STATE OF CALIFORNIA GRAY DAVIS, Governor

DEPARTMENT OF INDUSTRIAL RELATIONS
DIVISION OF LABOR STANDARDS ENFORCEMENT
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January 15, 2003

Gregory J. Smith, Esq.
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Re: **Payment Of Wages Earned Based On Employer's Receipt Of Payment For Services Rendered; Exempt Status Of Professionals** (00236)

Dear Mr. Stirrup:

Your letter of January 3, 2003, together with attachments has been forwarded to this office for response on behalf of the Division of Labor Standards Enforcement.

In your letter you state that your client is a corporation that operates a psychological treatment center in California. The facility employs three categories of employees: (1) Licensed Psychologists; (2) Psychological Assistants who are unlicensed but working under the direction of a licensed psychologist pending receipt of their license; and (3) Interns/Students studying to become licensed psychologists.

The employment agreement provides that the licensed psychologists and psychological assistants wages are based on a percentage of the total amount of the charge made by the employer to the patient for the services rendered by the employee. The employee, however, receives only a percentage of the "collections" received by the employer. The collections, of course, represent the total amount received by the employer for the services rendered by the employee to the patient.

The collections may be received directly from the patient or from the patient's insurance carrier. The payments are almost always at least three months behind the date the service was provided to the patient. In some cases, patients do not pay their bills or the insurance carrier refuses payment. If payment is not collected by the employer for either reason, the employee does not receive the wages earned for performing the services.

Your letter states that during the first few months of a new employee's employment, the fees collected and paid from patients do not rise to the level required of the required monthly wage to qualify the individual for the "professional" exemption.

After the first few months most of the workers receive the minimum monthly wage to qualify for the exemption; but in some months the amount may fall below the minimum requirement. In other months, based on the collections received, the wage received by these employees exceeds the minimum required for the exemption and, for the year, the figure exceeds the amount of $28,080.00[1].

Your letter seeks an opinion on four separate question, two of which are related to the issue of time for payment of wages earned and two of which relate to the question of the possible exemption of professional employees:

1. May workers who are paid on a piece rate basis for services performed be paid the wage owed for the services performed when the payment for the services is received by the employer; or must the wages earned for particular services performed in a particular payroll period be paid in at the end of that pay period?

2. May workers be denied payment of the piece rate they earned for services performed if, ultimately, the payment for those services is not received by the employer?

3. If the yearly income of a putative professional employee will be in excess of $28,080.00, is the employer in compliance with California law by treating the employee as exempt (if the worker otherwise meets the exempt standards) during any period of time during which the worker receives less than the minimum salary of two times the state minimum wage for any month?
4. Are psychological assistants properly treated as exempt employees.

The Exempt Status Of The Employees

[1]The "salary" required to be paid in order to meet the exemption requirements must be based on receipt, on regularly scheduled paydays consistent with California law, a predetermined amount constituting all or part of his compensation, which sum totals at least two times the California minimum wage (based on a monthly salary equivalent determined by multiplying the monthly wage of not less than $2,340.00 times twelve and dividing that product by 52 to reach a weekly salary). As will be discussed below, regardless of any other problems, the pay plan you submit does not meet these requirements since the "salary" is not based on a predetermined amount. We might add that this plan would not comply with the federal regulations which the DLSE uses as a guide.

Initially, we must point out that the plan you submit would not comply with the requirement that an exempt employee "receives each week a predetermined sum constituting all or part of his compensation which predetermined amount is not less than the remuneration required by the specific order the employee is subject to, multiplied by 12 and divided by 52." (See O.L. 2002.03.01) This interpretation is based in large part on the provisions of the federal regulations. The pay plan you describe does not provide for a salary in a predetermined sum; but instead, is based on the amount of collections recovered by the employer.

Consequently, we need not address the questions raised in your question number 4 regarding the exempt status of the unlicensed psychological assistants inasmuch as the pay plan would preclude those employees and, indeed, even the licensed psychologists from being exempt in any event.

The Payment Plan

The wage earned by the affected employees is based on a piece rate. The payment is not a "commission" since, in California, the courts have concluded that Labor Code § 204.1 sets up two requirements, both of which must be met before a compensation scheme is deemed to constitute "commission wages." First, the employees must be involved principally in *selling* a product or service, not making the product or rendering the service. Second, the amount of their compensation must be a percent of the price of the product or service. (*Keyes Motors v. DLSE* (1987) 197 Cal.App.3d 557) The employees you describe are engaged in performing a service, not selling a service.

