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Expert Analysis

Wage Deductions: Labor Law §193, 'Pachter v. Bernard Hodes'

Private employers contemplating deducting part of an employee's wages must comply with New York Labor Law §193, which prohibits all deductions other than those specifically identified therein.[1]

Making prohibited deductions subjects an employer to compensatory damages equal to the prohibited deduction, 25 percent liquidated damages if the violation was willful, and attorney's fees. Labor Law §198. Additionally, §198-a provides for criminal penalties for violation of article 6, which includes §193. Violation of §193 is a popular subject for class-action litigation, so employers are well-advised to respect its mandates and employees should be vigilant in reviewing their paystubs.

Section 193

In this section:

1. No employer shall make any deduction from the wages of an employee, except deductions which:

a. Are made in accordance with the provisions of any law or any rule or regulation issued by any governmental agency; or

b. Are expressly authorized in writing by the employee and are for the benefit of the employee; provided that such authorization is kept on file on the employer's premises. Such authorized deductions shall be limited to payments for insurance premiums, pension or health and welfare benefits, contributions to charitable organizations, payments for United States bonds, payments for dues or assessments to a labor organization, and similar payments for the benefit of the employee.

§193 Applies to Wages

By **Jeffrey D. Pollack**

Any discussion of §193 must start with a discussion of what constitutes wages. Labor Law §190(1) defines "wages" as:

> The earnings of an employee for labor or services rendered, regardless of whether the amount of earnings is determined on a time, piece, commission or other basis. The term "wages" also includes benefits or wage supplements as defined in section one hundred ninety-eight-c of this article, except for the purposes of sections one hundred ninety-one and one hundred ninety-two of this article.[2]

The Court of Appeals recently examined §193's application to commission payments in *Pachter v. Bernard Hodes Group Inc.*, 10 N.Y.3d 609 (2008). During more than a decade of employment the employer had calculated the plaintiff's commission after deducting certain expenses, including finance charges for late payments by clients, travel and entertainment expenses, and half the salary for the plaintiff's assistant.

After plaintiff's employment ended, she challenged this practice. The court held that although such deductions were outside those enumerated in §193, they were permissible because they were made before plaintiff "earned" the commission, which is when the commissions become "wages." Cf. *Gennes v. Yellow Book of N.Y. Inc.*, 23 AD2d 520 (2nd Dept. 2005) (deduction from earned commission unlawful); *Jacobs v. Macys East Inc.*, 262 AD2d 607 (2nd Dept. 1999) (allegation of deduction from earned commission sufficient to defeat motion to dismiss).

The *Pachter* Court stated that "in the absence of a governing written instrument, when a commission is 'earned' and becomes a 'wage'…[it] is regulated by the parties' express or implied agreement; or, if no agreement exists, by the common-law rule that ties the earning of a commission to the employee's production of a ready, willing and able purchaser…." *Pachter*, 10 NY3d at 618.[3]

Pachter also put to rest a disagreement among the lower courts as to whether article 6 of the Labor Law, including §193, applies to executives. The Court held that executives (and presumably similar level employees) are covered by the definition of "employee" in §190 (2)—"any person employed for hire by an employer in any employment"—except where specifically excluded by the statute. Id. at 616.

Benefits, Wage Supplements

Benefits and wage supplements fall within the definition of wages covered by §193 unless the employee at issue is an executive, professional or administrative employee earning more than nine hundred dollars per week. Labor Law §190(1). "Wage supplements" include health and retirement contributions, vacation and holiday pay, and reimbursement of expenses. See Labor Law §198-c.

Nevertheless, pay for unused vacation time may not qualify as wages in certain circumstances. In *Ireton-Hewitt v. Champion Home Builders Co.*, 501 F.Supp.2d 341 (N.D.N.Y. 2007), the vacation policy provided that all unused vacation would be forfeited upon termination. The court held that such forfeiture did not violate §193 because the employer "did not make unauthorized deductions from [the] vacation…pay. Rather, it never tendered payment of unused vacation pay…." Id. at 353. The court applied the same analysis to the severance policy which provided that employees fired for cause were ineligible for severance pay. Id.

• **§193 Does Not Apply to Discretionary Bonuses.** Section 193's restrictions do not apply to discretionary incentive bonuses. Id. at 353-54; *Winters v. American Exp. Travel*

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and Business Servs. Inc., 2007 WL 632765, *10 (S.D.N.Y. Feb. 27, 2007). In *Truelove v. Northeast Capital & Advisory Inc.*, 268 AD2d 648 (3rd Dept. 2000), the bonus "reflect[ed] a combination of the individual's performance and defendant's performance." Id. at 648. There were other conditions to payment of the bonus, including being employed on the date of payment. The court found that the bonus was not wages:

> The dispositive factor in determining whether compensation constitutes wages is…whether the compensation is vested and mandatory as opposed to discretionary and forfeitable.
> ***
> Compensation will be found to be part of an incentive compensation plan where an employee receives a guaranteed salary and also receives supplemental income based upon the dual performance of the employee and the business or as a result of other factors outside of the employee's control. Id. at 649 (citations omitted).

Compare *Hall v. United Parcel Serv. of America Inc.*, 76 NY2d 27 (1990) (incentive plan provided that employee had to be employed on particular date), with *Tuttle v. George McQuesten Co.*, 227 AD2d 754 (3rd Dept. 1996) (agreement provided that fixed bonus was "due" at end of year, so bonus was wages).

