DechertOnPoint

Current Trends in FLSA Litigation

by Alan D. Berkowitz, R. Michael Smith, Brian E. Hirsch, and Jane E. Patullo
Dechert LLP

Dechert LLP 2005 Labor and Employment Seminar

Copyright 2005 Dechert LLP. All rights reserved. Materials have been abridged from laws, court decisions, and administrative rulings, and should not be considered as legal opinions on specific facts or as a substitute for legal counsel.

www.dechert.com

Dechert LLP

Current Trends in FLSA Litigation

By Alan D. Berkowitz, R. Michael Smith, Brian E. Hirsch, and Jane Patullo

Fair Labor Standards Act ("FLSA") litigation is on the rise, with plaintiffs developing innovative litigation strategies. Due to the length and complexity of both the FLSA and its associated regulations, it can be difficult for employers to comply with their many and varied obligations. What follows is a non-exhaustive compendium of some of the more difficult situations employers have recently faced. They provide employers with an overview of the kinds of issues that have felled other businesses in the past, with the hope that similar difficulties can be avoided in the future.

A. Misapplication of The Executive, Computer Employee And Administrative Exemption Tests

In order to qualify as exempt under the executive, computer employee, or administrative exemption tests, an employee's primary duty must be the performance of exempt work as described in the U.S. Department of Labor, Wage and Hour Division ("DOL" or "WHD") regulations relevant to the particular exemption.[1] Generally, an employee who spends more than fifty percent of his/her time performing exempt work satisfies this primary duty requirement. The term "primary duty" means the principal, main, major or most important duty the employee performs, and the determination of what constitutes primary duty must be based on all of the facts in a particular case, with major emphasis on the character of the employee's job as a whole. Time alone is not the test, and an employee who does not spend over fifty percent of his/her time on exempt duties may qualify as exempt if all other factors support such a conclusion. However, in reality, it is difficult for an employer to prove that an employee who spends less than half of his/her time doing exempt work is exempt. See 29 C.F.R. §541.700.

An employee who "customarily and regularly" performs a task or function does so normally and recurrently every work week, but not necessarily constantly. 29 C.F.R. §546.701. Work "directly and closely related" to exempt work -- i.e., tasks that facilitate the performance of exempt work and are related to exempt duties (e.g., a department manager's keeping sales records for subordinates) -- is considered exempt work. See 29 C.F.R. §541.703.

1. Executive Employees

Some retail companies have misclassified certain workers as exempt executives. Executives are exempt from the FLSA's overtime obligations. DOL regulations define which employees are "executives" for

[1] See 29 C.F.R. Part 541. Each of the tests also requires that an employee be paid at least $455 per week on a salary basis. In the case of an administrative or computer employee, the person may also be paid on a fee basis, or in the case of a computer employee, an hourly rate of at least $27.63.

© 2005 Dechert LLP. All rights reserved. Materials have been abridged from laws, court decisions, and administrative rulings and should not be considered as legal opinions on specific facts or as a substitute for legal counsel.

overtime exemption purposes. To qualify as exempt, an executive must meet the following requirements, in addition to meeting the salary basis test:

(1) have as their primary duty the "management" of the enterprise for which she works;

(2) regularly direct the work of two or more other employees;

(3) have either the authority to hire and fire other employees, or at least give recommendations about hiring, firing, and promotions that are given particular weight.

See 29 C.F.R. § 541.100. Federal regulations go on to define "management" to include, among many things, hiring and training employees; directing the work of employees; evaluating employees' work; disciplining employees; budgeting; and monitoring legal compliance. See id. § 541.102.

In *Pendlebury v. Starbucks Coffee Company*, No. 04-80521, 2005 U.S. Dist. LEXIS 574 (S.D. Fla. Jan. 3, 2005), the court conditionally certified a class of current and former Starbucks' retail outlet store managers. The plaintiff was a current Starbucks' retail store manager in Broward County, Florida. Although he was a salaried employee classified by Starbucks as an executive exempt from FLSA overtime obligations, he claimed that his actual duties had little to do with the management work suggested by his job title. He claimed his predominant duties were waiting on customers, making coffee drinks, and ringing up sales. He also claimed he rarely exercised discretionary powers, was not free from supervision, and did not regularly supervise two or more full-time employees. Finally, he claimed his pay was not substantially different from other employees, such as shift supervisors and assistant managers, who were non-exempt. Plaintiff produced affidavits from store managers in three other states who made similar allegations.

