

## It's Not The End Of The Piece Rate Pay System In Calif.

*Law360, New York (February 11, 2014, 4:40 PM ET)* -- Recent decisions in California (Gonzalez v. Downtown LA Motors and Bluford v. Safeway Stores Inc. along with Armenta v. Osmose Inc.) requiring that employers pay employees the minimum wage for each increment of work time, including nonproductive time and rest breaks, have significantly impacted employers' pay policies. These decisions are thought to have made it more difficult, if not impossible, for employers to maintain the piece rate pay system. This system, in principle, pays employees based on productive time, which is not necessarily all hours worked. The most popular advice from employment attorneys to employers is to convert their piece rate system to an hourly pay system which may include extra performance-based bonus payments.

The piece rate system compensates employees based on their production or performance rather than hours worked, as in the hourly pay system. The piece rate system incentivizes employees by awarding harder working and more productive individuals with greater earnings, which is why this system is so popular in industries where output is easily measured.

Although it is up to each employer to determine how to change their pay system to comply with the recent rulings regarding California minimum wage, I would argue that they can do so, and still maintain the incentive structure of a piece rate pay system that rewards highly productive employees. In order to accomplish this, employers can switch to a hybrid pay system which pays employees at least the California minimum hourly rate for all hours worked in addition to a performance bonus, so total earnings would be comparable to earnings under a piece rate system. The following example demonstrates one such hybrid system.

### Piece Rate Pay System

Company XYZ currently uses the piece rate pay system where an employee is paid \$2 per completed piece. If this piece rate pay is less than what California minimum wage would require, then the company guarantees to pay California minimum wage for all hours worked by the employee. If an employee works overtime, then a premium is paid for the overtime hours worked using his regular rate. Suppose that the following two employees worked only one day during a given work week.

Employee A worked 10 hours in one day and, therefore, had two hours of overtime. He had nine productive hours where he was making pieces and one nonproductive hour waiting for an assignment. During his nine productive hours, he produced a total of 20 pieces making his piece rate pay \$40. However, this is lower than the \$80 that is required by the California minimum wage. Therefore, he would be paid \$80 and should be compensated at a premium rate for the two hours of overtime. In this case, his regular rate of pay is \$8 per hour because he earned \$80 for 10 hours worked. Thus, the

overtime premium is \$8, which is half of the regular rate times overtime hours. Employee A's total compensation is \$88.

Employee B also worked 10 hours — eight straight hours and two overtime hours. Of the 10 hours, nine were productive hours, while the remaining hour was nonproductive. During his nine productive hours, he produced a total of 100 pieces. His piece rate pay of \$200 is more than the minimum wage pay, and, thus, he should be paid \$200. His regular rate of pay is \$20 per hour because he earned \$200 for 10 hours worked. The overtime premium is \$20 which is half of the regular rate times overtime hours. Employee B's total pay should be \$220.

In the example above, Employee B is paid based on the number of pieces that were completed during his productive hours. However, according to the recent decisions regarding California minimum wage, he was not paid for his nonproductive time, and, thus, did not receive at least California minimum wage for all hours worked.

### **Hybrid Pay System Combining Hourly Pay and Performance Pay**

Now suppose that Company XYZ adopts a new pay system that has two pay components — hourly pay and performance pay.

First, all hours are paid at California minimum wage (or a higher rate). Second, performance pay is only given to employees who complete more pieces than the threshold, which is the number of pieces that make piece rate pay equal to minimum wage pay.

For employees who exceed the threshold, performance pay is calculated by paying each piece beyond the threshold at a piece rate (in this case \$2 per extra piece). Let's review the same example employees from above under this new system.

Under this new system, Employee A's hourly pay is \$80, which is the California minimum wage times hours worked. If he had produced 40 pieces, then his piece rate pay would be the same as his hourly pay of \$80. Therefore, in this case, 40 is the threshold number of pieces. Because he only completed 20 pieces, he would not receive any performance pay. For his two hours of overtime, the premium would be \$8 which is half of the regular rate times overtime hours. His total compensation is \$88.

Employee B's hourly pay is \$80 because he worked for 10 hours. By the same logic used in Employee A's case, the threshold number of completed pieces is 40. Since he produced 100 pieces, which is 60 more than the threshold, he would be entitled to the performance bonus. His performance pay is \$120, which is the piece rate times the number of extra pieces. Combining the hourly pay of \$80 and the performance pay of \$120, his total earnings are \$200 for 10 hours of work excluding the overtime premium pay, and, thus, the regular rate is \$20 per hour. Since he worked two hours of overtime, he should be paid \$20 of overtime premium, which is half of the regular rate times overtime hours. Employee B's gross pay should be \$220.

Under this new system, the final pay amounts are identical to those under the piece rate system and, therefore, this hybrid system has exactly the same incentive structure as the piece rate pay system. However, this new system does not violate California minimum wage law because all hours worked are paid at least California minimum wage.

## Conclusion

If employers like the incentive structure of their current piece rate system, then there is a way to keep that structure without triggering a California minimum wage violation by adopting a hybrid system that combines hourly pay and performance pay.

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