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A LITTLER MENDELSON REPORT

APRIL 2007

An Analysis of Recent Developments & Trends

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Missed Meal & Rest Periods Will Cost Employers More Following California Supreme Court Decision

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Summary: In a unanimous decision, the California Supreme Court in *Murphy v. Kenneth Cole Productions* has found that Labor Code section 226.7's "additional hour of pay" for missed meal and rest periods is a wage and not a penalty.

In *Murphy v. Kenneth Cole Productions, Inc.*,[1] the California Supreme Court announced in a unanimous opinion that the premiums provided by section 226.7 of the California Labor Code for missed meal and rest periods are subject to a three- or potentially four-year statute of limitations rather than a one-year statute of limitations. Under section 226.7, a premium of one hour of pay is due when meal or rest periods are not provided as required in a work day. The Supreme Court characterized the premiums as wages that are subject to a three-year statute of limitations, and the statute of limitations may be extended to four years if the claim for the premiums is raised as an unfair business practice.[2] A one-year statute of limitations would have applied if the Supreme Court had concluded, as had two courts of appeal earlier concluded,[3] that the premiums are penalties.

Background Concerning Meal and Rest Periods

The California Industrial Welfare Commission (IWC) first issued wage orders mandating meal and rest periods in 1916 and 1932, respectively, out of concern with the health and welfare of employees. In 1999, the Legislature codified and restated the obligation to provide meal periods:

> An employer may not employ an employee for a work period of more than five hours per day without providing the employee with a meal period of not less than 30 minutes, except that if the total work period per day of the employee is no more than six hours, the meal period may be waived by mutual consent to both the employer and the employee. An employer may not employ an employee for a work period of more than 10 hours per day without providing the employee with a second meal period of not less than 30 minutes, except that if the total hours worked is no more than 12 hours, the second meal period may be waived by mutual consent of the employer and the employee only if the first meal period was not waived.[4]

[1] 2007 Cal. LEXIS 3596 (Apr. 16, 2007).

[2] Cal. Bus. & Prof. Code §§ 17200, et seq.; see *Wang v. Chinese Daily News, Inc.*, 435 F. Supp. 2d 1042 (C.D. Cal. 2006).

[3] *Mills v. Superior Court*, Cal. App. 4th 1547 (2006), *review granted*, and *Murphy v. Kenneth Cole Prods.*, 134 Cal. App. 4th 728 (2005), *reversed by Murphy v. Kenneth Cole Prods., Inc.*, No. S140308 (Apr. 16, 2007). *But see National Steel and Shipbuilding Co. v. Superior Court*, 135 Cal. App. 4th 1072 (2006), *review granted* (characterizing such payments as wages).

[4] Cal. Lab. Code § 512(a). Limited variations exist for union-represented employees in the wholesale baking; motion picture and broadcasting industries. Cal. Lab. Code § 512(c),(d).

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In order to meet the requirement to provide meal periods, a meal period must be at least 30 minutes in length, the employee must be relieved of all duty and the employee must be free to leave the premises.[5] The beginning and ending times of off-duty meal periods must be recorded in the employee's time records and such meal periods are not paid work time.[6]

Rest periods are not required by the Labor Code, but each Wage Order contains a requirement that employers "authorize and permit" ten minutes of "net" rest time for each four hours worked or major fraction thereof.[7] No rest period need be provided if an employee will work less than 3.5 hours in the day.[8] Rest periods need not be recorded in the employee's time records, but are paid work time.

In 2000, both the IWC and the California Legislature added a remedy for nonexempt employees who were not provided meal or rest periods as required by the IWC's wage orders. Specifically, section 226.7 provides for "one additional hour of pay at the employee's regular rate of compensation for each work day that the meal or rest period is not provided." Thus, for example, a meal period which is too short, which begins too late, or during which an employee is not relieved of all duty will result in an obligation to pay the premium. However, until the California Supreme Court's ruling, it has been unclear whether this statutory pay remedy is considered a "wage," subject to a three- or four-year statute of limitations or a "penalty," subject to a one-year statute of limitation. Indeed, the California Courts of Appeal and the federal courts had issued conflicting opinions concerning the issue.[9] The Labor Commissioner has likewise taken inconsistent positions, more recently concluding that a one-year statute of limitations should apply to such claims.

