

***Employer Adviser Hot Sheet --***  
**Breaking Developments in Labor and Employment Law**

*Lawyers for Employers* ®

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**Department of Labor and Industries Adopts  
New Payroll Deduction Regulations  
That Take Effect on January 1, 2006**

On January 1, 2006, the existing Washington state wage deduction regulation (WAC 296-126-025) will be replaced with three new regulations: (1) WAC 296-126-025, which will govern deductions from an employee's final wages; (2) WAC 296-126-028, which will govern deductions from a current employee's wages during ongoing employment; and (3) WAC 296-126-030, which will provide a new procedure that employers can use to make deductions from employee wages to correct for prior wage overpayments.

**The New Payroll Deduction Regulations Are Intended to Resolve a Conflict  
Between the Current Payroll Deduction Regulation and Washington's Wage  
Deduction Statutes and Related Court Decisions**

The new payroll deduction regulations are intended to resolve a conflict between the current payroll deduction regulation (WAC 296-126-025) and Washington's wage deduction statutes (RCW 49.48.010 and RCW 49.52.060), as interpreted by the Washington State Supreme Court in the case of *Pope v. University of Washington*, 121 Wn.2d 479, 852 P.2d 1055 (1993).

RCW 49.48.010 limits the deductions that an employer may make from an employee's wages, and makes it unlawful for any employer to take deductions from an employee's wages except: (1) as required by state or federal law; (2) as specifically agreed upon orally or in writing by the employee and employer; or (3) for medical, surgical, or hospital care or service, pursuant to any rule or regulation.

By contrast, RCW 49.52.060 prohibits an employer from making any deductions from an employee's wages unless the employer is "required or empowered so to do by state or federal law or when a deduction has been expressly authorized in writing in advance by the employee for a lawful purpose accruing to the benefit of such employee," or when the deductions are "for medical, surgical, or hospital care or service, pursuant to any rule or regulation: PROVIDED, That the employer derives no financial benefit from such deduction and the same is openly, clearly and in due course recorded in the employer's books."

In *Pope v. University of Washington*, the Washington State Supreme Court held that the first of these wage deduction statutes, RCW 49.48.010, applies only to deductions from final wages upon termination of employment.

The current payroll deduction regulation, WAC 296-126-025, which was adopted by the Department of Labor and Industries prior to the Pope decision, attempted to reconcile and combine the requirements of the two different wage deduction statutes into a single regulation. In its current (original) form, WAC 296-126-025 prohibits deductions from an employee's wages for: (1) cash shortage, walkouts (failure of customer to pay), breakage or loss of equipment (with certain exceptions) unless caused by a dishonest or willful act of the employee; (2) acceptance of a bad check, unless it can be shown that the employee accepted such a check in violation of known employment procedures; or (3) cash shortages from a cash register, drawn or portable depository provided for that purpose unless the employee has sole access and has participated in the cash accounting at the beginning and ending of the shift.

Following the Washington Supreme Court's decision in the Pope case, there was some confusion among employers as to whether the Supreme Court's ruling meant that both wage deduction statutes (RCW 49.48.010 and 49.52.060) were limited to deductions from the final paychecks of terminating employees, or whether RCW 49.48.010 was limited to terminating employees and RCW 49.52.060 applied to current employees. The new regulations adopted by the Department of Labor and Industries are intended to resolve any conflicts in the payroll deduction statutes and regulations, and clear up any confusion about the proper application of the payroll deduction laws. Following the Washington Supreme Court's decision in the Pope case, there was some confusion among employers as to whether the Supreme Court's ruling meant that both wage deduction statutes (RCW 49.48.010 and 49.52.060) were limited to deductions from the final paychecks of terminating employees, or whether RCW 49.48.010 was limited to terminating employees and RCW 49.52.060 applied to current employees. The new regulations adopted by the Department of Labor and Industries are intended to resolve any conflicts in the payroll deduction statutes and regulations, and clear up any confusion about the proper application of the payroll deduction laws.

### **The New Payroll Deduction Regulations Clarify What Deductions May Be Made From Employee's Final Paycheck Upon Termination**

The new revisions to WAC 296-126-025 are intended to make it clear that the regulation only governs deductions from an employee's final paycheck upon termination. Under the new form of this regulation, employers may deduct any portion of an employee's final wages and may reduce the employee's final gross wages below the state minimum wage if the deduction is:

- Required by state or federal law; or
- Specifically agreed upon orally or in writing by the employee and employer; or
- For medical, surgical or hospital care or service (no deductions may be made for these services if covered under RCW 51.48.050 – the Industrial Insurance Act); or
- To satisfy a court order, judgment, wage attachment, trustee process, bankruptcy proceeding, or payroll deduction notice for child support payments.

The new regulation further clarifies that employers may make the following deductions from an employee's final paycheck (even if the employee's final gross pay is below the state minimum wage rate) as long as the deductions are specifically agreed upon orally or in writing by the employee and employer *in advance of the deduction*:

- For pension, medical, dental, or other benefit plans (e.g., monthly medical premium or 401k payroll deductions); or
- For a payment to a creditor or third party to pay a sum for the benefit of the employee (e.g., deductions for automatic auto loan payments to employee's financial institution by employer are permissible). The creditor or third party can be the employer (e.g., deductions to repay a loan provided to the employee by the employer are permissible provided that the employer charges a "reasonable interest" on the loan).

