

# EMPLOYMENT LAW COMMENTARY

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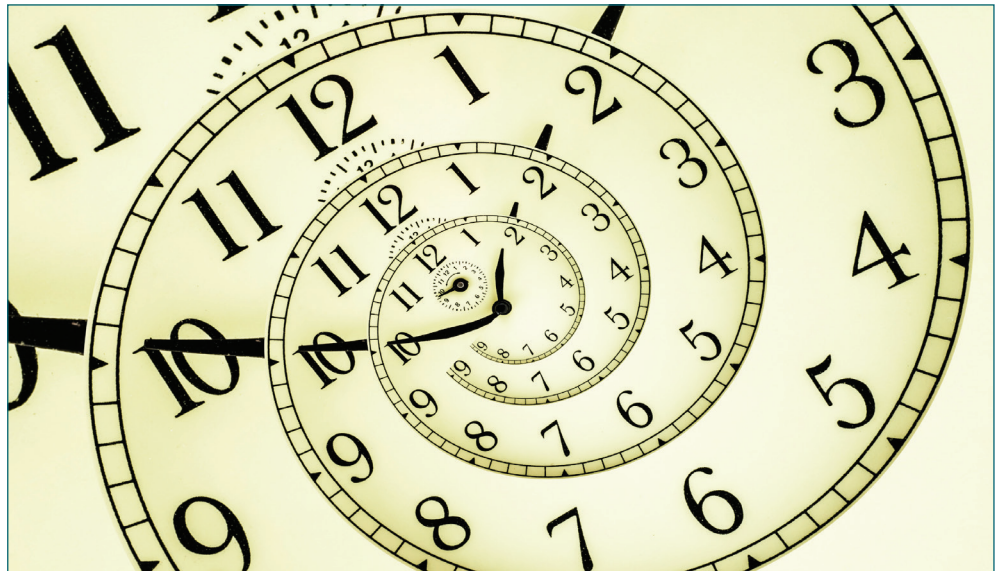
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## WHERE AVERAGE ISN'T GOOD ENOUGH: CALIFORNIA COURTS CONTINUE TO ATTACK PIECE-RATE AND COMMISSIONS COMPENSATION PLANS

By [Lucas V. Muñoz](#)

Employers who pay non-exempt employees solely on a commissions or piece-rate basis probably know by now that doing so in California is an increasingly risky proposition. Over the past few years, various California courts have issued several opinions requiring employers who use these compensation systems to make them ever more complex to satisfy minimum wage laws. Another recent decision, *Bluford v. Safeway, Inc.*, may mean that employers wanting to limit their exposure and to prevent these types of lawsuits will have to couple any commissions or piece-rate compensation systems for non-exempt employees with one that also pays hourly wages.

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## **Armenta Sends California Courts down the Rabbit Hole**

As previously reported in this Commentary, the California Court of Appeal in 2005 decided *Armenta v. Osmose*.<sup>1</sup> In *Armenta*, the employer, a company that installed and maintained utility poles, differentiated between “productive time” (time spent actually working on utility poles), and “nonproductive time” (time spent doing everything else). The class action complaint alleged that employees reported nonproductive time for which they were not paid, or were pressured not to report their nonproductive time by their supervisors. The employees sued, arguing that the employer failed to pay them the minimum wage for their nonproductive hours. The employer claimed that the plaintiffs’ minimum wage theory failed because under then-prevailing federal law, an employer could use a simple average to determine if the employer had satisfied the minimum wage: If total compensation divided by total hours was greater than the minimum wage (accounting for overtime), minimum wage requirements had been met.

*Armenta* could have—and probably should have—been argued and decided on the straightforward theory that the employer failed to compensate the employees for time they were “suffered or permitted” to work. That the hours were deemed “nonproductive” by the employer is not determinative of whether the employees were indeed working, and thus they should have been compensated. However, the *Armenta* court, faced only with the plaintiffs’ minimum wage theory, held that California’s minimum wage statute required that the minimum wage must be paid *each and every* hour an employee works. Dividing total compensation by total hours to determine if the minimum wage had been satisfied, or “averaging” as it was described by the court, was held impermissible under California law.

While the holding of *Armenta* may not sound controversial, it has had wide-ranging impacts (some intended some perhaps not) on compensation schemes not based on an hourly wage, like piece-rate or commissions-based compensation. Since *Armenta*, “averaging” has become a dirty word in wage-and-hour class actions, and California courts have continued to follow *Armenta*’s poor reasoning to seemingly bizarre results, making the use of anything but a straight hourly compensation system increasingly complicated and risky.

In our April *Employment Law Commentary*, we discussed *Gonzalez v. Downtown L.A. Motors*,<sup>2</sup> where the California Court of Appeal applied the reasoning of *Armenta* to what—at the time—appeared to be a lawful piece-rate compensation system. The employees

of Downtown L.A. Motors were mechanics who were paid a set amount for a particular repair job, regardless of how long the job actually took. Different repair jobs were paid at higher or lower amounts, depending on how long the job was supposed to take to complete. At the end of each week, if the mechanic’s total compensation did not at least equal the minimum wage for all hours worked, Downtown L.A. Motors paid the difference. Otherwise, the mechanic having been paid more than the minimum wage was deemed fully compensated. Everyone agreed that, on a week-to-week basis, the mechanics were paid at least the minimum wage, including overtime.

