

## Personal Liability for Wages

By Dolores Cordell, Esq. (Of Counsel)

July 2003

With the worsening economy, employers may be tempted to make deals with their employees, particularly key employees, to defer wages until cash flow is better. Or worse yet, the company might run out of money to pay wages which have already been earned, because of a cash crunch. Still worse, the company or a division could have to shut its doors leaving unpaid wages in its wake.

A recent California Court of Appeals case has highlighted a new pitfall for employers: personal liability for unpaid wages.

On April 2, 2003, the Court of Appeals issued an opinion in a case known as *Reynolds v. Bement* and held that corporate managers and officers are not individually liable for wages under California law. This is good news for management in the event an employee seeks to recover unpaid wages through the California Department of Labor or the California courts. However, the case also points out a hidden pitfall for employers under federal law.

The *Reynolds* case relies on a distinction between the definition of “employer” stated in the California Wage Orders and the definition applicable under federal law. In so doing, the Court did an extensive analysis of numerous federal cases which held the employer personally liable for unpaid wages. Thus, if an employee seeks payment of wages under a federal statute and/or through the federal Department of Labor, members of management could be at risk of personal liability.

In view of the risk of personal liability for wages, Clark & Trevithick recommends the following:

1. **Don't Create a Wage Liability:** While deferring wages is a tempting way to keep an employee, particularly a key employee, it is obviously a dangerous one for the individual manager(s). A better choice would be to pay the employee a minimum amount of wages or salary, and enter into an agreement that the employee will be paid a "bonus" if and when the company finds investors or the company turns a profit of a certain amount. Be careful, however, to comply with other wage and hour regulations: An hourly employee will have to be paid at least minimum wage (\$6.75 per hour as of the date this article was written) and an exempt employee must be paid twice the minimum wage (\$2,340.00 per month or \$28,080.00 per year).
2. **Notify the Employee of the New Wage Rate in Advance:** If you are reducing the employee's wages, it is important to give written notice to the employee of the new wage rate before the new rate goes into effect. Preferably, have the affected employee(s) sign an acknowledgement that he/she is aware of the new wage rate. Without the notice and proof that the employee was aware of the reduced wage rate before he/she continues to work, you run the risk that the employee will claim that he/she never agreed to the lower rate and believed that the higher rate was still in effect. This could result in a federal Labor Department or the federal courts imposing the higher wage rate, together with potential Waiting Time Penalties.
3. **Pay Employees or Implement a Reduction in Force:** If the company looks like it is headed for hard times and/or is at risk of not making a payroll, implement a reduction in force (layoff) sooner rather than later. Failing to make a payroll may be as risky as failing to make a payroll tax payment.
4. **Plan:** If the company looks like it is headed for serious trouble that could result in going out of business, be sure you plan ahead to have enough cash to pay all accrued wages and accrued vacation pay to all of the terminating employees.

Don't wait until the company is at the crisis point to address these employee wage issues. Employers should also pay off wage claims, even if it means having to put the employees ahead of trade creditors. Be sure to contact legal counsel with questions and to discuss any unusual situation.