Paul Hastings

February 2006

StayCurrent

A Client Alert from Paul Hastings

Wage and Hour Law 2005: The Year in Review

By Leslie L. Abbott, George W. Abele, Stephen L. Berry, Thomas Geidt and Kirby C. Wilcox

The development of wage and hour law in California and under the FLSA continued at a rapid pace in 2005. Even those who normally monitor these developments struggled in the past year to remain current. The purpose for this alert is to summarize what we believe are the most notable developments of the past year. Our focus is California law, but we include significant developments under federal law as well. Given the volume of activity in the wage and hour area, we cannot cover every new precedent, nor fully explore the developments that we have elected to review. Our intent is to identify some of the important issues that arose during 2005 and to prompt you to consider whether further analysis of those issues would benefit your business.

I. Top Four Claims in 2005

From the many types of claims that plaintiffs filed in 2005, we have chosen four that we believe dominated new class action litigation: (1) meal period claims; (2) misclassification claims; (3) "off-the-clock" claims; and (4) commissioned employee claims.

California Meal Period Cases

Three key issues remain unresolved under California meal period law: (1) what is the meaning of the word "provide"; (2) when does entitlement to meals accrue, after every work period of 5 hours or after 5 hours of work and again after 10 hours of work; and (3) are the one-hour payments for non-compliant meals wages or penalties? As of this writing, three developments highlight the continued uncertainty over the resolution of these issues: (1) a Superior Court jury in Alameda County awarded plaintiffs $172 million in one-hour payments and punitive damages for non-compliant meals; (2) the California Division of Labor Standards Enforcement ("DLSE") withdrew the meal period regulations that it had drafted and re-drafted over the course of an entire year;[1] and (3) three appellate courts have issued decisions specifically addressing the penalty vs. wage issue: *Murphy v. Kenneth Cole Productions, Inc.,* 134 Cal. App. 4th 728 (Dec. 2, 2005), *petition for review granted,* February 22, 2006, *National Steel and Shipbuilding Co. v. Superior Court,* 135 Cal. App. 4th 1072 (Jan. 20, 2006), and *Mills v. Superior Court,* 135 Cal. App. 4th 1547 (Jan. 27, 2006). In unanimous decisions, the First Appellate District in *Murphy* and the Second Appellate District in *Mills* held that the one-hour payments are penalties; in a 2-1 decision, the Fourth Appellate District in *National Steel* held that the one-hour payments are wages. The California Supreme Court just granted review in *Murphy.* As a consequence of the continued uncertainty, we recommend that employers consider a number of liability and damage mitigation strategies:

- Review all policy documents and employee handbooks to determine whether they address the three open issues set forth in the previous paragraph in a manner consistent with your Company's tolerance for risk;
- Review current meal period practices for the same purpose; and
- Provide a mechanism for employees to report violations of your Company's meal period policies and promptly investigate and respond to such reports.

Federal and California Exempt Status Misclassification Cases

The August 2004 amendments to the FLSA concerning the rules for determining exempt executive, administrative, professional and outside sales status clarified some previous ambiguities but left many open questions. The California rules for the same exemptions include both greater evidentiary burdens for employers and internal references to FLSA regulations that the August 2004 amendments replaced. Prior to 2005, these uncertainties provoked considerable litigation in a relatively small number of industry groups, notably the retail, restaurant, ho-

tel and transportation industries. In 2005, litigation spread to several other industries, notably the mortgage brokerage, securities brokerage and high tech industries. We expect the litigation to grow in all three of these industry segments and to continue to spread to others. In light of these developments, we recommend that employers consider the following options:

- Review the duties of exempt employees for compliance with federal and state exempt status rules;
- Determine whether your Company should reclassify any currently exempt employees; and
- Review and revise as necessary the time keeping and compensable time policies of your Company to make sure that all currently non-exempt employees and all reclassified employees receive proper pay for all hours worked.

Off-the-Clock Cases

An increasing number of cases target time keeping practices for non-exempt employees. The plaintiffs allege that their employers require the performance of uncompensated work and/or that they are aware of the obligation to record all of their work hours, but do not do so. Examples of alleged "work" without compensation include pre-and post-shift activities, some forms of training time, work at home and work on vacation. Examples of alleged under-reporting of time include asserted managerial antipathy to overtime, failure to fully understand employer time keeping guidelines and the lack of clear mechanisms for reporting off-timecard activity (e.g., work at home). To avoid litigation over these issues, employers should consider the following:

- Review all activities that employees perform at the request or knowledge of your Company for its benefit to determine which activities constitute work under federal and state law;
- Develop and communicate to non-exempt employees clear guidelines for capturing and compensating all hours worked;
- Specifically prohibit off-the-clock work and warn of disciplinary action for non-compliance;
- Provide a mechanism for employees to anonymously report any manager who explicitly or implicitly requires off-the-clock overtime work and promptly investigate and respond to such reports;
- Train managers to monitor employee time keeping practices and to promptly take appropriate disciplinary action for employee non-compliance; and
- Include on time records appropriate certifications that the hours reported are complete and accurate.