Employers may also make the following deductions from an employee's final paycheck, but only when the following incidents have occurred in the final pay period and only as long as the deductions *do not* reduce the employee's final gross wages below the state minimum wage:

- For acceptance of a bad check or credit card, if it can be shown that the employee accepted the check or credit card in violation of procedures previously made known to the employee by the employer; or
- For any cash shortage from a cash register, drawer or portable depository provided for that purpose, if it can be shown that the employee has sole access to the cash and has participated in the cash accounting at the beginning and end of the employee's shift; or
- For any cash shortage, walkout (failure of customer to pay), breakage or loss of equipment, if it can be shown that the shortage, walkout, breakage or loss was caused by a dishonest or willful act of the employee; or
- Deductions taken due to alleged employee theft are permissible only if it can be shown that the employee's intent was to deprive and that the employer filed a police report.

Employers bear the burden of proving the existence of any oral or written agreements and of any policies or procedures relied upon in making the deductions. Employers must also identify and record all wage deductions openly and clearly in employee payroll records.

### **The New Payroll Deduction Regulations Clarify What Deductions May Be Made From Current Employees' Paychecks During Ongoing Employment**

In addition to revising the old payroll deduction regulation (WAC 296-126-025), the Department of Labor and Industries has also adopted two completely new payroll deduction regulations: (1) WAC 296-126-028; and (2) WAC 296-126-030. The new regulation contained in WAC 296-126-028 governs deductions from current employees' paychecks during ongoing employment. Under this new regulation, employers may deduct any portion of an employee's wages below the state minimum wage if the deduction is for any of the following reasons and the employee expressly authorizes the deduction in writing and in advance for a lawful purpose for the benefit of the employee:

- The deduction is required by state or federal law; or
- The deduction is for medical, surgical, or hospital care or service; or
- The deduction is being made to satisfy a court order, judgment, wage attachment, trustee process, bankruptcy proceeding, or payroll deduction notice of child support payments.

The new regulation includes examples of proper deductions, including: (1) deductions for employee purchases (provided the product is sold to the employee for the same price or less than it would sell the product to the customer); (2) deductions for employee loans (provided the employee is charged a "reasonable interest"); (3) employee benefit deductions (e.g., deductions for monthly pension, medical, dental or other benefit plans); and (4) deductions for creditor or third-party payments (e.g., auto loan deductions paid directly to an employee's lender).

Employers and those acting in the interest of the employer cannot derive any financial profit or benefit from any of the "current employee" deductions permitted under this regulation. ("Reasonable interest" on employee or creditor loans is specifically exempted from this requirement.) As with deductions from final paychecks, an employer must identify and record all wage deductions for current employees "openly and clearly" in the employer's payroll records.

Employers should note that, unlike deductions for terminating employees, deductions from the pay of current employees are not permitted under any circumstances for bad checks or credit cards, cash register shortages, customer walkouts, or damage or loss to employer equipment.

### **The New Payroll Deduction Regulations Allow Employers to Make Deductions From an Employee's Pay to Recover for Certain Types of Accidental Wage Overpayments**

The new regulation contained in WAC 296-126-030 provides employers with a limited right to make deductions from employees' paychecks to recover for accidental wage overpayments. In addition to addressing overpayments through the wage deductions permitted under this new regulation, employers also retain the right to pursue private legal action to recover any overpayments to an employee.

For purposes of applying the new regulation, an "overpayment" occurs when an employer pays an employee for (1) more than the agreed upon wage rate; or (2) more than the hours actually worked. Under the new regulation, employers may recover for such overpayments, provided that the overpayments are infrequent and inadvertent, by making an adjustment or adjustments to future paychecks. The regulation clarifies that to be considered an infrequent and inadvertent overpayment, the overpayment must have occurred rarely (not regularly or part of a pattern), and the error must have been accidental, unintentional or not deliberately done. The burden of proving that the overpayment was infrequent and inadvertent rests with the employer.

An employer has a maximum period of 90 days from the date an employee has been paid such an overpayment to make any deductions from the employee's pay to recover for the overpayment. Once the 90-day period has expired, the employer may not recover the overpaid wages through a payroll deduction – the employer must pursue private legal action instead. To deduct an employee's wages for an overpayment, the employer must provide documentation of the overpayment to the affected employee or employees and advance written notice to the employee(s) of the terms under which any deductions will be made from their pay to recover for the overpayment. Such deductions may reduce the employee's gross wages below the state minimum wage. The employer must identify and record all permissible wage overpayment deductions openly and clearly in payroll records.

The wage overpayment regulation also provides that, for employees covered by collective bargaining agreements that expire on or after January 1, 2006, in which overpayments are included in the terms of the collective bargaining agreement, the effective date of the regulation shall be the later of (1) the first day following expiration of the collective bargaining agreement; or (2) the effective date of the revised collective bargaining agreement.

The wage overpayment regulation does not apply to public employers.

## **What This Means for Employers**

The good news for employers with employees in Washington is that the new payroll deduction regulations provide employers with detailed explanations and examples of when deductions from employees' paychecks will or will not be permitted by law, and resolve many unanswered questions about the application of the payroll deduction statutes in the wake of the *Pope* decision. The regulations also provide employers with a new method for recovering certain types of accidental overpayments. The bad news is that the new regulations prohibit certain types of payroll deductions for current employees that used to be permitted under the old regulation. For that reason, employers should revisit their payroll deduction policies and practices with legal counsel to ensure that they are in compliance with the new Washington state payroll deduction regulations.

For more information, please contact the [Hot Sheet/Practice Group] Law Practice Group at:

Lane Powell PC:  
(206) 223-7000 Seattle  
(503) 778-2100 Portland

[employlaw@lanepowell.com](mailto:employlaw@lanepowell.com)  
[www.lanepowell.com](http://www.lanepowell.com)

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