On Payment or Non-payment of Premium Wages When Incorporated Into Annual Salary

The Iryo Hojin Shadan Koshin Kai Case

Supreme Court (Jul. 7, 2018) 1168 *Rohan* 49

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Facts

In this case, X (plaintiff of the first instance, appellant of the court below) was employed as a medical doctor at incorporated medical institution Y (defendant of the first instance, appellee of the court below), and sued for premium wages for overtime and night work, etc. Below, only the points debated in the final appeal are described.

(1) According to the employment contract between X and Y, wages should consist of an annual salary totaling 17 million yen (approx. US$14,100) made up of a monthly base salary of 860,000 yen (approx. US$7,100) and a total of 341,000 yen (approx. US$2,800) in monthly fringe benefits (managerial position allowance, duty allowance, adjustment allowance), with a bonus based on the equivalent of three months' salary.

The employment contract specified a five-day work week, with working hours from 8:30 a.m. to 5:30 p.m. (with an hour's recess), and two days off per week, in principle, but stated that if needed the doctor could be called on to work at other times, in which case overtime wages would be based on Y's overtime compensation plan for doctors (hereinafter referred to as the "overtime plan").

In the overtime plan, work that qualifies for an overtime allowance is limited to (a) operations that directly contribute to hospital income or essential emergency services, (b) allowance payments are limited to the actual hours of emergency operations, and payment must be authorized by the manager in charge, (c) the time for which overtime allowances are paid shall be the time spent on emergency services occurring between 9:00 p.m. on a workday and 8:30 a.m. on the next day, or on days off, (d) overtime allowance is not paid for overtime work regarded as an extension of ordinary work, and (e) a separate duty allowance would be paid to doctors on duty or day duty.

In the employment contract, it was agreed that premium wages for overtime work, etc., other than those paid under the overtime plan, would be included in annual salary of 17 million yen (hereinafter referred to as "the agreement"), but what proportion of the annual salary consisted of premium wages for overtime work, etc. was not disclosed.

(2) Y calculated X's overtime work during the employment period (six months) as 27.5 hours (of which 7.5 hours was night work) for X, paid an overtime allowance of 155,300 yen for this, and paid a total of 420,000 yen as a duty allowance. In the calculation of overtime allowance, although night work was compensated at a premium rate, other overtime work was not.

(3) X filed a lawsuit against Y for payment of premium wages for overtime totaling 4,380,000 yen and damages for delayed payment, etc.

In both the first and the second trials, the judgments recognized part of X's claim, limited to 563,380 yen in premium wages, but dismissed the rest of the claim, and X appealed.

Judgment

The supreme court decided that in the high

court judgment the part of the claim related to premium wages was reversed, and the case was remanded to the Tokyo high court.

(1) Employers' obligation to pay premium wages for overtime work etc. under Article 37 of the Labor Standards Act (LSA) is intended to curtail overtime work etc. by making employers pay premium wages, and thus such obligation under the Act is understood to have the purpose of ensuring employers observe the Act's provision on working hours and compensate their employees…It is understood that employers are obligated only to pay premium wages to ensure that the amount paid is not less than that calculated by the method prescribed in said Article (author's note: related provisions on calculation of premium wages), and here the method itself, of paying premium wages by including them in advance in the base salary or other allowances, is not immediately against said Article.

(2) On the other hand, in order to determine whether an employer has paid an employee the premium wages mandated by Article 37 (LSA), it is necessary to consider whether the amount paid as premium wages is not less than the amount of premium wages calculated by the method prescribed in said Article, based on the wages for ordinary working hours. In line with said Article, in cases where premium wages are paid in advance as part of the base salary etc., as a prerequisite for this consideration, it is necessary to be able to distinguish between the ordinary wages and premium wages respectively in the employment contract's provisions on base salary. If the amount of the premium wages falls below the amount calculated by the method prescribed in said Article, etc., the employer is obligated to pay the difference to the employee.