Commissioned Employee Cases

Two types of cases pertaining to commissioned employees made headlines in 2005: (1) those involving the exempt status of commissioned employees (especially in the mortgage and securities brokerage industries); and (2) those involving chargebacks against the commissions for cancelled or returned sales.

The exempt status cases have raised issues regarding the interpretation of the outside sales exemption, the portion of the federal administrative exemption that pertains to employees in the financial services industry and the impact of deductions for goods, services and fines upon salaried status. At the current time, there are few clear guidelines from the courts or federal and state enforcing agencies regarding these issues. However, employers should consider:

- A review of outside sales positions to make sure that employees spend more than fifty percent of their time away from home and any employer facility engaged in sales, not promotion for sales;
- A review of all wage deduction practices; and
- A review of base compensation to ensure it meets minimum amounts set forth in applicable regulations.

With respect to the legality of chargebacks, *Steinhebel v. Los Angeles Times Communications,* 126 Cal. App. 4th 696 (2005), is the first published opinion in California in roughly a decade to discuss the issue directly.

The scenario is quite common in many industries: an employer agrees to pay its employee a commission for selling a product or service, but conditions that commission on the occurrence of some subsequent event, such as the employee performing follow-up activities or the employer receiving payment for the product or service. Despite the condition, the employer typically pays the employee the amount of the commission upon the actual sale, with the understanding that if the subsequent event does not occur, the employee will return the payment.

Plaintiffs in California began to challenge this common practice, primarily by asserting that the practice violated California Labor Code Sections 221 and 400-410. Section 221 states that it is unlawful for an employer to retrieve "wages" previously paid to an employee. Sections 400-410, as interpreted by the

California Supreme Court, preclude a company from recovering ordinary business losses from its employees.

Prior to *Steinhebel,* the existing authority had established certain rules:

- Chargebacks are permitted – only against the selling salesperson – if (i) the goods are returned, and (ii) the conditions leading to a chargeback are clear and unambiguous. DLSE Policies & Interpretations Manual, Section 34.3.1; *Hudgins v. Neiman Marcus Group, Inc.,* 34 Cal. App. 4th 1109, 1122 (1995).

- Commissions can be withheld until the Company receives payment for the product sold. DLSE Opinion Letter, 10/1/90.

- Commissions can be withheld, or chargebacks may be permitted, where a salesperson had ongoing responsibilities, but did not complete them prior to termination of employment, and thus did not "earn" the commission. *Division of Labor Standards Enforcement v. Dick Bullis, Inc.,* 72 Cal. App. 3d Supp. 52 (1977); *American Software, Inc. v. Ali,* 46 Cal. App. 4th 1386 (1996); *Prudential Insurance Co. v. Fromberg,* 240 Cal. App. 2d 185 (1966).

- Chargebacks are not permitted to recover ordinary business losses, such as cash or merchandise shortages, absent willful misconduct, dishonesty, or gross negligence. *Kerr's Catering Service v. Department of Industrial Relations,* 57 Cal. 2d 319 (1962); *Quillian v. Lion Oil Co.,* 96 Cal. App. 3d 156 (1979); DLSE Opinion Letter, 10/1/90.

None of these "rules," however, directly addressed the issue in *Steinhebel,* where the employer agreed to pay its commissioned employees a commission for selling a subscription to the Los Angeles Times that lasted at least 28 days. The employer advanced the amount of the commission upon the sale, but if the subscriber cancelled that subscription within 28 days, the employer "charged back" the commission – on the theory that the commission had not been earned – by reducing future advances by the amount of the commission. The court in *Steinhebel* held that this practice did not violate the California Labor Code.

As a result of the analysis in *Steinhebel* and previous authorities, employers should consider several issues when reviewing or revising their compensation plans for commissioned employees:

- *Advances, Not Earnings.* Compensation plans should state clearly that commissions are not "earned" until specific conditions precedent have been satisfied. Any payments made to the employees prior to the commissions being earned should be characterized as "advances."

- *Periodic Acknowledgments.* Employers should consider obtaining periodic acknowledgments from the commissioned employees that they understand (i) their commissions are not earned until certain specific events occur, (ii) the compensation they receive at the time of the sale is an advance on the as-yet-unearned commission, and (iii) if the subsequent events do not occur, the employer can recoup the advance.

- *Scope of Chargebacks.* In *Hudgins,* Neiman Marcus compensated its sales employees in part by commissions. Each sales employee was supposed to identify himself or herself on the sales receipt, so that if an item were returned, the salesperson who had made the original sale would be subject to a chargeback from future commissions. Where the initial salesperson was not identifiable, however, Neiman Marcus charged back against all remaining salespeople the commission presumably paid on the initial sale. The court found this practice unlawful. Because the commission paid was irretrievable (at least from the employee to whom it was paid), it amounted to a business loss that Neiman Marcus was attempting to spread among its remaining employees.

