CALIFORNIA'S OVERTIME LAW AND OTHER ISSUES THAT KEEP EMPLOYERS AWAKE AT NIGHT

While wage and hour law remains the subject of continuing decisions by the courts and the Division of Labor Standards Enforcement (DLSE), the following tips will help minimize your exposure to avoidable legal problems.

EXEMPT OR NON-EXEMPT?

Class-action lawsuits alleging that "non-exempt" employees have been misclassified as "exempt" (and have thereby been deprived of overtime pay) now rank among the most common and costly lawsuits in the employment area. Moreover, the large and highly publicized judgments in these cases have raised the awareness of this classification issue among all employees – including those who work for small and mid-size companies.

The classification of employees as exempt or non-exempt is a highly technical, fact-intensive exercise that requires case-by-case analysis. However, the following advice may provide a useful starting point.

An employee is not exempt merely because he or she is paid a salary. To qualify as exempt under California law (which is more stringent than federal law on this issue), employees must meet a minimum salary requirement as well as a duties test.

To qualify as exempt, an employee must be paid a salary of at least twice the current minimum wage for full-time employment. This means that, with rare exceptions discussed later in this article, an individual that might otherwise qualify as exempt will lose the exemption if that person is paid by the hour. Based on the current California minimum wage of $8.00 per hour, exempt employees must be paid at least $2,773.33 per month.

Even if the position satisfies the salary test, it must also meet one of the duties tests for exemption based on executive, professional or administrative status. Although the duties tests are quite lengthy, the following is a general summary of those exemptions:

- *Executive* employees must be primarily engaged in managing at least one recognized department or subdivision of a business, supervise two or more employees, and have authority to make significant personnel decisions.

- *Professional* employees must be licensed or certified by the State of California and primarily engaged in the practice of one the of the following recognized professions: law, medicine, dentistry, optometry, architecture, engineering, teaching, or accounting. The professional exemption also includes employees primarily engaged in an occupation commonly recognized as a "learned or artistic" profession.

- *Administrative* employees must be primarily engaged in performing non-manual work – other than routine clerical duties – relating directly to the business policies or general business operations of the employer. Such duties may include, by way of example, analyzing business data, planning, negotiating and purchasing.

The following exemptions, which are also relatively common, have their own compensation requirements, as described below:

- *Computer professionals* must be engaged in high-level work (such as the design, development, documentation, analysis, creation, testing or modification of computer systems or programs) and must be paid either on a salary or fee basis (as defined in the regulations) at a rate not less than $81,026.75 per year, *or*, if compensated on an hourly basis, at a rate not less than $38.89 an hour.

- *Licensed physicians and surgeons* must be primarily engaged in duties that require licensure and must be paid at least $70.86 in 2012 (the rate is subject to adjustment annually).

- *Outside salespeople* must spend more than 50% of their working time away from their employer's place of business.

- *Inside salespeople* that are governed by Wage Orders 4 and 7 may be exempt from overtime requirements (but <u>not</u> from other wage and hour laws) if they earn at least 1½ times the minimum wage and earn more than half their compensation through commissions.

If you have questions about the proper classification of a position, you should take the following steps:

- Carefully review job descriptions for accuracy. Involve Human Resources personnel as well as individual employees in the review process. Ensure the accuracy of the job descriptions for exempt positions, and if no job description exists, prepare one. Periodically review job descriptions and actual employee duties to ensure continuing accuracy.

- Compare each job description with the exact requirements for exempt status under California law to see if the position is really exempt. This is the most difficult part, because the tests are quite lengthy and complicated. In California, regulations commonly referred to as "wage orders" apply to employers. Each employer will be governed by only *one* of the wage orders. Most wage orders set forth the requirements for the executive, professional and administrative exemptions. After determining which wage order applies to your business, check the applicable exemptions to see if the position is properly classified as exempt. Find wage orders at http://www.dir.ca.gov/IWC/WageOrderIndustries.htm .