The Supreme Court in *Kenneth Cole* has now resolved the uncertainty by declaring that the pay remedy provided in section 226.7 is a wage subject to the longer statute of limitations.

Analysis of the Supreme Court's Opinion

Plaintiff John Murphy worked as a salary-paid store manager in a Kenneth Cole Productions (KCP) retail clothing store from June 2000 until his resignation in June 2002. He regularly worked 9- to 10- hour days during which he was only able to take an uninterrupted, duty-free meal period approximately once every two weeks. He rarely, if ever, had the opportunity to take a rest period and, on occasion, was unable to go to the restroom. He later filed a complaint with the California Labor Commissioner and ultimately took his case to trial in the San Francisco Superior Court. The superior court concluded that Murphy did not qualify as an overtime-exempt, white-collar employee and awarded Murphy unpaid overtime, premiums payments for missed meal and rest periods based upon a three-year statute of limitations, penalties for failing to furnish itemized pay statements, waiting time penalties, and prejudgment interest. KCP appealed and the court of appeal reversed in part, holding that Labor Code section 226.7 premiums for meal and rest period violations are penalties subject to a one-year statute of limitations. Murphy then appealed to the California Supreme Court.

The Supreme Court concluded that section 226.7's plain language, its administrative and legislative history, and its compensatory purpose compel the conclusion that the premiums for missed meal and rest periods are wages, and that the statute of limitations for pursuing unpaid wages applies.

The court first looked to the definition of "wages" in the California Labor Code and the text of section 226.7. The Labor Code defines "wages" as "all amounts for labor performed by

[5] Bono Enters., Inc. v. Bradshaw, 32 Cal. App. 4th 968 (1995).

[6] *Cf.*, Cal. Code Regs. tit. 8, § 11010(7)(A)(3) (Wage Order 1 ¶ 7(A)(3)).[7] *Cf.*, Cal. Code Regs. tit. 8, § 11010(12)(A) (Wage Order 1 ¶ 12(A)). "Net" rest time is generally construed to be the time available after an employee reaches a suitable location to take a rest break. Some variations in the obligation to provide rest periods appears in Wage Order 5 (Cal. Code Regs. tit. 8, § 11050(12)(C)), Wage Order 10 (Cal. Code Regs. tit. 8, § 11100(12)(C)), and Wage Order 14 (Cal. Code Regs. tit. 8, § 11140(12). No rest period provision appears in Wage Order 17 (Cal. Code Regs. tit. 8, § 11170).

[8] *Id.* The obligation to provide a rest period for every four hours of work or major fraction thereof, when combined with the absence of an obligation to provide rest periods for brief periods of work, results in an obligation to provide one rest period if an employee works from 3.5 to 6 hours, two rest periods if an employee works from 6 to 10 hours, and so on.

[9] *Compare, Wang* 435 F. Supp. 2d 1042, *and Corder v. Houston Rests., Inc.*, 424 F. Supp. 2d 1205 (C.D. Cal. 2006) (concluding that the premiums were a penalty).

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employees ... whether the amount is fixed or ascertained by the standard of the time, task, piece, commission basis or other method of calculation."[10] Courts have also recognized that "wages" include those benefits to which an employee is entitled as part of his or her compensation.[11] The text of section 226.7 requires that employees be paid "one additional hour of pay" for each work day that they are required to work through a meal or rest period. Noting that "pay" is defined in a dictionary as "money [given] in return for goods or services rendered," the court stated that the "one additional hour of pay" in section 226.7 is consistent with the Labor Code's definition of "wages."