- *"Unconscionability."* Plaintiffs also argue that chargeback provisions are unconscionable. While a discussion of substantive and procedural unconscionability is beyond the scope of this Alert, there are certain steps employers can take to reduce the risk that their chargeback provisions would be held unconscionable. For example, employers should clearly state their chargeback provisions in compensation plans, explain those plans in meetings with the employees, and secure employee acknowledgments in writing. In addition, employers should make sure that their chargeback provisions are reasonable and do not "shock the conscience." *In Steinhebel,* the chargeback period was just 28 days, which the court found to be a reasonable condition. The longer the chargeback period, the more susceptible the provisions become to attack. Moreover, if an employer can articulate a rationale – particularly one supportable by documentary evidence and understood by employees – for the length of the chargeback period, it will reduce the risk of an unconscionable finding. Finally, if the operation of the chargeback provisions are common in the employer's industry, the employer will have a stronger argument that the provisions are not unconscionable.

- *Chargebacks From Base Pay.* Chargebacks should apply to the advance made on the as-yet-unearned commission and should be taken only from future advances. An employer should not reduce an employee's base compensa-

tion, or it risks a violation of the Labor Code.

II. Key Cases

There were numerous court decisions in 2005 that affect employers with employees in California. In addition to *Steinhebel v. Los Angeles Times Communications,* discussed above, we summarize ten of those decisions.

1. COMPENSABILITY OF "WALKING TIME" AND OTHER PRELIMINARY AND END-OF-SHIFT ACTIVITIES. *IBP, Inc. v. Alvarez,* ___U.S.___, 126 S. Ct. 514 (2005).

In November 2005, the U.S. Supreme Court issued a major ruling on what types of preliminary and end-of-shift activities are compensable under the federal Fair Labor Standards Act, as amended by the Portal-to-Portal Act. The ruling involved employees at meatpacking and poultry processing plants whose jobs require them to put on elaborate protective equipment at the beginning of each shift and then walk from a changing area to the production area. At the end of the shift, they walk back to the changing area and take off the protective gear. The Court unanimously ruled that the employers were required to pay their employees for the time they spent walking between the changing area and the production area at the beginning and end of each shift. The Court also ruled that the time employees spend waiting to take off their protective gear in the changing area at the end of the day is compensable. However, the time they spend at the beginning of the day waiting to don the protective gear is not compensable. The Court premised its ruling on a determination that donning and doffing burdensome protective gear is "integral and indispensable" to the employees' "principal work activity," and that an employee's compensable workday runs continuously from the time that an employee begins engaging in a principal activity (in this case, donning the protective gear in the changing area) until the time that the employee finishes engaging in a principal activity (removing the protective gear).

2. INDIVIDUAL LIABILITY FOR WAGE CLAIMS. *Reynolds v. Bement,* 36 Cal. 4th 1075 (2005).

The plaintiff believed that his employer had misclassified him as exempt from overtime and sued not only the company, but also its president and seven other company officers and directors in their individual capacities. Reynolds relied on the definition of "employer" found in the Industrial Welfare Commission ("IWC") Wage Orders: "any person ...who directly or indirectly ... exercises control over the wages, hours, or working conditions of any person." The California Supreme Court declined to accept the IWC's definition of "employer" as controlling. The Court unanimously ruled that employees in California may not sue individual officers, directors and managers for unpaid wages under the Labor Code. The Court's decision, however, does not bar employees from seeking to impose individual liability under other applicable common law or statutory theories.

3. PARTIAL-DAY DOCKING OF EXEMPT EMPLOYEES' VACATION BANKS. *Conley v. Pacific Gas & Electric Co.,* 131 Cal. App. 4th 260 (2005).

Pacific Gas & Electric ("PG&E") maintained a policy of charging the vacation leave bank of its exempt employees when they wanted or needed to be absent from work for four or more hours in a day. In such cases, PG&E paid their full salaries, but debited their accrued vacation leave banks. Several PG&E employees brought a class action complaint, alleging that this practice caused all of PG&E's exempt employees to lose their exempt status and to be eligible for overtime pay. The plaintiffs theorized that, because California law treats vacation pay as earned "wages," PG&E's practice of deducting amounts from vacation banks is tantamount to making an improper salary deduction, in violation of the general rule that employees who work any part of a day, to be exempt, must always receive their full salary for the day. The California court of appeal rejected the plaintiffs' claim. In upholding the lower court's denial of class certification, the court of appeal determined that PG&E's practice of partial-day leave bank docking did not constitute an unlawful forfeiture of wages or otherwise violate California's salary-basis rules for exempt employees.

4. MEAL PERIOD PREMIUMS, OVERTIME MISCLASSIFICATION AND LABOR COMMISSIONER APPEALS. *Murphy v. Kenneth Cole Productions, Inc.,* 134 Cal. App. 4th 728 (2005), *petition for review granted,* February 22, 2006.

