IMPORTANT NOTE: Employment law is complicated and it's important to get good legal advice. This memo should not be relied on as legal advice. Also, we cannot guarantee that it is current or accurate.

Memo on Deducting Worker Cooperative Capital Contributions from Members' Wages

Written by the Green Collar Communities Clinic[1]

Current as of July 2013

I. Executive Summary:

This memo addresses (1) whether a California cooperative corporation, in which the worker members are employees, may make wage deductions to cover its workers' capital contribution, or "buy-in" to the cooperative, and, if permissible, (2) what parameters govern such buy-ins. In addition, it briefly addresses three methods by which a California cooperative corporation may collect an employee's buy-in. Last, it details when wage deductions are permissible under Employee Stock Ownership Plans (ESOPs), how they occur, and the statutory source of their authorization.

Wage Deductions Brief Answer: A California cooperative corporation employer may deduct co-op buy-ins from an employee's wages only if (1) the employer has received the employee's express written authorization for the deduction prior to making it; (2) the deduction does not result in a wage level below the employee's base pay (though language in a 2008 DLSE Opinion Letter does not mention this condition—defined in 2006 California Court of Appeals case[2]—when addressing employment practices in which it would likely apply); (3) the deduction does not constitute a rebate of the wages paid to the employee; (4) after deduction, the remaining wage does not fall below the minimum wage; and (5) the deduction is for the benefit of the employee, not the employer[3]—though courts have variably cited this requirement, and certain deductions heretofore held permissible by the DLSE[4] can be reasonably argued as benefiting the employer.

ESOP Brief Answer: The Pension Protection Act of 2006 (29 USC § 1001) amended provisions of ERISA and the IRC to grant employers the authority to enroll employees automatically in ESOPs, with such enrollment entailing an automatic wage deduction, unless the employee opts out. Cal Lab Code § 224 authorizes the deduction by its allowance for deductions authorized by "state or federal law."

II. Legal Authorities:

The California statute governing authorized wage deductions is Cal. Lab. Code § 224, which provides, with pertinent part underlined:

> The provisions of Sections 221, 222 and 223 shall in no way make it unlawful for an employer to withhold or divert any portion of an employee's wages when the

[1] Kudos to law student intern Jay Reidy, GC3 Summer Law Clerk 2013, for this research!

[2] *Koehl v. Verio, Inc.*, 142 Cal. App. 4th 1313 (Cal. Ct. App. 2006) (defining "standard wage" as an employee's "base pay").

[3] California Attorney General Opinion Letter 3 Op. Att. Gen. 178, 1994.

[4] DLSE Op. Letter 2008.11.25-1; See also DLSE Op. Letter 1999.09.22-1.

> employer is required or empowered so to do by state or federal law or when a deduction is expressly authorized in writing by the employee to cover insurance premiums, hospital or medical dues, or other deductions not amounting to a rebate or deduction from the standard wage arrived at by collective bargaining or pursuant to wage agreement or statute, or when a deduction to cover health and welfare or pension plan contributions is expressly authorized by a collective bargaining or wage agreement.[5]

Distinct from insurance premiums, or hospital or medical dues, a cooperative buy-in falls under those "other deductions not amounting to a rebate or deduction from the standard wage arrived at by collective bargaining or pursuant to wage agreement or statute."[6]

The California Supreme Court has provided dicta regarding interpretation of Section 224 and related sections: "Because the laws authorizing the regulation of wages…are remedial in nature, courts construe these provisions liberally, with an eye to promoting the worker protections they were intended to provide."[7] California courts have heeded public policy in scrutinizing various forms of deductions: "[t]he Legislature has recognized the employee's dependence on wages for the necessities of life and has, consequently, disapproved of unanticipated or unpredictable deductions because they impose a special hardship on employees."[8] In keeping with such policy, wages are exempt from attachment in California.[9]

According to the California Division of Labor Standards Enforcement (DLSE), among the Legislature's primary concerns in passing § 224 was the improper use of "kickbacks" by employers to recoup wages paid.[10] In its *Enforcement Policies and Interpretations Manual*, the DLSE enumerates several settings in which it views deductions under § 224 as permissible.[11] First, observing the statute, employers may deduct from wages "where the deduction is required or the employer is empowered to do so by federal or state law."[12] This category includes withholdings for state and federal taxes, and for defined contribution plans such as

---

5 (West 2012).