- Educate your Human Resources staff on the law concerning exempt/non-exempt classifications. This is one of the most misunderstood areas of employment law, and there is still a misconception among some employers that the test for exempt

status is whether the position is salaried. Make sure that the people in charge of job classification understand the law in this area.

- Do an annual audit of the salary levels of exempt employees. The current minimum is $2,773.33 per month. However, because the minimum salary level for exempt status is tied to the state minimum wage, the salary requirement for exempt employees will increase whenever the minimum wage increases.

- Don't assume that employees should be classified as exempt simply because others in the industry treat them as exempt. State and federal regulations do not take industry standards into account in determining exempt status.

- Titles are irrelevant when determining whether an employee should be classified as exempt or non-exempt.

- In many industries, some managers and supervisors also perform the same work as their subordinates. These positions run a higher risk of being found non-exempt, and should be evaluated closely to determine whether such employees actually spend the majority of their time performing exempt duties.

- Be alert to positions where the work performed is routine. If the employee is not required to exercise much independent thinking on the job, it is likely not an exempt position.

- Err on the side of caution. In view of the potential liability for misclassifying employees, don't resolve doubts in favor of the exemption.

- Consult employment law specialists for assistance with the tough ones.

OVERTIME REQUIREMENTS

Unless a non-exempt employee is covered by one of the three overtime exceptions discussed below, an employer must pay daily overtime to the non-exempt employee as follows:

Time-and-a-half (i.e., one and one-half times an employee's regular rate of pay) for:

- all hours worked beyond eight hours, up to an including 12 hours, in any workday; and

- the first eight hours worked on an employee's seventh consecutive day of work in a workweek.

Double time (i.e., two times an employee's regular rate of pay) for:

- all hours worked beyond 12 hours in a workday; and

- all hours worked beyond eight hours on an employee's seventh consecutive day worked in a workweek.

Weekly overtime remains in effect, requiring that employers pay time-and-a-half for all straight-time hours worked beyond 40 hours in a workweek.

WARNINGS: *Many employers inadvertently overpay employees by "pyramiding" overtime – that is, paying overtime for the same hours twice. For example, if an employee works nine hours on a particular day and receives daily overtime pay for the ninth hour, that ninth hour should not be counted as a "straight-time hour" in determining the employee's entitlement to weekly overtime pay. Weekly overtime is not earned by an employee until he or she has worked more than 40 straight-time hours in a workweek.*

Also, only hours actually worked should be included in overtime calculations. For example, if an employee is paid for eight hours for a holiday on which the employee does not actually work, those eight hours should not be used in determining whether the employee is entitled to weekly overtime.

OVERTIME EXCEPTION #1: EMPLOYEES WHO HAVE WORKED "MAKE-UP TIME" TO MAKE UP TIME LOST DUE TO PERSONAL OBLIGATIONS

Special overtime rules apply to non-exempt employees who work more than eight hours in a workday to "make-up" time lost due to personal obligations

If a non-exempt employee misses time from work due to personal obligations, the employee may request, in writing, that he or she be permitted to make up that lost time by working extra hours on another day during the same workweek in which the time is missed. If the employer approves that request, the employer will not be required to pay daily overtime for those make-up hours, provided that the hours worked in a single workday do not exceed eleven hours.

WARNINGS: *The DLSE will not permit employers to abuse this provision by colluding with employees to evade daily overtime requirements. Employers are expressly prohibited from encouraging or otherwise soliciting employees to request approval to take personal time off and make up the time pursuant to this provision.*

Make-up hours may be worked either before or after the employee misses the time being made up, so long as: (1) the make-up hours are worked during the same workweek in which the time is missed; and (2) the employee submitted the request to make-up time before working the make-up hours.

When make-up time results in an employee working more than 11 hours in a workday, payment of daily overtime at the applicable rate is still required for all hours worked beyond 11 hours in a workday.