The court analyzed whether meal period premiums under Labor Code section 226.7 properly should be characterized as a form of "wages," (subject to a four-year statute of limitations) or as a penalty (subject to a one-year statute of limitations). The court decided that meal and rest period premiums are in the nature of a penalty, because they bear no direct relationship to the actual losses that employees suffer as a result of meal and rest break violations. Moreover, according to the court, the legislative history of section 226.7 and the wage orders reflect that the California Legislature and the Industrial Welfare Commission intended the premiums to be penalties. Therefore, the court ruled that Murphy's meal and rest period claims were barred by the one-year statute of limitations because more than one year had elapsed since his employment with the company ended.

Two decisions on the same topic issued in early 2006: *Mills v. Superior Court,* 135 Cal. App. 4th 1547 (Jan. 27, 2006)

(3-0 decision; holding that section 226.7 is a penalty provision subject to a one-year statute of limitations based on the statute's language, the legislative history, other Labor Code provisions, and other federal and state court decisions bearing on the issue; the Court affirmed the trial court's sustaining of the company's demurrer, which dismissed the plaintiff's claims for various Labor Code penalties over and above Section 226.7, including Sections 203 (waiting time penalties for underpaid terminated employees), 210 (penalties for untimely wage payments), 226.3 (penalties for failure to provide a wage deduction statement), as well as the plaintiff's Section 17200 claim for restitution); and *National Steel and Shipbuilding Co. v. Superior Court,* 135 Cal. App. 4th 1072 (Jan. 20, 2006) (2-1 decision; holding that section 226.7 payments are wages).

5. MEAL AND REST BREAK CLAIMS OF EMPLOYEES COVERED BY A COLLECTIVE BARGAINING CONTRACT. *Valles v. Ivy Hill Corp.,* 410 F.3d 1071 (9th Cir. 2005).

The employer argued that California's meal period requirements do not apply to employees who are covered by a collective bargaining agreement. Alternatively, the employer argued that the employees' claims were preempted by federal labor law under the doctrine of "301 preemption." The Ninth Circuit rejected both arguments. It ruled that California's meal period rules are non-negotiable rights designed to protect all California workers, including those covered by a collective bargaining agreement, and that a union cannot waive those rights in a collective bargaining agreement.

6. MEAL PERIOD AND PAY STUB VIOLATIONS. *Cicairos v. Summit Logistics, Inc.,* 133 Cal. App. 4th 949 (2005).

Five truck drivers for a warehousing business alleged that their employer failed to provide meal and rest breaks and also failed to provide itemized earnings statements containing all of the information required by Labor Code section 226. The plaintiffs were members of the Teamsters Union and covered by a collective bargaining agreement that provided for meal periods and rest breaks. Overturning summary judgment for the company, the California court of appeal found that there were triable issues on the plaintiffs' claims. The court ruled that the plaintiffs' failure to exhaust their remedies under the contractual grievance-arbitration procedure did not preclude them from filing their court action. It further found that the "motor carrier exemption" in the applicable IWC Wage Order, although it exempts certain truck drivers from overtime pay, does not exempt employers from the duty to comply with California's meal and rest period rules. The court also held that the company's pay stubs did not satisfy the requirements of Labor Code section 226 because they did not reflect the total number of hours that the drivers worked in each pay period and did not list the employer's correct name and address. Finally, the court found that the employer did not provide sufficient evidence that it had complied with meal and rest period obligations. The court reasoned that it was insufficient for an employer to "assume" that drivers took their meal periods, especially when the company provided no mechanism for recording them. The court also relied on evidence of employer conduct discouraging drivers from taking rest breaks.

7. PRIVATE ATTORNEYS GENERAL ACT. *Caliber Bodyworks, Inc. v. Superior Court,* 134 Cal. App. 4th 365 (2005).

In November 2005, a California court of appeal issued the first comprehensive opinion interpreting California's Labor Code Private Attorneys General Act of 2004 ("PAGA"), Labor Code §§ 2699, *et seq.* This Act, which went into effect on January 1, 2004, and was amended in August 2004, allows aggrieved employees to pursue claims for Labor Code civil penalties that previously were enforceable only by the State's wage and hour enforcement agencies. Successful PAGA plaintiffs may retain 25% of any penalties they collect, while the other 75% goes to the State of California. In *Caliber,* several employees filed a class action alleging 13 separate claims, including claims for penalties, but without alleging prior exhaustion of administrative remedies. The court responded with several rulings, two of which are key. First, it created a distinction between "civil penalties," those that prior to PAGA were enforceable only by the State, and other Labor Code "statutory penalties," those that prior to PAGA were recoverable directly by employees. According to the court, the duty of a plaintiff to plead exhaustion of administrative remedies applies to all civil penalties, but not to statutory penalties. Thus, for example, the court concluded that Labor Code section 203 (waiting time penalties for underpaid terminated employees) is a "statutory" penalty not subject to exhaustion. Second, the court rendered a dubious and previously-unheard-of interpretation of the Labor Code's waiting time penalty provisions, concluding that an employee is permitted to seek 30 days of "statutory" penalties under section 203 and an additional 30 days of "civil" penalties under Labor Code section 256, for a combined total of 60 days' pay. This holding creates uncertainty regarding an employee's right to "stack" or "pyramid" multiple Labor Code penalties.