Quite clearly, the wages of the affected employees are "earned" for the services they perform for the client(s), else there would be no other way to ascertain the amount owed to the employee. Your letter impliedly acknowledges this fact when you ask: "May a clinician's payment for seeing a patient during the pay period be delayed until a later pay period when payment is received from the patient's insurance carrier?" (Emphasis added)

What the proposed pay plan does is pass on the employer's normal cost of doing business (i.e., collection of bills) to the employees. Such cost shifts are not allowed in California. The California Supreme Court in the case of *Kerr's Catering v. DIR* (1962) 57 Cal.2d 319, first recognized the fact that it would be unfair to allot the employer's normal costs of doing business to the employee thus making the employees "insurers of its business losses." *Id.* at 327-328. The court reasoned that the deductions must be disapproved because of "the reliance of the employee on receiving his expected wage, whether it be computed upon the basis of a set minimum, a piece rate, or a

commission." (*Id.* at 329) These same admonitions have been repeated time and again by the California courts. (*Hudgins v. Neiman Marcus Group, Inc.* (1995) 34 Cal.App.4th 1109, 1112; *Quillian v. Lion Oil* (1979) 96 Cal.App.3d 156, 162)

The cost of losses incurred as a result of non-collectibles is recognized as an ordinary cost of doing business. The pay plan which you submit directly links the collection of bills owed to the employer with the amount received by the employer for the services performed by the employee at the direction of the employer.

It has long been recognized that a commission plan may provide that the sale is not complete until the pay is received for the goods or services sold. Thus, these commission agreements may withhold the commission due on the sale from the salesperson pending receipt of the payment or, may provide that the employer may recover back any commissions theretofore paid from future commissions owed to the employee.

However, the wage owed these employees is based upon the rendering of services to the patients of the employer. Unlike the sale transaction upon which the commission wage is based which is not complete until the quid pro quo (payment) is received, the rendering of the services completes this transaction. Under the pay plan proposed, if the employee fails to receive full payment it is not because the services were imperfect or incomplete, but simply because the customer (patient) or their insurance carrier refused to pay the employer the full amount billed.

If we were to extrapolate this pay plan to other employment situations perhaps, it would be easier to understand why the plan is flawed. For instance, it could be argued that a pay plan such as this could be imposed upon farm workers who often work on a piece rate. The argument could be made that the farmer lacks sufficient capital to pay the farm workers before he is paid by the wholesaler to whom he sells the produce. If the wholesaler, for whatever reason, failed to pay the farmer the full price asked for the produce, the farm worker would be in the unenviable situation of being forced to accept the percentage of the price recovered by the farmer instead of the piece rate he earned. The farmer would, in fact, have instituted a system whereby the farm workers are the insurers of the farmer business.

This same situation could apply to any number of employment relationships where the method of payment is based on a calculation of the number of pieces made or services completed (e.g., framing carpenters, auto mechanics, factory workers, dental technicians, etc.) To quote the language used by the California Supreme Court when addressing a plan which was similarly defective: "The mere recitation of the

logical consequences of the employers' argument, of course, signals the extreme tenuousness of the employers' contention." (*Industrial Welfare Commission v. Superior Court* (1980) 27 Cal.3d 690, 726)

Since, as even your letter admits, it is the piece rate that is designed to compensate the employee for the services rendered to the patient, the piece rate is earned upon the rendering of the services. In this regard, Labor Code § 204 provides, in pertinent part:

> "All wages, other than those mentioned in Section 201, 202, 204.1, or 204.2, earned by any person in any employment are due and payable twice during each calendar month, on days designated in advance by the employer as the regular paydays. Labor performed between the 1st and 15th days, inclusive, of any calendar month shall be paid for between the 16th and the 26th day of the month during which the labor was performed, and labor performed between the 16th and the last day, inclusive, of any calendar month, shall be paid for between the 1st and 10th day of the following month...Notwithstanding any other provision of this section, all wages earned for labor in excess of the normal work period shall be paid no later than the payday for the next regular payroll period."

The provisions of the California Labor Code are clear and unambiguous. If the wage is earned in the pay period, the wage must be paid, pursuant to Section 204, at the regularly scheduled payday as provided in the statute.

To summarize:

(1) In order to be exempt from the California overtime requirements under the managerial, administrative or professional exemption, the employee, in addition to any other duties or licensing test, must receive a salary of a predetermined amount for each week of work which meets or exceeds the twice the California minimum wage.

(2) A payment plan which is based on a plan whereby the employee receives a percentage of the amount charged for the services rendered that plan is a piece rate; the amount is earned for performing the service, and the amount earned must be paid at the regularly scheduled pay day for the payroll period when the amount was earned.

We hope this adequately addresses the issues raised in your letter and the attachments contained therein. Thank you for your interest in

California labor law.

Yours truly,

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