquency percentage, and CM’s community reaches its goals on that issue. The money paid to CM is a true bonus, as it is “based on performance, that is received no more frequently than monthly and that does not exceed one-half of the agent’s or on-site manager’s total compensation for the time period.” It “does not constitute special compensation,” and thus CM may continue to receive the benefit of the license exemption.

Sam, however, is paid a “bonus” for each lease signed. Unfortunately for Sam and PMC, the beneficiary of the license exemption is precluded from receiving “special compensation for the acts described in subdivisions (a) through (e) of this paragraph” – and subsection (a) lists as a normal duty the “preparing and presenting to any person a residential lease, application or renewal or any amendment of the lease.” Sam is receiving a bonus for an action that falls within Sam’s normal duties, and in such a scenario Sam needs a license. Since Sam is not licensed but is receiving compensation in the method of a licensee, Sam’s efforts (and PMC’s compensation for those efforts) constitute an unlawful activity.

Read that last sentence again. Under the method of compensation adopted by PMC, Sam is engaged in prohibited conduct. Through that same process, PMC is engaged in prohibited conduct. Also due to that mechanism, PMC’s designated broker is engaged in prohibited conduct, as it “is unlawful for a person, firm or corporation [...], to pay or deliver to anyone compensation for performing any of the acts specified by this chapter [...] who is not licensed at the time the service is rendered.” A.R.S. § 32-2155(B).

How do you make sure that you aren’t engaged in the same problem plaguing PMC? Make sure your unlicensed leasing agents aren’t paid on a per-lease basis. Establish a bonus metric that is not derived from signing leases, whether it’s tied to delinquency or comment cards or something exotic. Don’t give bonuses for normal duties, because if you do, you just might find out what lies in store for PMC...