Because the court also concluded that an "additional hour of pay" in section 226.7 could also be characterized as a penalty, the court reviewed the administrative and legislative history of section 226.7 to determine whether the premiums were intended to be wages or penalties. The court addressed several aspects of that history and again concluded that the Legislature intended the premiums to be "wages."

First, the court noted that the provision regarding meal and rest periods is intended to address the Legislature's concern with the health and welfare of employees. For example, the court noted that employees denied their rest and meal periods face a greater risk of work-related accidents and increased stress, especially low-wage workers who often perform manual labor. It is in this context the Assembly considered adding both a specifically designated penalty *and* a separate wage payment to employees. However, the Senate later amended the bill by deleting the penalty provision and modifying the premium payment provision to be as it is now found in section 226.7. The court concluded that "the act should not be interpreted to include what was left out."

Second, the court noted that the "vast majority" of California statutes imposing a penalty provide for a fixed, arbitrary amount as the penalty. Such a fixed, arbitrary amount, the court further stated, is unlike the remedy contained in section 226.7, which provides compensation measured by the employee's rate of pay for his or her working through a meal or rest period.

Third, the Senate Rules Committee had explained its view during the legislative process that the pay remedy would be considered wages: "[f]ailure to provide such meal and rest periods would subject an employer to *paying the worker one hour of wages* for each worked day when rest periods were not offered" (emphasis in original).

Fourth, the court stated that under section 226.7 an employee is entitled to the additional hour of pay immediately upon being forced to miss a rest or meal period. Thus, a payment owed pursuant to section 226.7 is akin to an employee's immediate entitlement to payment of wages for overtime rather than comparable to a penalty that may be imposed only after an official administrative or judicial proceeding.

Finally, the court stated that had the Legislature intended section 226.7 to be governed by a one-year statute of limitations, the Legislature knew it could have so indicated by unambiguously labeling it a "penalty." It did not do so.

As noted, a lower court of appeal in *Mills* had come to precisely the opposite conclusion regarding the legislative history:

> [I]n agreeing to the Senate's change [to the original bill], the Assembly continued to describe the additional payment as a 'penalty.' ... [T]o the very end of the legislative process the additional money an employer would have to pay for failing to ensure mandated break periods was considered a penalty.[12]

Although the Supreme Court in *Kenneth Cole* acknowledged that the legislative history of section 226.7 and transcripts of IWC hearing at which the pay remedy was discussed contain numerous references to the word "penalty," the court nevertheless concluded that the statements characterized the premiums as a "penalty" in the sense that overtime is a "penalty" and overtime is, ultimately, a wage.

The Supreme Court concluded that the central purpose of section 226.7 is to compensate employees who work through, and do not receive, their meal and rest periods with a corollary purpose of ensuring employer meal and rest period compliance. This conclu-

[10] Cal. Lab. Code § 200 (a).

[11] *E.g. Suastez v. Plastic Dress-Up Co.*, 31 Cal. 3d 774, 780 (1982); *Department of Industrial Relations v. UI Video Stores, Inc.*, 55 Cal App. 4th 1084, 1091 (1997).

[12] *Mills*, 135 Cal. App. 4th at 1553

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sion must also be contrasted with the conclusion in *Mills* that: "[T]he failure of section 226.7 to correlate the payment due to any additional labor performed by an employee undermines any argument the payment is a wage."[13] In contrast, the Supreme Court concluded that the Legislature may assign different amounts to compensate employees for certain kinds of work without converting that amount into a penalty.

In sum, the Supreme Court found that the foregoing administrative and legislative history compelled the conclusion that the Legislature intended the payment provisions of section 226.7 to be compensatory wages subject to a three-year or four-year statute of limitations and not a penalty.

Looking Forward

Immediate Consequences

The immediate consequences of the *Kenneth Cole* decision are significant.