6 *Id*.; In 2007's *Prachasaisoradej v. Ralphs Grocery Co., Inc*., the California Supreme Court supplied definitions of "wages" and "deductions," as they are used in Cal. Lab. Code § 200, the parent section to § 224: "[A]n employee's "wages" or "earnings" are the amount the employer has offered or promised to pay, or has paid pursuant to such an offer or promise, as compensation for that employee's labor. The employer takes a "deduction" or "contribution" from an employee's "wages" or "earnings" when it subtracts, withholds, sets off, or requires the employee to return, a portion of the compensation offered, promised, or paid as offered or promised, so that the employee, having performed the labor, actually receives or retains less than the paid, offered, or promised compensation, and effectively makes a forced "contribution" of the difference." 42 Cal. 4th 217, 228 (2007).

7 *Prachasaisoradej v. Ralphs Grocery Co., Inc*., 42 Cal. 4th 217, 227 (2007).

8 *Hudgins v. Neiman Marcus Group, Inc.*, 34 Cal. App. 4th 1109, 1118-1119 (1995).

9 Cal. Code Civ. Proc. 487.020(c).

10 DLSE Op. Letter 2008.11.25-1.

11 *2002 Update Of The DLSE Enforcement Policies and Interpretations Manual* (2006) *available at* http://www.dir.ca.gov/dlse/dlsemanual/dlse_enfcmanual.pdf.

12 *Id*. at 11-1.

401(k)s and ESOPs.[13] Second, employers may deduct "for insurance premiums, hospital or medical dues or other deductions not amounting to a rebate or deduction from the standard wage" paid the employee under a wage agreement, collective bargaining agreement, or statute.[14] Observing § 224, the DLSE requires that this category of deductions receive prior written consent of the employee.[15]

A. The DLSE has stated that periodic deductions from wages (1) authorized in writing by an employee to (2) recoup predictable, expected overpayments that (3) occur as a consequence of the employer's payroll practice are permissible.

Notable for cooperative buy-in policies, in its 2008 Opinion Letter, *Re: Wage Deduction Authorization For Overpayments Due to Payroll Practice*, the DLSE held that "an employer may make deductions from wages to reflect predictable and expected wage overpayments made in the immediately prior paycheck that resulted from the employer's payroll system, if the employee provides voluntary, written authorization."[16] The DLSE emphasized that such deduction could not occur on the final paycheck,[17] citing *Barnhill v. Saunders*,[18] which prohibited deductions from an employee's final paycheck for debts owed to the employer, *but did not* expressly prohibit other forms of deduction for such debts.

B. The DLSE has also stated that deductions to recoup debt owed employer by employee are not prohibited by case law.

Also in Opinion Letter 2008.11.25-1 the DLSE stated, "*Barnhill* does not hold that employers are prohibited from making periodic set offs of wages (other than in final paychecks) to *repay a loan* owed to the employer where the employee has signed an express written consent to periodic set offs from wages." (Emphasis added) Here the DLSE does not expressly permit such loan repayment deduction; rather it holds the case law on point, *Barnhill*, not to prohibit them.[19] Moreover, in its *Enforcement Policies and Interpretations Manual* (2006), the

---

[13] *Id*.

[14] *Id*. at 11-1(a).

[15] *Id*.; Some exceptions apply to the written consent requirement: deductions to pay into health, welfare, and pension plans provided by a collective bargaining agreement; certain automatic contribution arrangements a defined contribution plan such as an ESOP, when the plan complies with federal requirements. *2002 Update Of The DLSE Enforcement Policies and Interpretations Manual* (2006). Additional permitted deductions under § 224 include those for employee tardiness.