8. MINIMUM WAGE. *Armenta v. Osmose, Inc.,* 135 Cal. App. 4th 314 (2005).

The court addressed a question that no prior California appellate court had resolved: whether California's minimum wage law entitles employees to the statutory minimum wage (now $6.75) for each and every compensable hour of work that they perform, or whether employers need only pay employees an

amount which averages out to at least $6.75 an hour for all the hours worked in the workweek. The plaintiffs alleged that their employer violated California's minimum wage law by failing to pay them for various "nonproductive" tasks, such as traveling to the job sites, loading equipment into company vehicles, filling out paperwork, and maintaining company vehicles. The employees' regular hourly rates for the "productive" work activities ranged from $9 to $20 an hour. The employer argued that it always paid the employees a weekly amount which averaged out to at least $6.75 an hour for all the compensable hours they worked in the workweek. The court of appeal rejected the employer's averaging method and ruled that California law, unlike the FLSA, requires an employer to pay its employees the minimum wage for each and every separate hour of compensable work. Therefore, the court upheld the lower court's prior award of unpaid minimum wages, liquidated damages (a doubling of the minimum wage award under Labor Code § 1194.2), waiting time penalties, attorneys' fees and costs totaling approximately $400,000 in favor of the nine plaintiffs.

9. EXPENSE REIMBURSEMENT. *Gattuso v. Harte-Hanks Shoppers, Inc.,* 133 Cal. App. 4th 985 (2005).

The employer paid outside and inside sales employees a base salary and commissions. However, it paid the outside sales employees at a higher salary and a higher commission percentage than it paid the inside sales employees, because the jobs of the outside sales employees required them to incur additional expenses, including the use of their personal automobiles to make sales calls. The employer did not directly reimburse the outside sales employees for the use of their automobiles by, for example, paying them on a cents-per-mile basis. Two of the outside sales employees brought a class action complaint in which they alleged that the company owed them indemnification under California's expense reimbursement statute, Labor Code section 2802, for the use of their automobiles and other unreimbursed expenses. In its defense, the company argued that it already was adequately reimbursing the plaintiffs for their expenses by paying them more in salary and commissions than it paid the inside sales force, specifically to cover their automobile and other expenses. The plaintiffs countered that California law does not permit an employer to meet its expense-reimbursement obligation by purporting to build it into the employees' taxable wages; instead, the employer must reimburse employees for their actual expenses by a separate payment. The court of appeal ruled that Section 2802 does not specify any particular method by which the employer must indemnify employees for their necessary expenditures so long as the amount that the employer pays for expenses is sufficient to cover them.

10. REGULAR RATE OF PAY. *Huntington Memorial Hospital v. Superior Court,* 131 Cal. App. 4th 893 (2005).

The trial court in this case certified a class of hospital nurses in Southern California who challenged the employer's overtime treatment of a "short-shift differential." The nurses normally worked 12-hour shifts, for which the hospital paid them eight hours of straight-time pay at a designated base hourly rate and four hours of overtime pay at time-and-one-half. Whenever the nurses worked fewer than 10 hours on a shift, the hospital paid them a short-shift differential, amounting to an extra $4.04 an hour for each hour worked. When nurses worked 10 to 12 hours, the hospital did not pay the differential. The hospital did not include the short-shift differential in the regular rate of pay for overtime purposes. The nurses argued that the payment of this differential, without including it in the regular rate of pay, was a subterfuge to evade the overtime laws, because it had the effect of allowing the employer to pay employees at a lower hourly rate when they worked 10 to 12 hours than the rate it paid them for working 10 or fewer hours, although they were performing the same work at all times. The trial court denied summary judgment for the hospital on the nurses' overtime claim, and the court of appeal affirmed. In a decision that extensively discusses the "regular rate of pay" under California law and how it is to be calculated, the court of appeal concluded that there is a triable issue as to whether the hospital's short-shift differential is a subterfuge or artifice designed to evade the overtime laws.

III. Department of Labor Opinion Letters

In 2005, the Wage and Hour Administrator of the Department of Labor ("DOL") issued fifty-four Opinion Letters interpreting many provisions of the FLSA. California employers often view such DOL Opinion Letters as not entirely relevant to their interpretation of their obligations under the Labor Code and the Wage Orders. However, because the FLSA sets a statutory and regulatory compliance "floor," it is critical to know and understand how the DOL is interpreting FLSA obligations that parallel those under the Labor Code and Wage Orders. There are too many DOL Opinion Letters to summarize here. We recommend that you periodically review the DOL's Opinion Letter web site at http://www.dol.gov/esa/whd/opinion/opinion.htm. Below, we summarize three Opinion Letters that we believe have general relevance to a broad array of employers.