(3) Although the agreement between X and Y states that premium wages for overtime work, other than those paid based on the overtime plan, are included in the annual salary of 17 million yen, it does not clarify which portion of wages corresponds to premium wages for overtime work etc. This means the agreement cannot be used to determine what amount of wages have been paid to X as premium wages for overtime work etc. Also, with regard to the annual salary paid to X, it is not possible to distinguish between the portion corresponding to wages for normal working hours and that corresponding to premium wages.

Therefore, it cannot be said with any certainty that Y has paid X premium wages for X's overtime work and night work.

(4) Being different from above-mentioned opinion, the judgment of the court below violates laws, which has obviously affected its decision. ..... We hereby remand this case to the court below and ask for further, careful consideration of whether Y has paid X all the premium wages calculated by the method prescribed by Article 37 (LSA) based on the amount of the portion equivalent to the wage of normal working hours.

Commentary

This decision is significant and distinctive in several ways.

First, regarding the form of wage payment, with premium wages included in wages normally paid, the court followed the precedents of Supreme Court decisions[1] in making a judgment on the suitability of this form of payment of premium wages for legally mandated overtime work and night work. It judged that in order to determine whether legally mandated premium wages have been paid, it is necessary to be able to distinguish between ordinary wages and premium wages, and furthermore that the amount of premium wages paid must not be less than the amount calculated by the legally prescribed method (see (2) in Judgment).

Second, while the court reiterated that the premium wage payment method of including premium wages in wages normally paid is not invalid per se,[2] as a precondition, there must be clear compliance with the purport of the premium wage provision under Article 37 of LSA. In particular, the purport of said Article is interpreted as being the curtailing of overtime work by mandating that employers pay premium wages (see (1) in Judgment).

The prior to Supreme Court rulings stated that the significance of the premium wage regulation was ensuring compliance with the working hours

principle (8 hours per day, 40 hours per week) and financial compensation for employees who do overtime work. The new judgment further emphasizes these and explicitly shows understanding of the intent to curtail overtime work. With the enactment of the Work Style Reform Bill (Jun. 29, 2018), while reducing excessively long work hours is being carried out on both the policy and practical fronts, this court judgment is in line with social trends in terms of its legal interpretation.

Third, the plaintiff in this case is a professional, medical doctor, who has discretion in performing work tasks and whose salary is considerably higher than those of average employees. According to this judgment, working hours regulations regarding premium wages are to be strictly applied not only to average employees such as shop-floor operators and office employees but also to specialized employees with high salaries and discretion in performing work tasks.

There were already lower court precedents with regard to premium wage for overtime work by such specialized employees with high salaries and discretion in performing work tasks.[3] In one of these cases, the *Morgan Stanley Japan* case, involving a foreign currency trader with a monthly salary of about 1,830,000 yen, interpreting premium wages as being included in wages ordinarily paid was not in violation of the LSA.

Also, regarding the *Tech Japan* case, the lower court ruled[4] that if fixed monthly salary of 410,000 yen is paid for total monthly working hours of between 140 hours to 180 hours, premium wages need not be paid even when exceeding the standard monthly working hours of 160 hours, and rejected the claim of the plaintiff, a programmer, whose salary was set significantly higher than those of other employees, as having voluntarily waived the right to premium wages if working in excess of 160 hours but less than 180 hours per month (however, the court mandated that for work exceeding 180 hours a month, the employer was to pay an hourly rate determined by dividing the prescribed monthly salary by the prescribed monthly working hours).

The initial and second decision in the *Koshin Kai* case adopted the same position as the lower court ruling for the Morgan Stanley Japan case, but the Supreme Court judgment in this case rejected its interpretation. In the decision for the Tech Japan case, the lower court judgment on normal wages and premium wages was overturned due to the impossibility of distinguishing between them at the Supreme Court. This can be seen as the Supreme Court reiterating the position that mandated premium wages regulations are to be strictly applied, regardless of the nature and mode of work and salary amount.

Given the Supreme Court ruling in this case in question, some readers may wonder whether Japanese law lacks provisions on exclusion from working-hours limits and premium wages for professional, discretionary, high-salaried employees.