[16] DLSE Op. Letter 2008.11.25-1; *See also* DLSE Op. Letter 1999.09.22-1.

[17] DLSE Op. Letter 2008.11.25-1.

[18] 125 Cal. App. 3d. 1 (Cal. Ct. App. 1981). Appellant employed respondent as a bookkeeper for nearly two years. Two months prior to termination, she executed a promissory note in favor of appellant in the amount of $587.50 at 10 percent interest. On its face, the note said, "To be paid by payroll deduction or on demand." On the date of termination, the balance due on the note was $475 plus interest, and respondent was owed two weeks wages, or $475. Respondent's final check was a stub with a net zero balance indicating various deductions including a $442.46 setoff against the balance owed on the note.

[19] Compare *California State Employee's Assn. v. State of California* 198 Cal. App. 3d. 37 (Cal. Ct. App. 1988) (holding impermissible deductions to recoup prior "erroneous salary advances," *not* debt owed employer or "predictable,

DLSE states that employers may make deductions for payments on loans made by the employer to the employee.[20] The *California Business Law Deskbook* interprets deductions for debt repayment as currently permissible: "[T]he DLSE has taken the enforcement position that employers may make a deduction to recover an overpayment, debt, vacation advance, or other amount owed to the employer if the employee has first voluntarily signed a written authorization to permit the deduction—whether as a one-time deduction or a series of installments—provided that the amount deducted does not exceed the amount authorized and the deduction does not have the effect of reducing the employee's pay below the minimum wage."[21]

III. Application: Best Practices for Buy-in Wage Deductions under Section 224

A. Employee's Express Written Authorization Required

A California cooperative corporation must obtain express written authorization from an employee before deducting wages for buy-in.[22] The authorization must establish the employee's voluntary consent to the deduction, and provide details of the deduction: its amount, purpose, and duration.[23]

In *Int'l Woodworkers of America, Local 6-64, CIO v. McCloud River Lumber Co.*, a federal court held that under California law, the employer could not deduct 7.5 cents per hour from its employees' wages without express authorization from each employee.[24] The employer, a logging and lumber company, arrived at an agreement with its employees' union to provide a wage increase of 7.5 cents per hour, to be subsequently deducted from consenting employees' wages to pay into a worker health and welfare program.[25] The court held the plain language of

---

expected" overpayments resulting from the employer's routine payroll practice). An audit report of a state medical facility at reported 731 outstanding erroneous salary advances totaling $463,113. Employer, the medical facility, then notified affected employees of a corrective repayment plan to deduct up to $400 from the net salary warrant and 40 percent of net overtime pay. Employees were given seven days within which to negotiate a modification of the repayment schedule due to undue hardship. The court held that specific provisions of state attachment and wage garnishment laws took precedence over general provisions of the California Government Code cited by the employer for recouping overpayments to state employees.

[20] However, the DLSE further states that the permissibility of such deductions is open to question given Cal. Lab. Code § 300(h), which sets conditions on wage assignment. (West 2012). Given that no third party exists in an employer-creditor, employee-debtor relationship, it is doubtful that § 300 applies to such wage deduction; no assignment is occurring. *See* Thomas E. Geidt & Judith M. Kline, California Business Law Deskbook § 16:18(7) (2012-13 ed.) available at http://www.paulhastings.com/Resources/Upload/Publications/2347.pdf. Likely for this reason, the *Barnhill* court did not address assignment in its opinion, nor the applicability of § 300 to its holding barring only deductions of employee debt from final paychecks. *Barnhill*, 125 Cal. App. 3d. at 9.

[21] Geidt & Kline, *supra* note 20..

[22] *Int'l Woodworkers of America, Local 6-64, CIO v. McCloud River Lumber Co.*, 119 F. Supp. 475 (N.D. Cal. 1953); *Koehl v. Verio, Inc.*, 142 Cal. App. 4th 1313 (Cal. Ct. App. 2006).

[23] *See infra* Due Process and Wage Deductions.