The court conditionally certified the class. Although Starbucks presented some evidence tending to rebut the plaintiff's allegations, the court noted that the plaintiff's burden at the conditional class certification stage was light. Based upon the plaintiff's allegations, as well similar allegations from other employees in several other states, the court found conditional class certification was warranted.

2. Computer Employee

To qualify as an exempt computer employer, an employee's primary duty must consist of one or a combination of:

- the application of systems analysis techniques and procedures, including consulting with users, to determine hardware, software or system functional specifications;
- the design, development, documentation, analysis, creation, testing or modification of computer systems or programs, including prototypes, based on and related to user or system design specifications; or
- the design, documentation, testing, creation, or modification of computer programs related to machine operating systems. See 29 C.F.R. §541.400.

Computer systems analysts, computer programmers, software engineers and similarly skilled employees in the computer field are eligible for this exemption. Not eligible are employees engaged in the repair of hardware and related equipment or those whose work is highly dependent on or facilitated by computers

but who are not primarily engaged in systems analysis, programming, or similar work. See 29 C.F.R. §541.401-.402.

In its preamble to DOL's revised Part 541 regulations, effective August 23, 2004, the DOL rejected commenters' proposals that the agency specify job titles beyond "computer systems analyst, computer programmer, software engineer or similarly skilled worker" in the regulations at 29 C.F.R. §§541, 400-402. Among job titles DOL declined to add were: network manager, LAN/WAN administrator, website design and maintenance specialist, systems support specialist performing similar duties with hardware, software and communications networks, systems integration professional, help desk professional, database analyst/developer, Internet administrator, person responsible for troubleshooting, person who trains new employees, person who installs hardware/software, and technical writer. See Fed. Reg. Vol. 69, No. 79, April 23, 2004, pp. 22158-60. DOL did acknowledge that employees in some of these titles/jobs could meet the primary duty test for computer exemption if the employee was similarly skilled to a systems analyst, programmer or software engineer, but only where the employee's primary duty included: applying systems analysis techniques/procedures to determine hardware, software or systems functional specifications; or, the design, development, documentation, analysis, creation, testing or modification of computer systems or programs based on/related to user or system design specifications; or, the design, documentation, testing, creation, or modification of computer programs related to machine operation systems; or, a combination of such duties. DOL also acknowledged that certain of the jobs might qualify for administrative exemption. For example, according to DOL, an employee whose primary duty is planning, scheduling, and coordinating activities to develop systems to serve complex business, scientific or engineering problems of his employer or employer's customer may qualify as administratively exempt, depending on the facts.

Recently in *Martin v. Indiana Michigan Power Company*, 381 F.3d 574 (6th Cir. 2004), the Sixth Circuit interpreted the computer exemption narrowly, concluding that a highly skilled employee who installed and upgraded hardware and software on workstations, configured desktops, checked and replaced parts, and troubleshot problems was not exempt. The employee, an Information Technology Support Specialist, was not a programmer, systems analyst, software engineer, or similarly skilled worker. While his primary duty required specialized knowledge of computers and software, it did not require highly-specialized knowledge in computer systems analysis, programming or software engineering. And, even though the employee consulted with users and did testing, the consulting was not for the purpose of determining hardware, software or functional specifications, and the testing was for troubleshooting purposes and not for the purpose of creating a system or otherwise substantially affecting a system.

Also, the U.S. District Court in Connecticut recently allowed a collective action brought by computer employees under FLSA to go forward. *Richards v. Computer Sciences Corp.*, D. Conn., No. 3-03-CV-00630 (DJS), 9/28/04. The employees were help desk workers who troubleshot clients' computer problems. They primarily spent time resolving application and network problems for their clients.

