

California Supreme Court Holds Break Premiums Must Account For Nondiscretionary Payments In Addition to the Hourly Rate of Pay

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Key Points:

- In *Ferra v. Loews Hollywood Hotel, LLC*, the California Supreme Court held that premiums paid for missed meal, rest or recovery periods must include nondiscretionary pay, not just hourly wages. The decision applies retroactively and significantly alters how employers must calculate meal and rest break premiums.
- Specifically, the Court found that the “regular rate of compensation” in Labor Code section 226.7(c) means the same thing as “regular rate of pay” in Labor Code section 510(a). Thus, the calculation of premium pay for a noncompliant meal, rest or recovery period, like overtime pay, must account for nondiscretionary payments in addition to the hourly rate of pay.

On July 15, 2021, the California Supreme Court issued a decision in *Ferra v. Loews Hollywood Hotel, LLC* that significantly changes how employers are required to calculate meal and rest break premiums. Overturning the California Court of Appeal, the California Supreme Court held that premiums paid for missed meal and rest breaks must include all nondiscretionary pay, not just hourly wages.

California Labor Code section 510(a) requires employers to pay employees premium pay for overtime hours, calculated as a multiple of the employee’s “regular rate of pay,” which must include not only hourly wages but also other nondiscretionary payments. California Labor Code section 226.7(c) requires employers to pay employees “one additional hour of pay at the employee’s regular rate of *compensation*” if an hourly employee is not provided with a compliant meal, rest, or recovery period. The question before the Court was “whether the Legislature intended ‘regular rate of compensation’ under section 226.7(c) to have the same meaning as ‘regular rate of pay’ under section 510(a),” such that a premium payment for a noncompliant breaks must account for nondiscretionary payments as well. Slip op. at 1.

In *Ferra*, Loews had paid employees an additional hour of pay at the employee’s base hourly rate each time they missed or took a noncompliant break. Loews did not factor nondiscretionary payments, such as quarterly incentive payments, into the calculation of the break premium payments. The trial court and Court of Appeal agreed with

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Loews' method of calculating premium payments, finding that the "regular rate of compensation" in section 226.7(c) is "not interchangeable" with the term "regular rate of pay" under section 510(a). Slip op. at 3.

However, the California Supreme Court reversed, finding that "the terms are synonymous: 'regular rate of compensation' under section 226.7(c), like 'regular rate of pay' under section 510(a), encompasses all nondiscretionary payments, not just hourly wages." Slip op. at 1. After an extensive analysis of the legislative history of both statutes, the Industrial Welfare Commission wage orders and how the words "compensation" and "pay" appear in legislative and judicial usage, the Court found "no evidence that 'regular rate of compensation' means hourly wages only." Slip. op. at 6. Thus, the Court concluded that the term "regular rate of compensation" in section 226.7(c), like "regular rate of pay" in section 510(a), must encompass "not only hourly wages but all nondiscretionary payments for work performed by the employee." Slip. op. at 25.

The Court went on to hold that this decision would apply retroactively, rejecting Loews' argument that retroactive application would expose employers to "millions" in liability. Opining that "it is not clear why we should favor the interest of employers in avoiding 'millions' in liability over the interest of employees in obtaining the 'millions' owed to them under the law," the Court found "no considerations of fairness or public policy" would warrant the decision applying only prospectively. Slip. op. at 25, 27.

Employers are well advised to closely examine the calculation of their break premium payments to ensure payments are consistent with this ruling. Additionally, employers must determine which bonuses are discretionary versus nondiscretionary to correctly include nondiscretionary payments in the calculation of break premiums.

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