[24] 119 F. Supp. 475 (N.D. Cal. 1953).

[25] *Id*. at 480. The union, on behalf of its workers in McCloud, California, sought declaratory judgment requiring the employer lumber company to pay the required costs of the program, deducted from wages, irrespective of

§ 224 to require "that individual authorizations in writing be given" by the employee before such deductions, adding, the "public policy of [California], as emphatically declared as it is in Sections 222 and 224…cannot be ignored by a Federal Court."[26] Importantly, under the holding, the benefits deduction affected only consenting employees; those not consenting could retain the wage increase meant to fund the deduction.[27]

Similar to *Int'l Woodworkers*, the DLSE held as permissible an employer's practice of deducting routine, periodic overpayments only if accompanied by "previous written agreement" establishing the employee's voluntary consent to the deduction.[28] The employer in question paid its employees at the end of each bi-weekly pay period based on the number of hours they were scheduled to work, and then made deductions in the next pay period to adjust for any resulting overpayments revealed by a review of the employees' electronic time sheets showing any hours that the employees did not actually work in the prior pay period.[29] The DLSE viewed such deductions as permissible "only if there is a previous written agreement based upon voluntary consent of employee, provided that the amount of the deduction does not exceed the authorized amount and, after making the deduction, the employee still receives no less than the minimum wage for all hours worked in the pay period."[30] The DLSE held that the electronic time sheets used by the employer failed as express written authorization.[31]

In *Koehl v. Verio, Inc.*, the court held permissible an internet service provider's chargeback of previously advanced sales commissions.[32] (The employer charged back the commissions on sales that fell through within a given timeframe.) The court reasoned that the practice was permissible because it met two criteria: "the deduction is (1) authorized in writing, and (2) does not reduce the employee's standard wage."[33] The court emphasized that the employer's chargebacks "were made pursuant to written commission plans which expressly authorized them."[34] The absence of such authorization would render the deductions impermissible.[35]

Similar to *Koehl*, in *Steinhebel v. Los Angeles Times Communications*, the court held permissible the Los Angeles Times' chargeback of commission advances to telesales employees whose sales

---

whether individual employees had executed individual written authorizations permitting the deduction. The employer, a Minnesota corporation, filed a counter claim for a declaratory judgment in support of its refusal to make said deductions and turn the money over to the insurance company, except for employees who had executed authorizations. Sitting in diversity, the federal court granted declaratory judgment to the employer.

[26] *Id*. at 486.

[27] *Id*. at 488.

[28] DLSE Op. Letter 2008.11.25-1.

[29] *Id.*

[30] *Id*.

[31] *Id.*

[32] 142 Cal. App. 4th 1313 (Cal. Ct. App. 2006).

[33] *Id*. at 1337. The court defined "standard wage" as an employee's "base pay." *See supra* note 1.

[34] *Id*.

[35] *Id*.

fell through.[36] Individual employees had read and expressly authorized the practice, agreeing to "hereby authorize such deductions."[37] Therefore, the court held, the policy did not violate § 224.[38]

A court would all but certainly rule impermissible any cooperative buy-in wage deduction not preceded by the employee's express written authorization. Distinct from the employers in *Steinhebel* and *Koehl*, whose deductions under § 224 were chargebacks of advances to certain employees, the employer in *Int'l Woodworkers* deducted a raise offered to all employees, yet could only permissibly deduct from those executing written authorization. Notwithstanding the deduction type, each court held the deduction to require express written authorization. Further, the DLSE has repeatedly emphasized the necessity of such authorization as required by the plain language of § 224.[39] Automatic deduction based on electronic time sheets, but not authorized in writing, fails to satisfy § 224.[40] Thus, for a cooperative buy-in deduction, an employee's express written authorization is required.

i. Due Process and Wage Deductions

Wages for work already performed are "property" under the Due Process Clause, affording an employee the right to notice and opportunity to be heard before deduction.[41]