3. Administrative Exemption

To qualify for this exemption, an employee must have as a primary duty office or non-manual work directly related to the management or general business operations of his employer or the employer's customers, and that work must include the exercise of discretion and independent judgment with respect to matters of significance. See 29 C.F.R. § 541.200. Note that in recent opinion letters, DOL stated that

the duties test for the administrative exemption test under its regulations revised in 2004 was substantially the same as under the prior rule. FLSA 2005-21 (8/19/05) and FLSA 2005-19 (8/2/05).

Under the regulations, work "directly related to the management or general business operations" means work directly related to assisting with the running or servicing of the business, as distinguished from the business's production -- such as selling in a retail/service establishment or working on a production line. "Directly related work" includes work in functional areas, such as tax, finance, accounting, budgeting, auditing, insurance, quality control, purchasing, procurement, advertising, marketing, research, safety and health, personnel management, human resources, employee benefits, labor relations, public relations, government relations, computer network, internet and database administration, legal and regulatory compliance and similar activities. See 29 C.F.R. § 541.201.

To qualify as exempt, an employee's primary duty must include the exercise of discretion and judgment with respect to matters of significance. Whether an employee actually does so is a factual determination. In general, the exercise of discretion entails the comparison and evaluation of possible courses of conduct and the setting or making of decisions after considering various possibilities; it implies the authority to make independent choices, free from direct supervision. The employee's decision need not be final. However, such exercise must be more than use of skill in applying established techniques, procedures, and standards. It does not include clerical or secretarial work, recording/tabulating data, or performing mechanical, repetitive, recurrent or routine work. Also, an employee does not exercise discretion and judgment respecting matters of significance merely because his/her employer will experience financial loss if the employee fails to perform his/her job properly.

Factors to consider when determining if an employee meets the discretion and judgment requirement are:

- The employee's authority to formulate, affect, interpret, or implement management policies/operating practices.
- Whether the employee carries out major assignments in conducting operations of the business.
- Whether the employee performs work that substantially affects business operations to a substantial degree, even if assignments are related to operations of a particular segment of the business;
- Whether the employee has authority to commit the employer in matters that have significant financial impact;
- Whether the employee has authority to waive or deviate from established policies and procedures without prior approval;
- Whether the employee has authority to negotiate and bind the company on significant matters;
- Whether the employee provides consultation or expert advice to management;
- Whether the employee is involved in planning long- or short-term business objectives;
- Whether the employee investigates and resolves matters of significance on behalf of management; and
- Whether the employee represents the company in handling complaints, arbitrating disputes or resolving grievances. See 29 C.F.R. § 541.202.

According to the relevant regulations, examples of exempt employees are: a purchasing agent with authority to bind the company on significant purchases; human resources managers; an employee who leads a team of others assigned to complete a major project, such as selling/closing a business, real estate transaction, etc.; an executive assistant to a senior executive or business owner who is delegated authority regarding matters of significance and handles them without specific instructions/prescribed procedures; certain financial services industry employees who analyze customer information and advise customers; certain insurance claims adjusters. Examples of clearly non-exempt positions are public sector inspectors and personnel clerks.

The Sixth Circuit's decision in *Martin v. Indiana Power*, which is described above, is illustrative of fact-finders' often narrow interpretation of this test. The Court concluded that the IT Support Specialist who failed to meet the computer exemption also was not an exempt administrative employee. The court noted that while the regulations distinguish administrative operations from production, they do not set up an absolute dichotomy under which all work that is not production qualifies as administrative or, more specifically, administratively exempt. Note that the decision parses the regulations in effect prior to August 23, 2004 and discusses whether the employee's work related to "administrative operations" -- that is, whether it entailed "servicing" the business as, for example, advising management, planning, negotiating, representing the company, purchasing, promoting sales, and business research and control. The current regulations do not refer to "administrative operations," but do note that the employee must be engaged primarily in work directly related to assisting with running or servicing the business, as opposed to production or sales.

Under the former version of the regulations, the employee's primary duty work had to be of substantial importance to the management or operation of the business of his employer or customer; such work was not limited to persons who would participate in the formulation of management policies or in operation of the business as a whole, but also included those whose work affected policy or whose responsibility it was to execute or carry policy out. See 29 C.F.R. § 541.205. According to the Sixth Circuit, examples of tasks the IT Support Specialist could have done that would have met this standard (but which he did not perform) were:

- making decisions that affect a segment of operations;
- determining types of workstations, network, hardware or software to be used;
- being involved in the design or development of the company's network;
- deciding what software would be available to the company's computer users or determining how the software would be configured; [or]
- deciding/recommending when equipment must be serviced or replaced.