Permitted Deductions

Section 193 permits only deductions made in accordance with law and those for the employee's benefit. Those made in accordance with law include taxes and social security payments, income executions, and wage assignments.[4] Deductions "for the employee's benefit" are limited to: insurance premiums, pension or health benefits, charitable contributions, payments for U.S. savings bonds, union dues or assessments, and "similar payments for the benefit of the employee." §193.1(b).

"Similar payments for the benefit of the employee" include deductions paid over to an investment fund on the employee's behalf— even if the fund contains a forfeiture provision in the event employment terminates before full vesting. *Marsh v. Prudential Securities Inc.*, 1 NY3d 146 (2003). They also include vehicle lease-to-buy payments and franchise fees, *Vysovsky v. Glassman*, 2007 WL 3130562, *15 (S.D.N.Y. Oct. 23, 2007), and deductions made pursuant to a collective bargaining agreement for the purchase of a bond required for route salesmen, *Bround v. New York State Guernsey Breeders' Co-Op Inc.*, 194 Misc. 701, 807 NYS2d 272 (N.Y. Mun. Ct. 1949). "A deduction made to enable an employee to furnish one of the prerequisites of his employment is made for the benefit of the employee." *Vysovsky*, 2007 WL 3130562 at *15.[5]

Other Deductions Prohibited

Deductions for things such as spoilage, breakage, cash shortages, or to punish an employee are prohibited. See, e.g., 12 NYCRR §142-2.10. "Section 193 was intended to place the risk of loss for such things as damaged or spoiled merchandise on the employer rather than the employee." *Hudacs v. Frito-Lay Inc.*, 90 NY2d 342, 349 (1997).

Employers may not deduct for the cost of uniforms or for security deposits on employer-provided equipment. In *Hudacs v. Celebrity Limousine Corp.*, 205 AD2d 155 (3rd Dept. 1994), defendant required its drivers to wear a uniform, which they obtained from an outside vendor whom the employer paid and then deducted the cost from the employee's wages. Drivers were also required to have an umbrella available, which the employer supplied but deducted a $15 returnable deposit. The court held that these deductions were illegal. See also *Trinidad v. Breakaway Courier Systems Inc.*, 2007 WL 103073 (S.D.N.Y. Jan. 12, 2007) (Rule 23 class certified based on allegations of deductions for bicycle repairs and use of two-way radios).

'Pachter' held that though certain deductions were outside those in §193, they were allowed because they were made before plaintiff "earned" the commission….

Probably the most common mistake employers make is deducting for prior overpayments. Prior overpayments may not be recouped by deduction. Instead, the employer must commence a civil action against the employee. *Hennessey v. Board of Educ. of City of N.Y.*, 227 AD2d 559, 560 (2d Dept. 1996). As discussed earlier, however, benefits and wage supplements for executives, professionals or administrative employees do not qualify as wages, so employers may deduct from benefits or supplements due such employees—but not from their wages—in order to recoup overpayments. See *Winters*, 2007 WL at *4; Labor Law §198-c (3).[6]

The statute also prohibits doing by separate transaction what an employer cannot do by deduction. In *Angello v. Labor Ready Inc.*, 7 NY3d 579 (2006), the court held that requiring employees who wanted to receive wages in cash rather than by check to use an ATM owned by the employer's subsidiary which charged a processing fee constituted an illegal deduction.

Preemption

Federal law may preempt §193 if the employee at issue is covered by a collective bargaining agreement. See *Vera v. Saks & Co.*, 335 F.3d 109, 115-16 (2d Cir. 2003) (section 193 preempted because claims required interpretation of the collective bargaining agreement's commission provision to determine when commission was "earned"); *Levy v. Verizon Info. Servs. Inc.*, 498 F. Supp.2d 586 (E.D.N.Y. 2007) (preempted because claims substantially depended on collective bargaining agreement's discipline provisions). Nevertheless, unionized employers should not read these cases as a license to make deductions beyond those set forth in §193. Instead, preemption should only be used as a defense, because if a court finds no preemption the employer will be liable for violating §193.

Conclusion

Employers and employees alike must be vigilant to insure compliance with §193.

1. The definition of "employer" in §190(3) specifically excludes government employers, so §193 does not apply to government employees. See also *Leirer v. Caputo*, 81 NY2d 455 (1993); *Salling v. Koch*, 115 Misc 2d 514, 515 (N.Y. County 1982).

2. Not all funds that pass through an employee's hands are wages. See, e.g., *Hudacs v. Frito-Lay Inc.*, 90 NY2d 342 (1997) (funds that route salesmen/drivers collected from customers and later paid over to the employer were not wages).

3. See also Labor Law §191(c) (in the absence of a written commission agreement signed by both parties setting forth how commissions are calculated and how recoverable draw is handled, if applicable, the commission structure will be presumed to be as the employee describes it).

4. See Labor Law §193(3); 12 NYCRR 137-2.5(a). The regulations governing wage assignments and income executions are found in CPLR §§5231, 5241, and 15 U.S.C. §1673.

5. The total of all voluntary deductions for "similar payments for the employee's benefit" may not exceed 10 percent of gross wages. 12 NYCRR §195.1.

6. See also *Graziano v. Society of the N.Y. Hosp.*, 1997 U.S. Dist. Lexis 15926 (S.D.N.Y. Oct. 15, 1997) (deductions from vacation, sick, or holiday time do not destroy FLSA's overtime exemption).