In *Sniadach*, the Supreme Court held unconstitutional a Wisconsin statute authorizing the seizure of wages in garnishment actions before trial of the main suit.[42] The seizure occurred without opportunity for the wage earner to be heard.[43] Importantly, the Court held wages to constitute "property" under the Due Process Clause: "Where the taking of one's property is so obvious, it needs no extended argument to conclude that absent notice and a prior hearing, this prejudgment garnishment procedure violates the fundamental principles of due process."[44]

California case law has not addressed the precise requirements of § 224 wage deduction authorization forms. In keeping with *Sniadach*, such deductions must satisfy Due Process. In *Steinhebel*, the court held the employment agreement as providing sufficient express written authorization.[45] In keeping with *Sniadach*, any deduction form must provide "notice" of the

---

[36] 126 Cal. App. 4th 696 (Cal. Ct. App. 2005)..
[37] *Id.* at 710.
[38] *Id.*
[39] *See e.g*. DLSE Op. Letter 2008.11.25-1.
[40] *Id.*
[41] *Sniadach v. Family Finance Corp. of Bay View*, 395 U.S. 337 (1969); *See* Steven G. Pearl, *The Limits on Employer Deductions from Pay in California*, 33 L.A. Law. 10 (2010).
[42] *Id*. at 342.
[43] *Id*.
[44] *Id*.
[45] *Steinhebel*, 126 Cal. App. 4th at 710. Refer to Appendix, *infra*, for employment agreement authorizing deductions.

deduction.[46] Courts have generally required authorizations to provide the employee with clear understanding of the deduction.[47] Therefore, a cooperative buy-in deduction authorization form should convey material facts related to the deduction, including the amount, purpose, and duration of the deduction, as well as the employee's voluntary consent.

B. The deduction may not go below the employee's standard or "base" wage.

The buy-in deduction may not bring the employee's wage level below her "standard wage," defined as her "base pay."[48]

In *Koehl*, the court defined "standard wage" in § 224: "Although 'standard wage' is not defined in Section 224, and we can find no authority defining it, common usage of the term refers to an employee's base pay, as shown by the testimony of the [employees], who referred to their base pay as their 'standard' wage."[49] In *Koehl*, the employer's chargeback of specified commissions recouped only what had been paid above the "standard wage," not decreasing the wage level below it, thereby satisfying § 224.[50]

Distinct from the *Koehl* employer, the employer in DLSE Opinion Letter 2008.11.25-1 paid its employees at the end of each bi-weekly pay period based on the number of hours they were scheduled to work, and then made deductions in the next pay period to adjust for any resulting overpayments revealed by a review of the employees' time sheets showing any hours that the employees did not actually work in the prior pay period. The DLSE held this deduction permissible under § 224.[51]

Important for cooperative buy-in policies, the DLSE stated to the employer, "The deductions you described in the factual scenario at issue do not amount to an improper or unfair deduction to the employee's wages, *so long as* affected employees provide written authorizations *and the employee still receives, after such deductions, not less than the minimum wage*" (emphasis added).[52] Here the employer made an upfront balloon payment for all work hours scheduled. The employer then deducted to reflect the number of hours actually worked, as reported by

[46] *See Sniadach*, 395 U.S. at 342.

[47] *See Steinhebel* 126 Cal. App. 4th 696 at 710; *Int'l Woodworkers* 119 F. Supp. at 480.

[48] *Koehl*, 142 Cal. App. 4th at 1337 (interpreting § 224). Neither case law, nor the DLSE, has precisely defined "base pay," as proffered by the *Koehl* court. It is unclear whether "base pay" is an employee's original hourly wage level, or, the present wage level as established by prior raises or cuts. It is also unclear whether "base pay" includes only base hourly pay, or additional compensation forms, such as salary. Given the California Supreme Court's insistence in *Prachasaisoradej* that courts "construe provisions [of § 224] liberally, with an eye to promoting the worker protections they were intended to provide," "base pay" will likely be interpreted broadly. *Prachasaisoradej*, 42 Cal. 4th at 227.

[49] *Id*.

[50] *Id*.

