WINSTON & STRAWN LLP

CLIENT ALERT

Ninth Circuit Decides Rate of Vacation Payout To Terminating Employees in California

MAY 15, 2023

California law requires employers to pay employees their unused accrued vacation at the time of termination. Specifically, California Labor Code section 227.3 states that "all vested vacation" shall be paid "as wages at [the employee's] ***final rate*** in accordance with such contract of employment or employer policy respecting eligibility or time served."

What is the "final rate"? Can it be just the base hourly pay/salary—or must it take into account other wages paid, such as shift differentials, commissions, and incentive pay?

For years, many employers have relied on the longstanding Division of Labor Standards Enforcement ("DLSE") interpretation that the employer's ***policy*** sets the rate of vacation pay—and that the "final rate" can be base pay if that is what the employer's policy provides.

The Ninth Circuit's recent decision in *Mills v. Target Corp.* interpreted "final rate" differently.

Target had paid the plaintiff, Cinnamon Mills, vacation wages at termination using only her base hourly rate. Mills argued that her vacation wages should have been paid at a rate including the $2 per hour shift differential she received before her termination. The federal district court and Ninth Circuit agreed with Mills.

The Ninth Circuit concluded that the plain and commonsense meaning of the term "final rate" is the "final ***wage*** rate," which includes shift differentials. It rejected the argument that the "final rate" refers to the "final ***vacation*** rate."

The Ninth Circuit also considered whether Target owed Mills "waiting time penalties" under California Labor Code section 203, based on Target's failure to pay vacation at the final wage rate. The court did not impose waiting-time penalties because it found that the law before its decision was uncertain and that Target's actions were based on a good-faith belief of what the law required.

The court's decision is brief and leaves many questions unanswered, including which wages (other than shift differentials) must also be factored into the "final rate," how to calculate the "final rate," and whether employers in future cases may be exposed to waiting-time penalties now that the *Mills* decision exists.

Although the case is unpublished, we expect to see new cases filed that bring this type of vacation "final wage" claim. Ultimately, the issue may need to be decided by the California state courts.

We recommend California employers consult their labor and employment counsel regarding their vacation policies and practices to determine whether changes may be advisable in light of the *Mills* decision.
2 Min Read

Related Locations

Los Angeles

San Francisco

Related Topics

Federal Circuit

Wage & Hour

California Labor Code

Related Capabilities

Appellate & Critical Motions

Labor & Employment

Related Regions

North America

Related Professionals

Jason Campbell

Joan Fife

Emilie Woodhead

Zar Papazyan

© 2024 Winston & Strawn LLP.