

THE RECORDER

In Practice: New Wage Laws Impact Classification



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On Sept. 25, Gov. Jerry Brown signed AB10, a bill that will raise California's minimum wage from \$8.00 an hour to \$10.00 an hour by 2016. The increase will occur incrementally, rising to \$9.00 an hour on July 1, 2014, and finally to \$10.00 an hour on January 1, 2016. While most employers understand that these increases affect their non-exempt hourly employees, they must keep in mind that they may also affect exempt employees. This is because California's test for whether an employee is properly classified as exempt is tied to the state's minimum wage. Thus, the increase creates a potential land mine for uninformed employers as

employees who do not meet the new minimum salary threshold would no longer be properly classified as exempt. This change in the law provides employers with an opportunity to review their exempt employees' job duties and ensure that they are properly classified as exempt.

Although often confusing, whether employees are paid a salary is not the determining factor for whether they are exempt. While under certain circumstances, non-exempt employees may be paid on a salary basis, exempt employees must always be paid a fixed salary. In order for an employee to be properly classified as exempt under the California Industrial Welfare Commission Orders, and thus stripped of many of its protections such as overtime and break requirements, the employer must demonstrate that the employee satisfies two tests: the "salary" test and the "duties" test.

THE SALARY TEST

The salary test, codified in California Labor Code §515, requires that an exempt employee earn at least two times the state minimum wage for full-time employment. Full-time employment is

defined as 40 hours per week, and thus the minimum wage threshold cannot be prorated if an employee works only part-time. Additionally, the salary test requires that an employee receive a set salary—that is, a predetermined amount that is not reduced due to variations in the quality or quantity of work performed.

Because the test is based upon the state's minimum wage, the minimum wage ordinances recently enacted in San Francisco and San Jose increasing the minimum wage in those cities do not have any effect on employees' exempt status. Based on California's current minimum wage of \$8.00 per hour, an employee must currently be paid at least \$2,773.33 per month or \$32,280 per year to satisfy the salary test. When the minimum wage increases to \$9.00 per hour next year, an exempt employee must be paid at least \$3,120 per month or \$37,440 per year. By 2016, an exempt employee must earn \$3,467 per month or \$41,600 per year. Overall, the result is an increase of \$9,320 or 29 percent.

THE DUTIES TEST

In addition to ensuring that all

employees classified as exempt meet the new minimum salary threshold, employers should also confirm their employees satisfy the duties test which examines the time the employee spends performing exempt duties. Even employees that are classified as exempt and meet the minimum salary threshold must also have job duties that meet the duties test. If an employee is classified as exempt but does not meet the duties test, the employer must convert the employee from exempt to non-exempt. Such a conversion usually raises red flags, alerting the employee that they were previously misclassified and thus potentially have a claim for unpaid overtime or meal and rest-break premiums. Misclassification suits may be very expensive for employers as the premiums and penalties may quickly add up. The increase in minimum wage and corresponding change in the salary test, however, would tend to deemphasize conversions that must be made.

While there are several different exemptions, the most common are the “white collar” exemptions for administrative, executive, and professional employees. The specific requirements of each of these exemptions are laid out in the IWC orders; all three of them require that the employee be “primarily engaged” in exempt duties (the “duties” test). An employee is primarily engaged in exempt duties if more than half of the employee’s time is spent on either exempt duties or duties that are directly and closely

related to exempt duties. This California “quantitative” test is therefore more protective of workers than the federal “qualitative” duties test where an employee’s “primary duty” may represent less than half of his or her regular work. In addition, each of the three white collar exemptions requires that an exempt employee customarily and regularly exercise discretion and independent judgment. This means that an employee should have the authority to make decisions, and may not simply be following delineated procedures or performing routine tasks.

In determining whether an exemption applies, employers should carefully consider the actual duties performed by the employee, not just the employee’s job description. Likewise, an impressive job title has no bearing on an employee’s classification. Simply labeling an employee a “manager” or “executive” does not make the employee exempt, nor does the parties’ agreement that the employee will be classified as such. Instead, the determination of whether an employee is exempt must be based on a review of whether the actual work performed meets the requirements of one of the exemptions. The employer bears the burden of establishing the exemption.

As the minimum wage increases over the next three years, employers should reevaluate their salaried employees. Any employee who does not meet the new minimum threshold needs either to be given

a raise or be reclassified as non-exempt. Determining whether an employee is exempt or non-exempt is the subject of many class actions and is one of the most important tasks the employer faces in complying with wage and hour laws. Misclassification is costly as it may result in liability for unpaid overtime for up to four years, premiums for missed meal and rest breaks, attorney’s fees, interest, and other penalties. Employers should seek legal advice when classifying employees as exempt.

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