But the class action complaint, relying on *Armenta*, alleged that the piece-rate system failed to pay the mechanics for hours not spent repairing cars (e.g., time spent sweeping, cleaning, attending meetings, or even just waiting around). Under federal wage-and-hour law, it is permissible for piece-rate compensation to cover both productive and nonproductive hours, as long as the employer and employees understand this is the case.<sup>3</sup> The California Labor Commissioner had historically followed this interpretation, issuing an Interpretative Bulletin in the mid-1980s which specifically followed the federal regulation. Indeed, even the California Division of Labor Standards Enforcement (DLSE) Manual stated (and still states) that a piece-rate system exactly like the one used by Downtown L.A. Motors was permissible.<sup>4</sup> Nevertheless, following *Armenta*, the court held the nonproductive time in the auto shop was like the nonproductive hours in the *Armenta* case, and thus the employer was not allowed to “average” the piece-rate compensation to satisfy the minimum wage requirements. Instead *Downtown L.A. Motors* requires that nonproductive time be paid *separately*, i.e., with a separate hourly wage, presumably in addition to the piece-rate compensation. The California Supreme Court declined to review the case. Thus *Downtown L.A. Motors* continues to drive California law farther from established federal law and the interpretations of California’s own executive agency charged with protecting employees and enforcing wage-and-hour laws, the DLSE.

## **A New Twist and Its Potential to Impose Liability on Otherwise Compliant Pay Systems**

The California Supreme Court may, at some point, address the flawed reasoning of *Armenta*. However, until that time, California courts appear prepared to follow *Armenta* in ways that increase liability for employers. The most recent example is *Bluford v. Safeway, Inc.*<sup>5</sup> In *Bluford*, the plaintiffs were a class of unionized truck drivers. Plaintiffs’ compensation was

broken into several parts, apparently to comply with the *Armenta* holding: compensation was composed of 1) a piece-rate based on the number of miles driven; 2) a piece-rate for certain non-driving tasks, for example, based on the number of palettes delivered or picked up; 3) a predetermined hourly rate for certain tasks, like setup time at a store; and 4) an hourly rate for all driving delays like breakdowns and traffic jams.

The plaintiffs alleged that this compensation system failed to provide them with paid rest breaks because they were not paid a *separate* hourly wage for those breaks. *Bluford* agreed. The court started with the Wage Order's language that says "[a]uthorized rest period time shall be counted as *hours worked* for which there shall be no deduction from wages."<sup>6</sup> From this language, the court determined that paid rest breaks had not been provided unless they were paid at an hourly rate (regardless of whether the breaks were actually taken). Despite the fact that *Armenta* expressly declined to address the impact of its decision on rest break regulations, *Bluford* holds that "under the rule of *Armenta v. Osmose*, rest periods must be separately compensated in piece-rate systems."<sup>7</sup> *Bluford* also holds that "[u]nder California minimum wage law, employees must be compensated for each hour worked at either the legal minimum wage or the contractual hourly rate," citing authorities that say nothing of the sort. Once again, keying in on the concept of "averaging," the court held that the employer's argument that paid rest breaks were compensated in piece-rate earnings was akin to "averaging pay to comply with the minimum wage law." The upshot of *Bluford* is that because Safeway paid the drivers for productive time on a piece-rate basis, the court found the company had failed to provide paid rest breaks, which the court said had to be paid by separate hourly compensation.

## The Take Aways for Employers

Even before *Bluford* and *Downtown L.A. Motors*, minimum wage cases relying on *Armenta* were cropping up against employers who pay commissions (as opposed to piece rates). For example, in *Balasanyan v. Nordstrom, Inc.*,<sup>8</sup> a district court in California denied summary judgment in a class action brought on behalf of commissioned Nordstrom salespeople who contended the commission failed to pay them the minimum wage for certain non-sales activities. Although it was "concerned" with the "peculiar result" of requiring separate compensations systems for hourly and commissioned work, the court nonetheless concluded that *Armenta* "forces employers to craft hybrid compensation systems" for commissioned and piece-rate employees.<sup>9</sup> Although *Balasanyan*, like

*Downtown L.A. Motors*, was primarily concerned with unpaid minimum wages, it is likely that *Bluford* opens the door to further rest break class actions in the commissions context, and we fully expect to see more of these class actions against employers using both piece-rate and/or commissions compensation until *Armenta* is overturned.

*Armenta* and its progeny, when read together, may create exposure for *any* compensation system that has any component where work time is paid in some way *other* than an hourly wage. Put another way, the *Armenta* cases may require that *any* piece-rate or commissions compensation pay system be built *on top* of an hourly compensation system. That both the Labor Code and the Wage Orders contemplate and authorize piece-rate-only and commissions-only pay systems has not stopped the *Armenta* train. Paying non-exempt employees solely by piece rate or commissions is becoming increasingly risky, and employers may need to seriously consider implementing "hybrid compensations systems" if they want to reduce or eliminate exposure.

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1 135 Cal. App. 4th 314 (2005).

2 215 Cal. App. 4th 36 (2013).

3 9 C.F.R. § 778.318(c).

4 See DLSE Enforcement Policies and Interpretations Manual §§ 49.2.1.6–8.

5 216 Cal. App. 4th 864 (2013).

6 *Id.* at p. 871.

7 *Id.* at p. 872 (citations omitted).

8 913 F.Supp. 2d 1001 (S.D. Cal. 2012).

9 *Id.* at p. 1007, fn. 7.

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