Opinion Letter 2005-40, October 14, 2005

DOL clarifies meaning of "particular weight" in executive exemption.

The executive exemption under the FLSA and the Wage Or-

ders specify that employees who meet the exemption have the authority to hire or fire or to make suggestions and recommendations regarding hiring, firing, advancement, promotion or any other change in status that are given "particular weight." Neither federal nor state law requires that an exempt executive employee make the ultimate decisions regarding hiring, firing or other changes in employment status. Further, the recommendation of a higher level manager may receive greater weight. However, the meaning of the phrase "particular weight" is not readily apparent. This Opinion Letter indicates that the factors that the DOL will consider in analyzing the "particular weight" issue include "whether it is part of the employee's job to make such recommendations, the frequency with which such recommendations are made or requested, [and] the frequency with which the recommendations are relied upon . . . ." To the extent that California courts look to federal precedent to interpret identically-phrased state law obligations, this Opinion Letter may be relevant authority.

Opinion Letter 2005-50, November 5, 2005

DOL clarifies that degree requirement for learned professional exemption applies only to occupations that customarily require specialized academic training.

At the current time, the DLSE requires an advanced (post-bachelor's) degree to qualify for the learned professional exemption, whereas the DOL does not. However, the DOL does not permit employers to apply the learned professional exemption to a group of employees simply because the employer, for its own purposes, has elected to require specialized degrees of applicants and incumbents. According to this Opinion Letter: "Only occupations that customarily require specialized academic training are considered learned professional fields under the regulations; occupations that do not customarily require specialized academic training at the level intended by the regulations as a standard prerequisite to enter the field do not qualify for the learned professional exemption."

Opinion Letter 2005-54, December 16, 2005

Paralegals and legal assistants generally do not qualify for the professional exemption because an advanced specialized academic degree is not a standard prerequisite for entry into the field.

Both the DLSE and the DOL have issued opinion letters indicating the general view of both agencies that paralegals and legal assistants are not exempt professional employees. The regulations under the FLSA now specifically state: "Paralegals and legal assistants generally do not qualify as exempt learned professionals because an advanced specialized academic degree is not a standard prerequisite for entry into the field. Although many paralegals possess general four-year advanced degrees, most specialized paralegal programs are two-year associate degree programs from a community college or equivalent institution." Stated alternatively, because there are no minimum education or training requirements that a person must satisfy before using the occupational title "paralegal," "[t]his indicates that the occupation lacks a requirement of 'knowledge of an advanced type … customarily acquired by a prolonged course of specialized intellectual instruction' . . . . "

IV. California Legislative Digest

The 2005 legislative session turned out to be unusually mild in terms of wage and hour-related legislation. We summarize below two key legislative developments.

ASSEMBLY BILL 1093 (Direct Deposit of Wages and Payment of Computer Professionals on Salary Basis). AB 1093 was signed into law on August 30, 2005, and took effect on January 1, 2006. It amended portions of Labor Code sections 213 and 515.5. Employees contended that Labor Code section 213(d) barred employers from offering direct deposit of wages unless the employee's financial institution was headquartered or incorporated in California. AB 1093 amended Labor Code section 213 to make clear that pay by direct deposit is valid as long as the employee's financial institution has a physical location in California. In addition, the new law eliminates the automatic termination of the employee's direct deposit authorization upon termination of employment, which effectively had required payment of final wages in cash or by check. Thus, if an employee has elected direct deposit, the employer now will be allowed to pay the employee's final wages by direct deposit as well.

AB 1093 also addressed the counter-intuitive hourly pay requirement for an employee to be eligible for the computer professional exemption under Labor Code section 515.5. To qualify for the executive, administrative and professional exemptions, under both federal and state law, an employee must be paid on a salary basis. However, under California law, to qualify for the computer professional exemption, the employee must be paid on an "hourly" basis ($47.81 per hour as of January 1, 2006) for all hours worked. Since employers are familiar with the requirement that exempt employees must be paid on a salary basis, many employers misunderstood section 515.5 to mean that an employee who performs the required duties may qualify for the computer professional exemption as long as he or she receives a salary that is equal to the specified hourly rate based on a 40-hour workweek. As a result, some employers have been subjected to wage and hour class actions for misclassification of computer professional employees who perform the required duties but are paid on a salary and not an hourly basis.

AB 1093 now allows an employer to pay a computer professional on a salary basis, as long as the employee is paid "the annualized full-time salary equivalent of that rate, provided . . . that in each workweek the employee receives not less than forty-one ($41.00) per hour worked . . ." Labor Code § 515.5(a)(4).