Instead, the employee set up and repaired parts of a system designed and approved by others. That the employee's work was "not clerical" and arguably was "complex" made no difference.

In a recent opinion letter, DOL considered whether background investigators of a private employer who investigated employees in the federal government were administratively exempt. FLSA 2005-21

(8/19/05). The investigator conducted extensive interviews and checked records on-line and otherwise, according to broad guidelines determined by the federal government. DOL concluded the employees were related to their employer's day-to-day operations, and were not directly related to managing their employer's business. If their work directly related to managing the federal government's business, the employees did not exercise sufficient discretion and judgment to qualify as exempt.

4. Combination Jobs

Employers sometimes have difficulty determining whether an employee who works in two positions for his/her employer is exempt. Note that in a recent opinion letter, DOL explained that if an employee regularly works in two positions for an employer – only exempt and the other non-exempt, the employer must determine which job's duties qualify as the employee's primary duty. If the primary duty is non-exempt, the employer cannot purge the tasks of the two jobs and separate exempt and non-exempt work for calculating compensation. Total hours spent on both jobs would need to be aggregated to determine the number of overtime hours worked. See FLSA 2005-14 (3/17/05).

B. Errors In Applying The Salary/Fee Basis Test and Use of "Safe Harbor"

1. "Window of Correction"; "Safe Harbor"

Some employers have policies and/or practices which evidence an intent not to treat employees as exempt executives. As a result, covered employees lose any exemption they would otherwise be entitled to, and the employer is precluded from taking advantage of the FLSA's "window of correction" or "safe harbor" provision that would otherwise have allowed the employer to correct the mistake without any further penalty. Exemptions for salaried employees depend in part upon whether those employees are paid on a "salary basis." The Federal regulations define payment on a "salary basis" as "regularly receiv[ing] each pay period on a weekly, or less frequent basis, a predetermined amount constituting all or part of the employee's compensation, which amount is not subject to reduction because of variations in the quality or quantity of the work performed." 29 C.F.R. § 541.602. Employers, of course, sometimes make mistakes in calculating proper salary deductions. Some improper deductions result in the loss of an employee's exempt status (thus triggering, among other things, overtime obligations on behalf of the employer towards the employee). Other improper deductions do not. See id. at § 541.603.

Improper deductions that cause the loss of an employee's exempt status include those that reveal that the employer did not intend to pay its employees on a salary basis. Factors relevant to this determination include the number of improper deductions, the time period during which improper deductions were made, and the number and geographic location of employees' whose salaries were subject to improper deductions. A factual demonstration that the employer had an actual practice of making improper deductions will also cause the loss of the employee's status. Note that an improper deduction with respect to one salaried employee will cause the loss not only of that employee's exempt status, but also of the exempt status of all employees in the same job classification working for the same managers responsible for the actual improper deduction (but no other employees).

Improper deductions that are either "isolated or inadvertent" do not result in the loss of exemption for affected employees so long as the employer reimburses the employees for the improper deductions. This opportunity to correct mistaken deductions without penalty is referred to as the "window of correction."

In *Wilkes v. J&J Enterprises, Inc.*, 2005 Ohio 106 (Ohio Ct. App. 2005), the court held that the employer was not entitled to the "window of correction." In *Wilkes*, the plaintiffs were managers of pizza franchise locations. They were all paid a salary plus non-discretionary bonus if sales goals were met. Managers were subject to suspension without pay and salary reductions for cash shortages. The plaintiffs were all subject to disciplinary deductions. Well into the litigation, the employer agreed to repay employees for the deductions at issue. The court nevertheless held that the employer was not entitled to protection under the window of correction. The management handbook that discussed the employer's salary deductions policy created a significant likelihood of disciplinary-based pay reductions, reductions which are inconsistent with the salary basis test. The evidence demonstrated a clear, intentional, and ongoing policy of making these pay deductions. Accordingly, the employer had both a policy and an actual practice of making improper deductions, and thus the safe harbor of the "window of correction" did not apply. Note that although *Wilkes* was decided under the previous version of the applicable regulation, it would likely be decided the same way under the current regulations.