This provision does not allow for "rolling notice." That is, an employee must provide a signed written request for <u>each separate occasion</u> on which the employee requests approval to make up lost time; provided, however, that an employee who knows in advance of a personal obligation that will recur at a fixed time over a succession of weeks may request to make up work time (during the same week that the work time will be missed) for up to four weeks in advance.

OVERTIME EXCEPTION #2:
<u>EMPLOYEES COVERED BY A VALID COLLECTIVE BARGAINING AGREEMENT</u>

State mandated overtime and meal-period provisions that typically apply to non-exempt employees do not apply to employees covered by a valid collective bargaining agreement (CBA) if the CBA expressly provides for: (1) the wages, hours of work and working conditions of employees; and (2) premium wage rates for all overtime hours worked; and (3) a regular hourly rate of pay at least 30 percent above the state minimum wage.

WARNINGS: *The DLSE will consider any wage rate in excess of an employee's regular straight-time rate of pay to be a "premium wage rate" for purposes of this exception. However, remember that even when employees are covered by a valid CBA, they are still subject to the federal Fair Labor Standards Act, which requires payment of time-and-a-half for all hours worked in excess of 40 hours in a workweek.*

OVERTIME EXCEPTION #3:
<u>ALTERNATIVE WORKWEEK SCHEDULES</u>

Under certain circumstances, employees can elect to work under an alternative workweek schedule that will eliminate their employer's obligation to pay daily overtime for the first 10 hours of work in a workday. If an alternative workweek schedule is adopted in accordance with the procedure set forth below, the employer will be obligated to pay overtime as follows:

Time-and-a-half for:

- all hours worked after regularly scheduled alternative workweek hours in a workday have been completed, through the twelfth hour of work;
- all straight-time hours worked beyond 40 hours in a workweek.
- the first eight hours worked on an employee's seventh consecutive day of work in a workweek.

Double time for:

- all hours worked beyond 12 hours on a regularly scheduled workday; and
- all hours worked beyond eight hours on a day that was <u>not</u> a regularly scheduled workday under the alternative workweek.

- all hours worked beyond eight hours on an employee's seventh consecutive day worked in a workweek.

An employer who wishes to adopt an alternative workweek -- which must not exceed 40 hours in a workweek and must not include any workday exceeding 10 hours -- should take the following steps:

1. Prepare a written disclosure for affected employees concerning the proposed alternative workweek, including the effect on the employees' wages, hours and benefits. The disclosure must be in English and in any other language that is the primary language spoken by at least five percent of the affected employees. Although the proposal need not designate the specific days to be worked, it must designate the number of workdays and work hours regularly recurring. The employer may propose a single schedule that would become the standard schedule for all employees in a work unit, or a menu of work schedules from which each employee in the work unit would be entitled to choose.

2. At least 14 days before conducting an election, provide the written disclosure to all affected employees at noticed meetings during which the purpose and effects of the proposed alternative workweek will be discussed. NOTE: An employer must mail the written disclosure to any employee who does not attend such meetings.

3. Have all affected employees vote on the proposed alternative workweek in a secret-ballot election conducted during regular working hours at the worksite of the affected employees.

4. Within 30 days after the election results are final, report the results to: Division of Labor Statistics and Research, Attention: Alternative Workweek Election Results, P.O. Box 420603, San Francisco, CA 94142.

5. If the schedule was approved by at least 2/3 of the affected employees, implement the alternative workweek. Note, however, that employees whose hours are affected by the new workweek cannot be required to work the new hours for at least thirty days after the announcement of the election results.