In fact, such provisions exist in Japan. One is in Article 41(ii) of LSA (persons in positions of supervision or management), another in Article 38-3 and 38-4 of LSA (specialized work and discretionary management-related work, and the other in the bill that recently passed the Diet (The "highly professional" work system).

The system for persons in positions of supervision or management excludes said persons from the application of the provisions regarding working hours. As to whether or not someone is covered by this system, in administrative practice and judicial precedents thus far, people have been judged on whether they (i) participate in management decisions and have labor management authority, (ii) have discretion about working hours, such as what time they begin and end work, and (iii) their wages and treatment, etc. are in line with such status and authority. Those who meet these criteria are excluded from the application of the regulations pertaining to working hours, rest periods, and days off, including regulations governing overtime work and premium wages (those regarding premium wages for night work and annual leave still apply).

The discretionary work system is one that deems people to have worked for a certain period of time, and in some cases overtime work and premium

wage regulations do not apply to these employees. Execution of tasks is largely up to the discretion of employees because of the nature of the work, and it is difficult for employers to specify procedures and allocation of time for the jobs in question (19 specialized and 8 planning-oriented occupations). The system can be applied after certain procedures such as a majority labor-management agreement (specialized type) or a resolution by a labor-management committee and employee's consent (planning-oriented type). Since the discretionary work system deems employees to have worked the hours prescribed in these agreements or resolutions, regardless of the actual working time, unless the number of hours deemed worked exceeds the legal limit working hours, premium wages are not paid. This system has the same effect as the system for exclusion from overtime work and premium wages (regulations governing premium wages for night work, rest periods, days off, and annual paid leave still apply).

The highly professional work system was established as one of the work style reforms the current administration is pursuing, and excludes a wider range of application than the above two systems. Under this system, in cases where the scope of jobs is clear and employees with a specified annual income (at least 10 million yen) are engaged in work requiring highly specialized knowledge, they are excluded from premium wage regulations governing working hours, rest periods, days off, and night work (annual paid leave regulations still apply), on the condition that they are given, and actually take, 104 days off per year as a health protection measure, and that there is both a resolution by a labor-management committee and employee's consent. As a result, employees to whom this system applies are not covered by overtime work and premium wage regulations.

Those exclusionary systems or similar systems do not specify "medical doctor" as a job category to which they apply (note that the highly professional work system has not yet gone into effect), and cases like these regarding overtime work and premium wages for employees of this particular profession must be determined by court decisions such as this one. Thus, in practice, an employer adopting a system where total wages include premium wages (even if there is some form of agreement between the employer and employees about the wage payment system, as in this case) bears the duty to calculate the premium wages based on the purport of Article 37 (LSA) covering the wage form of all employees including high-salaried employees who perform specialized, discretionary work, unless the employer applies one of the above systems of exclusion from regulations governing overtime work and premium wages to the employees. Otherwise, the employer is required the thorough management of working hours and calculation of overtime and night work hours. And under a wage system where it is possible to distinguish between the portion constituting normal wages and that constituting premium wages, it is necessary to pay employees premium wages not less than the amount calculated by the method specified by law. Therefore, this judgment promises to have a highly significant impact on employers' wage and working-hours practices.

1. The *Kochi Kanko* case, Supreme Court (Jun. 13, 1994) 653 *Rohan* 12; The *Tech Japan* case, Supreme Court (Mar. 8, 2012) 1060 *Rohan* 5; The *Kokusai Motorcars* case, Supreme Court (Feb. 28, 2017) 1152 *Rohan* 5.
2. This point was also mentioned in the *Kokusai Motorcars* case (see note 1) reviewed in *Japan Labor Issues*, vol 2, no. 4 (January 2018).
3. The *Morgan Stanley Japan* (overtime allowance) case, Tokyo District Court (Oct. 19, 2005) 905, *Rohan* 5.
4. The *Tech Japan* case, Tokyo High Court (Mar. 25, 2009) 1060 *Rohan* 11. The *Tech Japan* case, Yokohama District Court case (Apr. 24, 2008) 1060 *Rohan* 17.

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