[51] DLSE Opinion Letter 2008.11.25-1 at 4.

[52] *Id*.

timesheet. The deduction did not reduce the actual hourly wage. Rather it removed hours paid but not worked, from the employee's total pay.

In this light, the DLSE's warning that the post-deduction wage level not be "less than the minimum wage" seems odd. The employer did not deduct from the actual wage level. It deducted *hours* not worked. Hypothetically, an employee here could schedule numerous hours and receive the upfront payment for them, but only work one. The deduction would then eliminate pay for all the hours scheduled but not worked, with the wage level for the hour actually worked not falling. No question of a post-deduction, sub-minimum wage level (the DLSE's caution) arises.

Thus, if base pay (the *Koehl* court's definition of § 224's "standard wage") were above the minimum wage, the DLSE's caution leaves open the possibility of deduction beneath base pay, just *not* beneath minimum wage. Deduction beneath base pay would violate the definition of "standard wage" proffered by the *Koehl* court.[53] No cases or further opinion letters elucidate this issue, though it may be well settled that the *Koehl* court's definition is binding on the DLSE, thus disallowing a deduction practice based on differing interpretation of § 224's "standard wage."

In this light, it becomes unclear whether deduction to recoup an employee debt requires a preceding wage increase, thus preventing the resulting wage level from falling beneath the employee's base pay. A preceding wage increase could also be argued as setting a new "standard wage," thus *still* disallowing deduction beneath it.[54] The federal court in *Int'l Woodworkers* reviewed such a scenario 53 years prior to *Koehl*, where employees were to receive a wage increase of 7.5 cents per hour, to be subsequently deducted from consenting employees' wages to pay into a worker health and welfare program.[55] However, the *Woodworkers* court decided only the questions before it, including the necessity of written authorization for such deductions.[56] It did not review, and provided no dicta regarding, the deduction in question and "standard wage" under § 224.[57] Even if it had, its disposition and/or dicta may not have persuaded California courts.[58]

If the *Koehl* court's definition of "standard wage" is binding on the DLSE—which it likely is, absent competing or higher authority—such a deduction could not go below an employee's "base pay." In both *Koehl* and Opinion Letter 2008.11.25-1, the deduction did not fall below the

---

[53] However, it would not contravene the DLSE's requirement, "*the employee still receives, after such deductions, not less than the minimum wage*." See *Koehl*, 142 Cal. App. 4th at 1337; DLSE Opinion Letter 2008.11.25-1.

[54] *See* note 47, *supra*.

[55] *Int'l Woodworkers of America,* 119 F. Supp. at 482.

[56] *Id*. at 484-88.

[57] *Id*.

[58] The *Woodworkers* court reviewed a question of California law as a federal court sitting in diversity. It is unclear to what degree such decisions by a federal court serve as binding or persuasive authority for state courts.

base pay. The Opinion Letter employer recouped hours paid but not worked; the employer in *Koehl* deducted only commissions made above the standard wage.

A court will likely require a cooperative buy-in deduction to fall within the *Koehl* court's definition of "standard wage;" a coop buy-in deduction very likely may not bring employees' wage levels beneath their base pay.

C. The deduction may not constitute a rebate of paid wages.

No court has defined "rebate" in § 224 or in the parent section, § 200. In keeping with the *Koehl* court, which defined "standard wage" according to its "common usage," rebate is likely to receive similar, plain-meaning interpretative treatment. Black's Law Dictionary provides the definition of "rebate" as, "A return of part of a payment, serving as a discount or reduction." (9th ed. 2009).