Although the procedure described above may appear relatively simple, the rules governing alternative workweeks, as interpreted by the DLSE, are actually restrictive and highly technical. Following is a summary of some potential pitfalls for the unwary:

WARNINGS: *Even if an alternative workweek schedule is adopted pursuant to the procedure above, if an employer <u>regularly</u> requires its employees to work more than 10 hours per day or more than 40 hours per week, the DLSE will conclude that the employees are <u>not</u> working an alternative workweek, and will require the payment of standard overtime compensation for all hours worked in excess of eight in a day or 40 in a week. Similarly, an employer cannot deprive its employees of a predictable work schedule by continually changing the specific days and hours to be worked under the alternative work schedule.*

Any alternative workweek schedule that was in place before January 1, 2000 has been nullified unless the schedule conforms to the new requirements (i.e., not more than 10 hours in any workday and not more than 40 hours in a workweek) and was adopted by at least 2/3 of the affected workers in a secret-ballot election.

If a current employee is voluntarily working an alternative workweek schedule that conforms to the new requirements but that was adopted without the required 2/3 vote in secret-ballot election, the employer may permit the employee to continue working that schedule as an alternative workweek ***only if****: (1) the employee has been employed and working that schedule since at least July 1, 1999 as the result of an individual agreement between the employee and employer made after January 1, 1998; and (2) the employee made a written request to continue working that schedule,* ***which the employer approved no later than May 31, 2000****.*

If a menu of work schedule options is offered by the employer and approved by secret ballot, each employee must be permitted to work the specific alternative work schedule of his or her choice. So, for example, even if many employees choose one of the alternative schedules offered and only a few employees choose another, the employer cannot correct that imbalance by assigning any employee to work a schedule other than the specific schedule that individual chose. Accordingly, if an employer wants to offer more than one alternative schedule but its business needs preclude allowing employees to freely choose from among a menu of options, the employer should consider, instead, dividing the workforce into separate work units and proposing a different alternative work schedule for each unit.

If an employer wishes to offer a 9/80 alternative work schedule (i.e., a week consisting of nine hours per day Monday through Thursday and eight hours on Friday, followed by a week of nine hours per day Monday through Thursday and no hours on Friday), it may do so only by designating its workweek as beginning on Friday at noon and ending the next Friday at noon, thereby avoiding the prohibition against regularly scheduling any workweek in excess of 40 hours.

If an employee working under an alternative workweek schedule is required on a particular workday to work more than eight hours but fewer hours than the employee was scheduled to work, the employee must be paid daily overtime for all hours worked beyond eight on that workday.

Alternative workweek schedules of <u>less</u> than 40 hours per week are permitted but no workshift of less than four hours is permitted.

When calculating an employee's entitlement to weekly overtime under an alternative workweek schedule, an employer should not "pyramid" by including hours for which the employee has already been paid a daily overtime premium.

An employer cannot reduce an employee's regular rate of hourly pay as a result of the adoption, repeal or nullification of an alternative workweek schedule. So, for example, if a previously existing alternative workweek schedule was nullified by the new law, resulting in increased overtime obligations for the employer, the affected employer cannot avoid those obligations by reducing hourly wages to maintain the same gross payroll as existed prior to the nullification.
If an employer implements an alternative workweek schedule and an affected employee who was eligible to vote cannot work the alternative schedule, the employer is obligated to make a reasonable effort accommodate the employee with a work schedule not exceeding eight hours in a workday. The employer may (but is not obligated to) similarly accommodate any employee hired after the adoption of the alternative workweek schedule.

An employer must explore "any available reasonable alternative means" of accommodating the religious belief or observance of an affected employee that conflicts with an adopted alternative workweek schedule, whether or not the affected employee was hired before or after the adoption of the alternative workweek schedule.

OVERTIME EXCEPTION #4:
EMPLOYEES RECEIVING TIPS OR GRATUITIES

A "gratuity" is defined by the California Labor Code as any tip, gratuity, money or part thereof, that has been paid or given to or left for an employee by a patron of the business over and above the actual amount due the business for services rendered for goods, food, drink, or other articles sold or served to that person. California Labor Code §351 declares that gratuities are the sole property of the employee or employees to whom they are given or for whom they are left. Accordingly, an employer is prohibited from collecting, taking or receiving any portion of a gratuity given to or left for an employee by a patron, or from making wage deductions or credits on account of these gratuities.