At a minimum, the new language permits an employer to pay a salary covering the first 40 hours of work in a workweek at the indexed hourly rate (currently $47.81). The amendment does not permit employers to pay a higher weekly salary (for example, a salary based upon 45 times the indexed rate) and declare the excess above 40 hours to cover the hours worked up to the applicable limit of the salary. This is because the amendment uses the phrase "full-time." In the absence of that phrase, the amendment would have permitted salaries to cover the "annualized salary equivalent of that [indexed] rate," without restriction to the first 40 hours of work in the workweek. Finally, the amendment does not permit carry-over of any "excess" salary paid in one week to a subsequent week. Each workweek stands on its own.

ASSEMBLY BILL 1734 (Private Employment: Meal Periods). AB 1734 was signed into law on September 29, 2005. The bill amended Labor Code section 512, which requires employers to provide meal periods to employees during work periods of specified duration. Specifically, AB 1734 provided an exemption from the meal period requirement for certain employees in the motion picture and broadcasting industries who are covered by a valid collective bargaining agreement that contains specified terms. Labor Code section 512(d) now provides:

> If an employee in the motion picture industry or the broadcasting industry, as those industries are defined in Industrial Welfare Commission Wage Orders 11 and 12, is covered by a valid collective bargaining agreement that provides for meal periods and includes a monetary remedy if the employee does not receive a meal period required by the agreement, then the terms, conditions, and remedies of the agreement pertaining to meal periods apply in lieu of the applicable provisions pertaining to meal periods of subdivision (a) of this section, Section 226.7, and Industrial Welfare Commission Wage Orders 11 and 12.

V. California Labor Commissioner Developments

The DLSE underwent fundamental change in 2005. The early 2005 appointment of Donna Dell as the new California Labor Commissioner ushered in a period of internal review by the agency of its enforcement positions and opinion letters. The DLSE issued its first Precedent Decision, published two new opinion letters and withdrew ten such letters with little or no explanation. By December 2005, Ms. Dell had left the DLSE, replaced on an interim basis by the Chief Lawyer to the Department of Industrial Relations, Bob Jones. The DLSE's internal review is ongoing and will continue into 2006. The key DLSE developments in 2005 are described below.

Precedent Decision

On June 17, 2005, pursuant to the authority provided in Section 11425.60 of the California Government Code, the DLSE designated as a "precedent decision" the Order, Decision or Award of the Labor Commissioner in *Hartwig v. Orchard,* Case No. 12-56901RB (May 11, 2005). In *Hartwig,* the Labor Commissioner held that the one-hour payment in Section 226.7 of the California Labor Code is a penalty that is intended to enforce the meal and rest period requirements of the Industrial Welfare Commission Wage Orders, not a wage to compensate employees for labor performed. Accordingly, the DLSE's enforcement position is that the one-year statute of limitations applicable to statutory penalties found in Section 340 of the California Code of Civil Procedure applies to claims brought under Section 226.7.

According to the DLSE, a precedent decision is any decision that contains a significant legal or policy determination that is likely to recur. Precedent decisions are not subject to judicial review and are not "underground regulations." Such decisions are binding as to claims heard by Deputy Labor Commissioners and Hearing Officers.

New Opinion Letters

The DLSE issued two new opinion letters in 2005 regarding the following topics:

Tip Pooling: On September 8, 2005, the DLSE provided advice to a casino club concerning its mandatory tip pool policy that required employees receiving tip pool monies to contribute 15% of their actual tips to the tip pool. The DLSE concluded that such a policy is consistent with Labor Code section 350 and the California Supreme Court's decision in *Leighton v. Old Heidelberg, Ltd.,* 219 Cal. App. 3d 1062 (1990), provided that (1) tip pool participants are limited to those employees who contribute in the chain of the service bargained for by the patron, pursuant to evolving industry custom; and (2) employers or agents with the authority to hire or discharge any employee or supervise, direct or control the acts of employees do not collect, take or receive any part of the gratuities intended for the employee(s) as his or her own.

Personal Attendants: On November 23, 2005, the DLSE advised a vendor providing home health care services regarding the classification of employees as personal attendants, who

are exempt from the IWC Wage Order 15 except as to the minimum wage requirement. The DLSE affirmed its prior position that efforts which are essential for the client's independent living, such as bathing, dressing, taking clients for an outing, preparing meals, managing money, shopping for groceries or personal items, performing housework and isolated assistance with medications, are in the nature of personal attendant work so long as no "significant amount" of work other than the foregoing is required. However, the DLSE clarified and superceded an earlier opinion letter dated December 6, 2002, which erroneously deemed 20% of the work an individual is performing, rather than *exceeding* 20%, as a "significant amount." The DLSE also stressed that the determination of whether an employee meets the exemption for personal attendants is fact intensive and must be narrowly construed on a case-by-case basis.