D. The deduction may not result in a wage level below the minimum wage.

A cooperative buy-in deduction may not bring the resulting wage level below the minimum wage.[59]

In *Div. of Labor Standards Enforcement v. Williams*, the court held that a restaurant-employer could deduct from its employees' minimum wage to cover their meals, provided the value of the meals filled the difference between the actual wage and the minimum wage.[60] Employees authorized such deductions by "voluntary written agreement."[61]

Pursuant to California case law, IWC wage order, and the DLSE's statements on § 224, deduction under the Section may not bring the employee's wage beneath the minimum wage.[62]

E. The deduction must be for the benefit of the employee, not the employer.

In a 1944 Opinion Letter, the California Attorney General stated, "Deductions permitted by law and which may be voluntarily requested in writing by the employee are insurance premiums, hospital or medical dues, and other items which are for the benefit of the employee, not the employer."[63] The Letter addressed a restaurant employer's practice of automatically deducting $00.25 per day from waitresses' wages (minimum wage plus tips) and prorating the sum to

[59] *See e.g.* DLSE Opinion Letter 2008.11.25-1; See *Div. of Labor Standards Enforcement v. Williams*, 121 Cal. App. 3d 302, (Cal. Ct. App. 2006 1981); IWC Minimum Wage Order (2007).

[60] 121 Cal. App. 3d 302, 310 (Cal. Ct. App. 2006 1981) (holding such practice to satisfy § 224).

[61] *Id.*

[62] See *Williams* 121 Cal. App. 3d at 310; DLSE Opinion Letter 2008.11.25-1; IWC Minimum Wage Order (2007).

[63] 3 Op. Att'y Gen. 178.

busboys.[64] The Attorney General viewed the deduction as impermissible under both a Wage Order and § 224.[65]

In *Koehl* the court did not address whether such deductions satisfied the "for the benefit of the employee" requirements. Rather, in a footnote, the court cited *Prudential Ins. Co. of America v. Fromberg*, 240 Cal. App. 2d 185 (Cal. Ct. App. 1966) as establishing that § 224 is not limited to deductions for "employee benefits."[66] Similarly, in *Steinhebel*, the court did not address whether the deductions complied.[67] Conversely, in DLSE Opinion Letter 2008.11.25-1, permitting the employer's deduction of predicable, expected overpayments, the DLSE opined that such deductions benefited the employee because—as deductions of overpayments rather than earned wages—the practice satisfied an obligation (debt) owed the employer. The *California Business Law Deskbook* responds, however, that such recoupment of overpayments could arguably be construed as benefiting the employer.[68]

In its *Enforcement Policies and Interpretations Manual*, the DLSE states emphatically, "Deductions are only permitted for items which are for the direct benefit of the employee—not deductions which *in any way* benefit the employer *either directly or indirectly*," citing this AG Opinion Letter.[69] (Emphasis added.)

The DLSE has consistently observed this standard in its opinion letters. Courts have to a lesser degree in their opinions. If the standard is applied to a buy-in deduction, a strong case can be made that it benefits the employee by affording her the benefits of cooperative membership/ownership.

IV. Conclusion

An employer may deduct a cooperative wage buy-in under § 224 only if (1) the employer has received the employee's express written authorization for the deduction prior to making it; (2) the deduction does not result in a wage level below the employee's "standard wage" or base pay (though language in recent DLSE Opinion Letter 2008.11.25-1[70] does not mention this condition when addressing employment practices in which it would likely apply); (3) the deduction does not constitute a rebate of the wages paid to the employee; (4) after deduction, the remaining wage does not fall below the minimum wage; and (5) the deduction is for the

---

[64] *Id*.

[65] *Id*.

[66] *Koehl*, 142 Cal. App. 4th at 1341, note 8.

[67] *Steinhebel v. Los Angeles Times Communications*, 126 Cal. App. 4th 696 (Cal. Ct. App. 2005).

[68] Geidt & Kline, § 16:18(2). *See supra* note 20.

[69] *2002 Update Of The DLSE Enforcement Policies and Interpretations Manual* (2006) at 11-3, *available at* http://www.dir.ca.gov/dlse/dlsemanual/dlse_enfcmanual.pdf.

[70] DLSE Opinion Letter 2008.11.25-1 at 4 ("The deductions you described in the factual scenario at issue do not amount to an improper or unfair deduction to the employee's wages, so long as affected employees provide written authorizations and the employee still receives, after such deductions, not less than the minimum wage.").

benefit of the employee, not the employer—though courts have variably cited this requirement, and certain deductions heretofore held permissible by the DLSE can be reasonably argued as benefiting the employer.

