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COMMISSIONED EMPLOYEES MUST BE SEPARATELY COMPENSATED FOR REST BREAKS IN CALIFORNIA

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In *Vaquero v. Stoneledge Furniture LLC*, 9 Cal. App. 5th 98 (2017), a California court of appeal recently held for the first time that employers in California must separately compensate commissioned sales employees for rest breaks. Significantly, the court further held that employers cannot comply with this requirement by paying employees a recoverable draw, even if the draw is large enough to cover the minimum wage for all hours worked in each week.

This decision continues a trend toward making it increasingly complicated for employers in California to pay employees by commission or piece rate.

Background

Stoneledge, a retail furniture company, paid its sales associates on a commission basis. Associates did not receive separate compensation for non-selling time, such as time spent in meetings or rest breaks. However, associates did keep track of their non-selling time by clocking in and out of Stoneledge's electronic timekeeping system for shifts and meal breaks. Until early 2014, if a sales associate failed to earn at least $12.01 per hour in commissions in any pay period, Stoneledge paid the associate, as a draw or advance against future commissions, the difference between (a) his or her commissions and (b) the number of hours worked multiplied by $12.01 per hour. The draw could be "recovered" by Stoneledge in future weeks through deductions if and when the associate earned commissions exceeding the draw amount.

In March 2014, Stoneledge implemented a new commission agreement that paid sales associates a base hourly wage plus various incentive payments that were based on a percentage of sales. Under the new agreement, Stoneledge did not deduct any portion of an associate's base pay from the incentive payments.

Plaintiffs filed a putative class action on behalf of sales associates employed by Stoneledge from September 2009 through March 2014, when the previous commission agreement was in place. The complaint asserted claims for failure to provide paid rest breaks, failure to pay all wages owed upon termination, unfair business practices, and declaratory relief.

Plaintiffs based their rest break claim on California Labor Code section 226.7 and Wage Order No. 7, which applies to the mercantile industry. Section 226.7 provides in part: "An employer shall not require

an employee to work during a meal or rest or recovery period mandated pursuant to an applicable statute, or . . . order of the Industrial Welfare Commission."

Subdivision 12(A) of Wage Order No. 7 (and most of the other Wage Orders) states in part: "Every employer shall authorize and permit all employees to take rest periods . . . . Authorized rest period time shall be counted as hours worked *for which there shall be no deduction from wages*." (Emphasis added.)

The trial court granted Stoneledge's motion for summary judgment, finding that its pay system ensured that sales associates would be paid for all hours worked, including rest breaks. Plaintiffs appealed.

Discussion

Background on "Pay Averaging"

Over a decade ago, in *Armenta v. Osmose, Inc.*, 135 Cal. App. 4th 314 (2005), a California appellate court held that employers in California could not comply with California's minimum wage obligations merely by averaging an employee's hourly wage over a workweek. Instead, the minimum wage requirements apply to each separate hour that an employee works. In *Armenta*, the parties' collective bargaining agreement classified employee hours as productive or nonproductive, depending on whether the work was directly related to maintaining utility poles in the field. Employees were paid an hourly rate only for productive time; they were not compensated for nonproductive time, which included activities such as traveling between job sites and maintaining company vehicles. The employees' total pay for the week, on average, was more than enough to satisfy California's minimum wage for all hours worked in the week.

The *Armenta* court explained that, unlike the Fair Labor Standards Act – which allows employers to satisfy the federal minimum wage if an employee's total weekly pay, divided by the hours worked, averages out to at least the federal minimum wage – California law prohibits such pay averaging. Instead, California requires that non-exempt employees be paid at least the applicable minimum wage, if not the contractual hourly rate, for each and every compensable hour worked in the week.

More recently, courts have applied *Armenta*'s rule against pay averaging to employees in California who are compensated on a commission or piece-rate basis. These courts have held that employers must separately compensate employees – outside the commission or piece-rate pay – for various non-selling or other non-productive activities.

For example, in *Balasanyan v. Nordstrom, Inc.*, 913 F. Supp. 2d 1001 (S.D. Cal. 2012), Nordstrom guaranteed commissioned salespersons a minimum draw or commission for all "selling time," which it defined as including up to 30 minutes of stocking time and 40 minutes of pre-opening and post-closing time. Nordstrom separately paid an hourly rate for other non-selling time, which included stocking time over 30 minutes and pre-opening and post-closing activities over 40 minutes. A federal district court found that *Armenta* requires employers to pay commissioned salespeople at least minimum wage for time spent on activities that do not allow them to directly earn commissions, such as the stocking, pre-opening, or post-closing time that Nordstrom had sought to include in the calculation of its commission.

