Federal Court Finds That Agreement to Defer Payment of Salary Violates the Massachusetts Payment of Wages Statute

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An increasingly common practice among employers, particularly start-ups, is to enter into agreements with senior managers to defer salary payments until certain financial targets are reached. The employees typically welcome these arrangements because they often own a portion of the business. However, a recent decision by the federal court in Massachusetts warns that these types of arrangements may be unlawful. In *Stanton v. Lighthouse Financial Services, Inc.*, the court held that an agreement to defer the payment of salary violated the Massachusetts Payment of Wages statute and was therefore void.

In *Stanton*, the plaintiff John Stanton was the co-founder and president of a start-up company, Lighthouse Financial Services. His written employment contract with Lighthouse provided for an annual salary of $144,000, but the company's board of directors reserved the right to defer any salary payments. The contract stated that Stanton would be paid any deferred salary before the company distributed any profits to shareholders. Stanton worked for Lighthouse for over a year, but his salary payments were deferred. After Stanton resigned from his position, he sued Lighthouse and another officer of the company under the Payment of Wages statute, claiming over $180,000 in unpaid wages.

On cross-motions for summary judgment, the federal court found that the defendants were liable to Stanton under the Payment of Wages statute. The court rejected the defendants' arguments that the statute did not apply to Stanton. It held that Stanton was an employee covered by the statute, even though he was the co-founder and president of the company. The court also concluded that the salary payments were wages because the payments were not truly contingent. Based upon these conclusions, the court determined that the written contract, in which Stanton agreed to defer payment of salary, was void under the statute. The court thus held that the defendants had violated the Payment of Wages statute and ordered a trial on damages.

The decision in *Stanton* is a warning against the use of formal or informal salary deferral arrangements. Even if the employee agrees to the arrangement, the deferral of wages may constitute a violation of the Payment of Wages statute, which provides for mandatory treble damages, interest and an award of attorneys' fees and costs. Plus, certain company officers may be individually liable under the statute. To the extent that a company needs an employee to forgo compensation until it reaches financial viability, a safer course is to pay that employee a base salary that meets or exceeds the minimum wage rate or, if exempt, at least $455 per week and to offer a bonus expressly conditioned upon the company's financial performance.