Under Due Process, any deduction authorization form should convey the amount, purpose, and duration of the deduction, as well as the employee's voluntary consent. The DLSE (and likely a court) will evaluate a co-op buy-in deduction under the standard that it must benefit the employee, and not the employee.

Under DLSE Opinion Letter 2008-11-25-1, the DLSE has taken the enforcement position that periodic deductions from wages (1) authorized in writing by an employee to (2) recoup predictable, expected overpayments that (3) occur as a consequence of the employer's payroll practice are permissible. In addition, the DLSE has stated that case law does not prohibit wage deductions to recoup debt owed an employer by an employee. Neither deductions for overpayments, nor deductions to recoup debt held by the employee, may be deducted from an employee's *final* paycheck.

The *Koehl* court has defined "standard wage" under § 224 as an employee's "base pay." No other courts have defined this phrase of the statute. Therefore, absent competing or higher authority, if an employer wishes to deduct employee debt or overpayments from wages, the deduction may not bring the resulting wage beneath the employee's base pay.

APPENDIX: Cooperative Buy-in Deduction Best Practices

A. Employer Loan to Employee, Paid Back through Wage Deduction, or Outside of Wages

Under this option, the co-op would issue debt to the employee in the amount of the co-op buy-in, repaid through wage deduction (see B. Wage Deduction, below). Pursuant to the "base pay" definition of "standard wage" under § 224, repayment through deduction could not result in a wage level below base pay.

Repayment outside of wage-deductions would not occur within the confines of § 224, because wage deduction would not repay the buy-in loan. Rather, the employee would enter a debtor-creditor relationship with the cooperative, and make non-wage-deducting repayments.

B. Wage Deduction

Any wage deduction to cover a co-op buy-in may not bring the employee's wage level below "base pay." Therefore, to deduct the buy-in, the co-op would have to establish the wage level *resulting* from the deduction as the base pay of those employees buying in. Therefore the cooperative could give employees a wage increase prior to buy-in deduction, and then deduct only the amount of the increase, similar to the logging company in *Int'l Woodworkers*. However, some ambiguity surrounds the exact definition of "base pay."[71] If courts define "base pay" *not* as the employee's original wage level, but as the present wage level as established by prior raises, a wage increase would merely establish a new "base pay"—below which a buy-in deduction could not go.

C. Example of Employee Consent Authorizing Deductions

"Even though an order is not commissionable until the customer keeps it 28 days, The Times will pay you two weeks in advance for the order. Beginning on the second pay period after your start date, you will receive an advance against your commissions. The amount will be equal to the commissions attributable to the preceding pay period. However, if the subscription is rejected by The Times or by the customer before 28 days, the amount advanced in respect to the rejected subscription will be deducted from your compensation payable subsequent to the date of such rejection based on your commission rate for [the] current week and you hereby authorize such deductions." *Steinhebel v. Los Angeles Times Communications* 126 Cal. App. 4th 696, 701-2 (Cal. Ct. App. 2005).

D. Wage Deduction and Employee Stock Ownership Plans (ESOPs)

An ESOP is a qualified defined contribution retirement plan, similar to profit-sharing or 401(k) plans. Unlike 401(k) plans, which invest in a wide variety of securities, ESOPs invest primarily in employer securities.

The Pension Protection Act (PPA) of 2006 (29 USC § 1001) amended provisions of the Internal Revenue Code (26 USC § 401) to give employers the authority to enroll employees in a defined

---

[71] *See* note 47, *supra*.

contribution plan automatically, with such enrollment carrying an automatic wage deduction to fund the plan—unless the employee chooses to not participate. Employees not participating may instead receive standard payment of the portion of their wages that would have otherwise been deducted. Under 29 USC § 1144, the PPA may "supersede any law of a State which would directly or indirectly prohibit or restrict the inclusion in any plan of an automatic contribution arrangement."