An employer must pay all of the wages that are due for a pay period on the payday for that pay period.[14] With the declaration that meal period remedies and rest period remedies are wages, an employer must pay the premiums for missed meal and rest periods on the payday for the pay period in which the meal periods or rest periods were missed. When paying the premiums, an employer must be mindful that the premiums are calculated as an hour of pay at the employee's regular rate of pay, not an hour of pay at the employee's straight-time rate of pay.[15]

The starting and ending times of meal periods must be recorded in an employee's time record.[16] In the absence of a recorded meal period entry, an employer will likely bear the burden of showing that a meal period was taken.

Meal and rest period premiums will, as wages, now be subject to the withholding of income and payroll taxes. The Internal Revenue Service had previously issued a letter opinion that the premiums were subject to taxation as wages.[17] With the *Kenneth Cole* decision, the position of the IRS is no longer open to question.

The need to pay and tax the premiums will require, as a practical matter, that the premiums appear on an employee's earning statement. Such premiums, insofar as they are related at least in part to the hours worked, also fall within the categories of information that must be itemized on an employee's earnings statement.[18]

A further question is whether meal and rest period premiums must be included in the regular rate of pay on which overtime is calculated. While the Labor Commissioner had informally opined that such premiums are not included in the regular rate of pay, the remedies for missed meal and rest periods are akin to the premiums paid for working off-hours shifts, and such shift differential premiums are included in the overtime calculation.[19] Inasmuch as the meal and rest period premiums are pay for work actually performed, it is difficult to exclude such amounts from the regular rate on the basis that pay for time not worked, such as minimum reporting pay, is excluded from the regular rate of pay.

Finally, the failure to timely pay meal and rest period premiums can now give rise to penalties for the late payment of wages. Section 203 of the California Labor Code provides a penalty of up to thirty days' pay for a terminated employee whose employer willfully failed to pay all wages when due. Section 210 of the Labor Code provides a civil penalty which is to be paid to the state for every payday on which all wages are not paid. In addition, Labor Code section 558 provides a civil penalty that is to be paid to the state for every violation of a provision of a Wage Order regarding hours and days of work. With the enactment of the Private Attorneys General Act, an employee can seek recovery of the penalties that would otherwise be paid to the state. And, the Private Attorneys General Act specifically provides an employee the ability to pursue class action claims and to recover attorneys' fees for successfully pursuing such claims.[20]

[13] *Id.* at 1553-54.
[14] Cal. Lab. Code §§ 204, et seq.
[15] *Id.* § 226.7(b).
[16] *See, e.g.*, Cal. Code Regs. tit. 8, § 11010(7)(A)(3) (Wage Order 1 ¶ 7(A)(3)).
[17] *See*, IRS Information Letter 2006-0094 (June 30, 2005)
[18] Cal. Lab. Code § 226(a).
[19] 29 C.F.R. § 778.223
[20] Cal. Lab. Code §§ 2699, *et seq.*

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Questions Regarding Meal and Rest Periods

The decision in *Kenneth Cole* will create additional pressure to find answers for unresolved questions regarding meal and rest periods.

One of the principal questions is whether an employer must actually make an employee take a meal period, or the meal period simply must be "provided" in the sense that an employee is given the opportunity to take a meal period. The Labor Commissioner has generally concluded that an employer must undertake whatever steps are necessary to ensure that an employee actually takes a meal period of sufficient duration within the required time limit. With respect to rest periods, the Labor Commissioner has consistently concluded that an employer's obligation is limited to providing the opportunity to take a rest period. While the Wage Orders provide that "no employer may employ any person" for longer than the specified time without providing a meal period and an employer only need "authorize and permit" rest periods, the premiums for both missed meal periods and missed rest periods are triggered by the same standard: an employer's failure to "provide" the required meal or rest period.[21]

The decision in *Bearden vs. U.S. Borax, Inc.*[22] raises further questions regarding meal periods. In *Bearden*, the court concluded that the Industrial Welfare Commission could not lessen an employer's obligation to provide meal periods as set out in the Labor Code.[23] One of the most significant differences between the Industrial Welfare Commission's Wage Orders and the Labor Code is that Wage Orders provide for on-duty meal periods, but the Labor Code does not.[24] The decision in Bearden jeopardizes the use of on-duty meal periods to allow an employee to remain on duty when no other individual is available to relieve the employee.