Similarly, in *Gonzalez v. Downtown LA Motors, LP*, 215 Cal. App. 4th 36 (2013), automotive service technicians were paid by piece rate based on repair tasks completed. They did not receive a piece rate

for non-repair tasks, such as obtaining parts or attending meetings. If a technician's piece-rate wages fell below the total number of hours the technician was at work, multiplied by the applicable minimum wage, the employer would supplement the technician's wages to cover the difference. The court found the reasoning of *Armenta* to be equally applicable to hourly workers and employees compensated on a piece-rate basis. It held that the technicians were entitled to separate hourly compensation for the time they spent waiting for repair work or performing other non-repair tasks; it was not proper for the company to treat this as being encompassed by the piece rate.

In *Bluford v. Safeway Stores, Inc.*, 216 Cal. App. 4th 864 (2013), the court held that "a piece-rate compensation formula that does not compensate separately for rest periods does not comply with California minimum wage law." Safeway paid its truck drivers based on mileage rates for trips taken, fixed rates for certain tasks, and hourly rates for other tasks and delays. None of these rates directly compensated drivers for rest breaks. Safeway argued that pay for rest breaks was specifically built into its mileage rates, but the court rejected this argument. It found that under *Armenta*, "rest periods must be separately compensated in a piece-rate system." The California Supreme Court declined to review the court of appeal's decision.

Employees Paid on Commission Must Be Separately Compensated for Rest Breaks

The *Vaquero* decision extended the *Bluford* holding on rest breaks to commission systems. The court agreed with *Bluford* that California's Wage Orders require employers to "separately compensate employees for rest periods if an employer's compensation plan does not already include a minimum hourly wage for such time." It concluded that the plain language of the Wage Order covers employees paid by commission, and nothing about commission compensation justifies treating commissioned employees differently from other employees.

The court found support for this interpretation in the DLSE Enforcement Policies and Interpretations Manual, which states that "if, as a result of the directions of the employer, the compensation received by piece rate or commissioned workers is reduced because they are precluded, by such directions of the employer, from earning either commissions or piece rate compensation during a period of time, the employee must be paid at least the minimum wage (or contract hourly rate if one exists) for the period of time the employee's opportunity to earn commissions or piece rate [is reduced]."

Stoneledge argued that because California's new piece-rate law, Labor Code section 226.2 – which requires employers to compensate piece-rate employees for rest, recovery, and other nonproductive time – does not apply to commissioned employees, the court should interpret the Wage Order as excluding employers from the duty to pay commissioned employees separately for rest breaks. The court rejected this contention.

A Recoverable Draw Does Not Separately Compensate Employees for Rest Breaks

The court next determined that Stoneledge's commission system did not separately compensate sales associates for rest breaks. The court observed that the formula Stoneledge used for determining commissions did not include any component that *directly* compensated sales associates for rest periods. According to the court, Stoneledge merely multiplied weekly sales by a commission rate and paid that commission amount *if* it exceeded the minimum contractual rate. As a result, associates who were paid commissions received the same amount of compensation regardless of whether they took rest breaks or

not. Whenever Stoneledge paid an associate the minimum contractual rate (the draw), it later clawed back (by deducting from future paychecks) wages advanced to compensate employees for their hours worked, including rest breaks.

In surprisingly harsh language, the court concluded that the draws under this pay system were not compensation for rest periods "because they were not compensation at all." Rather, they were, at best, "interest-free loans" because of the claw-back feature. As the court put it, "a loan for time spent resting" is not compensation for the rest period. To the contrary, "taking back money paid to the employee effectively reduces either rest period compensation or the contractual commission rate, both of which violate California law." The court summarized the issue this way:

> Thus, when Stoneledge paid an employee only a commission, that commission did not account for rest periods. When Stoneledge compensated an employee on an hourly basis (including for rest periods), the company took back that compensation in later pay periods. In neither situation was the employee separately compensated for rest periods.

The court therefore directed the trial court to enter an order denying Stoneledge's motion for summary judgment.

Conclusion

The *Vaquero* court explained that its decision "does not cast doubt on the legality of commission-based compensation." Oddly, the court also gave an assurance that its decision will not lead to "hoards of lazy sales associates."

While that may be true, the decision undoubtedly will complicate the job of employers in designing pay systems for commission-based employees, as is already true under Labor Code section 226.2 for piece-rate employees. Moreover, the court's decision leaves several questions unanswered, including how employers must calculate the rest break pay for commissioned employees, and whether a *non-recoverable* draw is sufficient to satisfy the requirement to pay for rest breaks.

Analytically, we believe that a properly-drafted *non-recoverable* draw against commissions – one that functions essentially as a guaranteed salary in an amount sufficient to pay employees at least minimum wage for all hours worked in a week (including rest break time) – would comply with *Vaquero*'s interpretation of the law, so long as commissions are paid to the extent they exceed the draw, without deduction. However, these issues are complicated, and employers in California should consult with competent counsel regarding their commission or piece-rate systems.

If you have any questions about the application of *Vaquero* to your policies and practices, please contact us.

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