



# Payment by Piece Rate:

## Employers Should Proceed With Caution

By Nicole Kamm

**T**HE PIECE RATE COMPENSATION SYSTEM has been commonly used in the auto technician, manufacturing, agricultural, truck driving, and other industries for years. Piece rate compensation means employees are paid a set amount based on the tasks performed, rather than hours worked. For example, a furniture assembly worker may be paid \$5.50 for each table assembled; a piece rate delivery driver may be paid 15 cents for each mile driven; or an auto technician may be paid \$15 for each oil change.

Piece rate compensation plans are intended to incentivize employees to be more productive—the more tasks completed, the more money earned. These types of compensation plans had generally been accepted, provided employees earned at least minimum wage for each hour worked. However, in 2013, two California appellate court decisions created new requirements for employers using piece rate compensation systems and called such plans, regardless of whether they guaranteed compensation of at least minimum wage for each hour worked, into question.

### **Gonzalez v. Downtown LA Motors LP**

In March 2013, the California Court of Appeal held that California's minimum wage law requires employers who compensate employees on a piece rate basis to also pay those employees a separate hourly wage for all other time worked, including work performed before, after and between piece rate tasks.

In *Gonzalez v. Downtown LA Motors LP*<sup>1</sup>, the employer was an automobile dealership that sold and serviced Mercedes-Benz automobiles. The dealership paid its automotive service technicians a flat rate ranging from \$17 to \$32, depending on the technician's experience, for every "flag hour" worked. "Flag hours" were assigned to every task the technician performed on an automobile and was intended to correspond to the actual amount of time the

technician would need to perform the task. For example, if a tire rotation was assigned two flag hours, a technician would be paid two times the flat rate for all tire rotations performed during the week. The technician who completes the repair task accrues the number of flag hours assigned to the task, regardless of how long the technician actually took to complete it.

Technicians accrued flag hours only when working on a repair task and regularly did not have repair work to do because there were not enough vehicles to service. When this occurred, technicians had to remain at work, and those who asked to leave were told to stay in case customers came in. While waiting for repair work, technicians were expected to perform various non-repair tasks, including obtaining parts, cleaning their work stations, attending meetings, traveling to other locations to pick up and return cars, reviewing service bulletins, and participating in online training.

To ensure technicians earned at least minimum wage, the dealership tracked all work time. If a technician's total compensation was less than minimum wage times the total number of hours worked, the dealership would supplement the technician's pay to meet the minimum wage requirement. Thus, the dealership argued its compensation plan was lawful because it ensured technicians always earned at least minimum wage for every hour worked.

The court found, however, that despite this assurance, the dealership's piece rate compensation plan violated California's minimum wage requirement because it did not pay employees for "all hours worked."

Relying on *Armenta v. Osmose, Inc.*<sup>2</sup>, a non-piece rate decision holding an employer may not "average" unpaid hours worked and hours worked at an hourly rate greater than minimum wage to meet the California minimum wage obligation, the court distinguished California's minimum wage requirement from federal law, and found the averaging method accepted under federal law could not be applied under California law.



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Under California law, “every employer shall pay to each employee...not less than the applicable minimum wage for all hours worked in the payroll period, whether the remuneration is measured by time, piece, commission, or otherwise.”

The court in *Downtown LA Motors* noted “hours worked” is defined as “the time during which an employee is subject to the control of the employer.” Therefore, because the dealership required technicians to remain on-site and perform other tasks between vehicle repairs, technicians must be paid a separate hourly rate for that time. Payment for such time was not accounted for in the dealership’s compensation plan, thus the court found it was unlawful.

The misstep in this case, however, is that in a piece rate system, the question is not “averaging” of hourly rates. Rather, it is whether the minimum wage obligation is met by an employer paying the greater of the piece rate versus actual hours worked at minimum wage.

By definition, a piece rate is not an hourly rate. Further, the California Labor Commissioner has historically followed federal law, under which the compensation system used by the dealership in this case appeared to be lawful. In fact, the California Division of Labor Standards Enforcement (DLSE) Manual recognizes that a piece rate system like the one used here is permissible. Nevertheless, the *Downtown LA Motors* court held employers may not “average” the piece rate compensation to satisfy the California minimum wage obligation.