The benefit of providing tips or gratuities to employees (as opposed to distributing service charge revenue to them), is that there is no obligation to consider tips or gratuities wages for purposes of calculating the base rate. Therefore, the overtime rate will not fluctuate regardless of the amount of tips or gratuities received by an employee from a patron.

WARNINGS: *Service charges are mandatory amounts that are added to the bill of a restaurant patron or member of a club in accordance with the terms of an agreement to purchase food, beverages or other items. The portion of the mandatory service charge that an employer distributes to employees (for example, their servers and bartenders) is not considered a "tip" or "gratuity" within the meaning of wage and hour laws. The problem with utilizing such service charges is that, because they do not pass directly from the customer or member to the employee/service provider, they must be considered to be part of an employee's straight time wages if the employee is non-exempt. This, of course, can cause the employee's base*

rate to increase significantly, which will, in turn, cause the employee's overtime rate to proportionately increase.

CIVIL PENALTIES FOR THE ENFORCEMENT OF OVERTIME PROVISIONS

In addition to other civil and criminal enforcement mechanisms, the DLSE has power to issue citations that provide for civil penalties in the following amounts:

1. for an employer's initial violation, $50 for each underpaid employee for each pay period in which the employee was underpaid in addition to an amount sufficient to recover underpaid wages; and

2. for each subsequent violation by the employer, $100 for each underpaid employee for each pay period in which the employee was underpaid in addition to an amount sufficient to recover underpaid wages.

WARNINGS: *The DLSE may issue civil penalty citations even when a violation was neither willful nor intentional.*

The DLSE may impose penalties not only on an employer, but on any "other person acting on behalf of an employer" who violates or causes to be violated any provision regulating hours and days of work. Although that expansive language empowers the DLSE to penalize individual payroll clerks and payroll supervisors, the DLSE has announced its intention to restrict its issuance of citations to the following persons and entities: (1) the legal entity that is the employer; and (2) on appropriate occasions, to those corporate officers or managers who directly or indirectly exercise control over wages, hours or working conditions.

EMPLOYEE OR INDEPENDENT CONTRACTOR?

Independent contractors are not entitled to overtime pay nor to benefits customarily provided to employees. Consequently, in an effort to reduce labor costs, many businesses have classified as "independent contractors" individuals who, by every reasonable standard, are actually employees. A misclassification of this type carries with it considerable risk. In addition to the possibility of being penalized by taxing authorities, a company that has misclassified an employee as an independent contractor could face catastrophic liability if such an individual is injured on the job and is not covered by worker's compensation insurance.

Like the test for exempt status, the determination of an individual's status as an employee or independent contractor requires a fact-intensive, case-by-case analysis. The exercise is further complicated by the fact that various jurisdictions and administrative agencies apply different tests depending on the type of claim asserted. For example, if an underlying dispute concerns unemployment insurance or withholding taxes, the Employment Development Department and the courts generally apply a 12-factor common law test. If the underlying dispute concerns a wage-and-hour claim or a claim brought under the Fair Employment and Housing Act, courts generally apply a 6-factor California common law test. In certain other cases (e.g., in connection with worker's compensation claims), courts may apply another test known as the "economic realities test." While the particular factors included in each test vary, most analyses place

considerable emphasis on whether the company has a right to dictate the means by which the worker is to accomplish the desired results (which suggests an employee relationship), whether the type of work being done by the worker is the primary type of work done by the company or is identical to the work done by employees of the company (both of which suggest an employee relationship) and whether the relationship is ongoing for an indefinite period of time (which suggests an employee relationship) or is limited to a particular project (which suggests an independent contractor relationship).

For additional insight into the type of factors considered in making this determination, you may log on to http://www.irs.gov/Businesses/Small-Businesses-&-Self-Employed/Independent-Contractor-%28Self-Employed%29-or-Employee%3F to access the factors considered by the Internal Revenue Service.

Questions?

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