Withdrawn Opinion Letters

Pursuant to Executive Order S-203, the DLSE is reviewing all previously-issued opinion letters, guidelines, criteria, bulletins, manuals, instructions, orders, or standards of general application to determine if they comply with the rulemaking procedures of the Administrative Procedures Act and *Tidewater Marine Western, Inc. v. Bradshaw,* 14 Cal. 4th 557 (1996). In 2005, the DLSE withdrew twelve opinion letters in connection with its internal review. The DLSE no longer posts these opinion letters on its website and they will be accorded no weight in administrative proceedings. The withdrawn opinion letters pertain to the following topics:

Alternative workweek schedules: On November 22, 2005, the DLSE withdrew three letters, 1990.02.22 (Beyond the regular schedule), 1991.04.11 (Regular schedule over 40 hours) and 1991.10.31 (Limits of accommodation). The DLSE provided no explanation for its withdrawal of these opinion letters.

Bonus pay: On November 22, 2005, the DLSE withdrew letter 1988.04.01 (Requirement to be on payroll at time of distribution). The DLSE provided no explanation for its withdrawal of this opinion letter.

Compensatory time off: On November 22, 2005, the DLSE withdrew letter 1996.05.29 (Limits, Labor Code § 204.3). The DLSE provided no explanation for its withdrawal of this opinion letter. However, as there were no material changes to the law regarding compensatory time off in 2005, the withdrawal decision may have been due to the letter's lengthy discussion regarding the limits of the agency's authority in the interpretation of California's wage and hour laws.

Exempt employees: On May 31, 2005, the DLSE withdrew letter 2002.08.30 (Wages; PTO/vacation use; PTO/vacation/salary reduction for partial day absence). In an internal memorandum to all DLSE staff, former Labor Commissioner Donna Dell determined that partial-day absence deductions may be taken from the banks of accrued vacation or personal time off of exempt employees. Such deductions are not inconsistent with paying exempt employees on a salaried basis because the employees receive paid vacation or PTO and thus do not forfeit any wages. However, salary deductions for partial-day absences remain prohibited.

Personal attendants: On November 29, 2005, the DLSE withdrew letter 2002.12.06 (IWC Order 15-2001). The DLSE superceded this letter with a new opinion letter issued on November 23, 2005, *see supra,* which clarified the maximum percentage of time personal attendants may perform other work in order to be deemed exempt from the protections of IWC Wage Order 15 (except the minimum wage requirement).

Vacation: On November 22, 2005, the DLSE withdrew three letters, 1993.02.16 (Earnings cap; reasonableness), 1993.02.16-1 (Earnings cap; reasonableness) and 1993.05.17 (Earnings cap; reasonableness; "Use it or lose it" not allowed). These letters pertained to the Labor Commissioner's prior interpretation of the "reasonable notice" requirement in Labor Code section 227.3 as requiring employees to receive at least nine months to use vacation after accruing it before a cap on accruals may be imposed. The DLSE withdrew these letters consistent with the Labor Commissioner's May 31, 2005 internal memorandum which stated that there was no legal authority or sound business basis for the nine-month rule. The Labor Commissioner concluded that the "reasonable notice" requirement in Labor Code section 227.3 may be satisfied by giving employees no less than one full fiscal quarter or ninety days, whichever is greater, to use vested vacation time.

Regulations

In 2005, the DLSE issued proposed regulations concerning the meal and rest period provisions contained in Sections 226.7 and 512 of the California Labor Code. On three occasions following public comment, the DLSE modified the text of the proposed regulations. The last period for public comment expired on July 25, 2005. The Governor's office announced in January 2006 that the meal and rest period regulations would not be submitted to the Office of Administrative Law for final approval, but that new draft regulations will be prepared and submitted later this year. In the meantime, the DLSE's website cautions employers to continue to follow the meal and rest period procedures contained in the Labor Code.

Note:
1. The meal period regulations that the DLSE withdrew included a clause that would have permitted meals to begin for employees in all industries no later than the end of the 6th hour of work. We are aware of no pending case that presents that issue for potential appellate consideration and the DLSE has not indicated whether its revised regulations will include the 6-hour concept once again.

Please contact any of the following Paul Hastings employment lawyers should you have questions regarding the contents of this client alert, or employment law in general.

Los Angeles:
Leslie L. Abbott 213-683-6310
leslieabbott@paulhastings.com

George W. Abele 213-683-6131
georgeabele@paulhastings.com

Orange County:
Stephen L. Berry 714-668-6246
stephenberry@paulhastings.com

Palo Alto:
Bradford K. Newman 650-320-1827
bradfordnewman@paulhastings.com

San Diego:
Mary C. Dollarhide 858-720-2660
marydollarhide@paulhastings.com

San Francisco:
Kirby C. Wilcox 415-856-7002
kirbywilcox@paulhastings.com

StayCurrent is published solely for the interests of friends and clients of Paul, Hastings, Janofsky & Walker LLP and should in no way be relied upon or construed as legal advice. For specific information on recent developments or particular factual situations, the opinion of legal counsel should be sought. Paul Hastings is a limited liability partnership. Copyright © 2006 Paul, Hastings, Janofsky & Walker LLP.