In sum, the court held California law requires an employer that compensates an employee on a piece rate basis to also pay that employee a separate hourly minimum wage for time spent performing non-piece rate work.

### **Bluford v. Safeway**

While the *Downtown LA Motors* court did not expressly consider any obligation with respect to compensation requirements for paid rest breaks, another California Court of Appeal did shortly after. In *Bluford v. Safeway*<sup>3</sup>, the court held “a piece rate compensation formula that does not compensate separately for rest periods does not comply with California minimum wage law.”

Safeway employed a team of truck drivers to complete deliveries. It compensated the drivers primarily based on miles driven and the performance of specific tasks, a common form of piece rate compensation. Specifically, a driver’s pay was calculated based on mileage rates applied according to the number of miles driven, the time of day the trips were taken, and the locations where the trips began and ended; fixed rates for certain tasks (e.g., pallets delivered and picked up); an hourly rate for a predetermined amount of minutes for certain other tasks (e.g., 10 minutes at a fixed hourly rate for set-up time at each delivery location); and an hourly rate for delays (e.g., breakdowns, time spent at scales, and other delays beyond the drivers’ control).

Drivers were also given regular and timely breaks. Drivers alleged, however, this compensation system failed to provide them paid rest breaks as required by law because they were not paid a separate hourly wage for such breaks.

Safeway noted its policies specifically provided for paid rest breaks and the piece rates for driving miles included compensation for paid break time. Safeway further argued California law did not require employers who use piece rate or incentive-based compensation systems to put employees on the clock just to pay separately for rest periods.

The court disagreed; holding piece-rate compensation could not be “averaged” over non-piece rate idle (or rest break) time. On this basis, the *Bluford* court concluded drivers’ rest breaks could not be considered “paid” in violation of California law. In particular, the court held Safeway’s compensation system did not specifically account for rest periods or provide an ability to be paid for them. The court stated, “a piece rate compensation formula that does not compensate separately for rest periods does not comply with California minimum wage law.” The court based its ruling in part on a broad reading of the Industrial Welfare Commission (IWC) Wage Orders, which generally state “authorized rest periods shall be counted as hours worked for which there shall be no deduction from wages.” Safeway’s compensation plan, by contrast, did not provide any means by which an employee could verify rest periods were in fact paid.

In essence, the court found Safeway’s system relied on minimum wage averaging, which earlier courts had ruled impermissible. *Bluford* was the first court to expressly require employers to separately pay piece rate employees for rest breaks.

The employers in *Downtown LA Motors* and *Bluford* filed petitions for review with the California Supreme Court. Despite strong support from employer groups across the state, the Supreme Court recently denied the petitions.

### **Impact on Employers**

The *Downtown LA Motors* and *Bluford* decisions highlight the risks for any California employer using a piece rate or similar incentive-based pay structure.

Employers who pay employees on a piece rate basis and want to limit their potential exposure will have to modify their compensation plans to merge piece rate compensation systems with one that also pays hourly wages. Piece rate employees should now receive an additional hourly rate (at least minimum wage) for all time the employee spends performing non-piece rate tasks. Employers should also separately compensate piece rate workers for rest breaks and show such payment on the employees’ pay stubs.

Some employers may consider eliminating piece rate compensation plans altogether and providing a base hourly rate in addition to a bonus to reward employees for productivity. As long as the base rate is at least minimum wage, employers can argue this leaves no doubt whether each and every work hour, including rest breaks, are compensated.<sup>4</sup> ↩

<sup>1</sup> 215 Cal.App.4th 36 (2013).

<sup>2</sup> 135 Cal.App.4th 314 (2005).

<sup>3</sup> 216 Cal.App.4th 846 (2013).

<sup>4</sup> In this scenario, employers must factor any incentive-based bonus into the “regular rate of pay” for purposes of calculating overtime.