The on-duty meal period provision is, if valid, a limited means of addressing an employer's concerns. It is only possible to enter into an on-duty meal period agreement where the nature of the employees' duties precludes the employee from being relieved of all duty during a meal period.[25] Any such agreement must be in writing, be signed by the employee, and must state that it is revocable by the employee either immediately, or upon one day's notice if the employee is engaged in the health care industry and working shifts of more than eight hours.[26] Once revoked, issues arise as to whether a new, signed writing is needed for an employee to work on-duty meal periods in the future. Ultimately, the on-duty meal period provision is a "catch 22": an on-duty meal period agreement is permissible only when the nature of the employee's duties precludes the employee from being relieved for meal periods, but an employee is free to revoke an on-duty meal period agreement at any time, thus obligating the employer to allow the employee to take the time off.

The *Bearden* decision also raises an issue of potentially broad sweep: whether meal periods must be provided to overtime-exempt, white-collar employees. While the Wage Orders exclude such employees from the receipt of meal periods, the Labor Code has no such exclusion.[27]

Questions also linger as to how and exactly when meal periods have to be provided. While the most common reading of the meal period provision of the Wage Order suggests that a meal period must commence by the end of the fifth hour of work, other interpretations are possible, including the sometimes offered interpretation that a meal period must be completed within five hours of work.

Additional questions exist with respect to the provision of second meal periods in extended workdays. Wage Orders 4, 5, 12 and 14 provide that a meal period can be waived whenever six hours of work will complete an employee's work for the day, but do not have the provision regarding the waiver of the second meal period that appears in the Labor Code.[28] The Labor Code states that a second meal period can be waived by an employee who will

21 Cal. Lab. Code § 226.7(b).

22 138 Cal. App. 4th 429 (2006).

23 *Bearden*, 138 Cal. App. 4th at 438. In so concluding, *Bearden* invalidated the exemption of union represented employees from the meal period requirements of Wage Order 16. A similar meal period provision appears in Wage Order 1.

24 *Compare* Cal. Code. Regs. tit. 8,§ 11010(11)(C) (Wage Order 1 ¶ (11)(C)) *and* Cal. Lab. Code § 226.7(a).

25 *See, e.g* Cal. Code. Regs. tit. 8,§ 11010(7)(A)(3) (Wage Order 1 ¶ 7(A)(3)).

26 *Id., see, e.g,.*, Cal. Code Regs. tit. 8, 11050(11)(D), Wage Order 5 ¶ (11)(D).

27 *Compare* Cal. Code Regs. tit. 8, 11010(1)(A) (Wage Order 1 ¶ (1)(A)) *and* Cal. Lab. Code § 226.7(a).

28 Cal. Code. Regs. tit. 8,§ 11040(11)(A) (Wage Order 4 ¶ 11(A)); Cal. Code. Regs. tit. 8,§ 11050(11)(A) (Wage Order 5 ¶ 11(A)); Cal. Code. Regs. tit. 8,§ 11120(11)(A) (Wage Order 12 ¶ 11(A)); Cal. Code. Regs. tit. 8,§ 11140(11) (Wage Order 14 ¶ 11).

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work between ten and twelve hours in a day only if the first meal period is not waived.[29] The provisions of Wage Orders 4, 5, 12 and 14 can be reconciled with the Labor Code if a waiver of a meal period under Wage Orders 4 and 5 where six hours of work will finish an employee's work for the day is limited to the circumstances where the employee has not waived any required meal period that was to occur earlier in the day.

Employers must be mindful that rest periods must, insofar as practicable, be provided in the middle of work periods. Scheduling meal periods at other times of the day for the simple convenience of the employer may be problematic.[30]

Finally, the amount of the meal and rest period premiums due, and the ultimate impact of the *Kenneth Cole* decision will be determined by whether separate premiums are due for missing a meal period and a rest period in a day or whether only a single premium is due for missing both a meal and a rest period in a day. One federal court concluded that only a single premium is due if both a meal and a rest period are missed in the same day, but the federal court's opinion is not binding on a state court.[31]

Compliance Solutions

The *Kenneth Cole* decision, when magnified by the effect of the Private Attorneys General Act, mandates action by employers.

First, employers should make employees allies in the search for compliance. Only by educating employees as to their rights and their need to comply with the employer's meal and rest period policies can compliance be obtained. Supervisors, too, must be trained regarding the provision of meal and rest periods. Such training may be conveniently provided in an electronic format. Employers should maintain effective handbook polices that advise employees of the obligation to take meal and rest periods.

Second, employers should allocate the staffing and budget resources necessary to achieve compliance. Plaintiff's counsel in class actions regarding meal and rest periods often focus on incentive plans for supervisors that provide an incentive for supervisor's to achieve labor cost targets without regard to meal and rest periods. Incentive plans that only provide a reward for achieving labor cost targets should be modified to include an incentive for achieving meal and rest period compliance.

Third, employers should take the steps necessary to prove compliance with their meal and rest period obligations. Employers should ensure that meal periods are accurately recorded on time cards. Furthermore, employers should take steps to ensure that any rounding that occurs in a timekeeping system does not inaccurately reflect that a meal period of sufficient length was taken when not taken, or that a meal period of sufficient length was not taken when one was, in fact, taken. It may be appropriate to add postings next to time clocks, pop-up messages in electronic timekeeping systems, and reminders on earnings statements of the importance of taking meal and rest periods and accurately recording when such periods are and are not taken.

While rest periods need not be recorded on time cards, it may be advisable to have a certification signed by an employee that rest periods were provided. An employer that wishes to go an additional step and actually record rest periods must remain diligent in doing so or the absence of rest period entries may create an inference that rest periods were not taken.

Fourth, employers should allocate resources both to ensure compliance with the obligation to pay meal and rest period premiums. It is essential that employers designate someone in the payroll processing operation to review timecards and pay the appropriate premiums. There should be an effective means of having payroll communicate with supervisors regarding missed meal periods. Enhancements in payroll software may offer some solutions to this process. Opening compliance hotlines to concerns regarding the provision of meal and rest periods will also help achieve compliance.

Fifth, employers should periodically audit the provision of meal and rest periods to ensure that the education of employees and supervisors, the allocation of resources to payroll, and the steps taken to prove that meal and rest periods are provided all work together to produce compliance. Employers that now suspect – or know – of meal and rest period compliance issues may find it advantageous to audit and pay any premiums due in order to mini-

[29] Cal. Lab. Code § 512(a)

[30] An employer may seek an exemption from the Labor Commissioner from the obligation to provide rest periods, but cannot seek an exemption from the obligation to provide meal periods. *Cf.*, Cal. Code. Regs. tit. 8, § 11010(17) (Wage Order 1 ¶ (17)).

[31] *Corder*, 424 F. Supp. 2d at 1207.

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mize the prospect of litigation.

Finally, when all the steps taken to ensure compliance unfortunately fail, employers should make sure that any counseling, negative evaluation or discipline is directed to the employee *and* supervisor responsible, without a presumption that the employee is at fault.

The Distant Future

Meal and rest period lawsuits will likely plague employers through the distant future. Industries particularly at risk will be trucking, industries which require one person to be on duty at a time such as small retail stores and security operations, and other businesses that have employees who work unsupervised.

With the resolution of the issue regarding meal and rest period remedies are wages, the pressure on the Division of Labor Standards Enforcement to issue effective regulations, and the pressure on the legislature to address those *bona fide* circumstances in which some compromise in the meal period obligation is necessary must be addressed.

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