2. "Fee basis" exemption

Some employers lose the exempt status of their workers by incorrectly implementing payment fee basis systems. Federal regulations allow employers to pay "administrative and professional" employees on a fee, rather than salary, basis. See 29 C.F.R. § 541.605. A "fee basis" means paying the employee "an agreed sum for a single job regardless of the time required for its completion." Id. Fee basis differs from piecework payments in that the former are for work "that is unique rather than for a series of jobs repeated an indefinite number of times and for which payment on an identical basis is made over and over again." Id. Payments based on hours worked rather than accomplishing a specific task are not made on a fee basis. See id.

Broadly defined, "administrative" employees are paid at least $455 per week, perform office or non-manual work directly related to the management of the company, and primarily exercise discretion and judgment on significant matters. See 29 C.F.R. § 541.200.

"Professional" employees also earn at least $455 per week and perform duties that require advanced knowledge in their field (usually gained through advanced study) or exercise invention, imagination, artistry, or creativity. See 29 C.F.R. § 541.300.

The Wage and Hour Division of the Department of Labor ("WHD") recently issued an opinion letter helping to define the contours of the fee basis provision. In FLSA2005-24, dated August 26, 2005, the WHD considered a plan propounded by an accounting firm to pay its accountants on a "per transaction" or "flat fee" basis. Most of the employer's accounts worked from home and were tasked with a number of relatively routine matters, such as electronically entering vendor bills, generating checks for payment, and entering invoices. The company charged flat fees for many of these tasks. Rates to clients were relatively low: $2 per entered transaction, for example. Employees were paid a fixed percentage of the flat fees, usually 30-40% of the fee charged to the client. Other work, such as setting up computer

systems, was charged to clients on an hourly basis. Again, employees received a fixed percentage of whatever the amount charged to clients ended up being.

WHD assumed for purposes of its analysis that the accountants were professionals for FLSA exemption purposes. The issue was whether the payments to the accounts were properly made on a fee basis. WHD opined that they were not. It reasoned that the arrangement most resembled a piecework structure, not a fee basis. It viewed most of the accountants' tasks as a series of repeated, indefinite, and identical tasks. The fact that accountants repeatedly earned the same amount for the same kinds of tasks reinforced its view. Plus, the WHD viewed the hourly-based compensation structure as intrinsically inconsistent with permissible fee basis arrangements.

3. Changes In Salary

Employees who change salaries in response to changes in business circumstances must do so carefully to avoid losing an exemption. Recently, in *Archuleter, et al. v. Wal-Mart Stores, Inc.*, 345 F.3d 1177 (10th Cir. 2005), pharmacists challenged their exemption, alleging they were not paid on a salary basis. The pharmacists were assigned a certain number of base hours (typically 90 hours for two weeks) and paid a specified minimum salary each pay period, plus pay for work beyond base hours. The minimum salary was not subject to deductions. However, on occasion in response to sales declines and seasonal drops, Wal-Mart prospectively reduced base hours and minimum salaries, which policy plaintiffs' contend was inconsistent with payment on a salary basis. Reversing summary judgment in favor of plaintiffs, the court stated that FLSA permits and employer to prospectively adjust salary to accommodate business needs, so to prevail plaintiffs' would need to establish that the changes were so frequent as to note the salary equivalent to an hourly wage and thus a sham.

C. Problems Related To Correctly Capturing "Hours Worked" and Calculating The Regular Rate For Operation Purposes

1. "Joint Employer" situations

Some employers incorrectly calculate employees' overtime hours for employees who work for more than one of a parent company's subsidiaries. Others become liable for work performed by their contractors' employees. An "employer" includes "any person acting directly or indirectly in the interest of an employer in relation to an employee." 29 U.S.C. § 203(d). A "person" is defined broadly to include associations, corporations, or "any organized group of persons." 29 U.S.C. § 203(a). An "employee" is "any individual employed by an employer." 29 U.S.C. § 203(3)(1). To "employ" means "to suffer or permit work." 29 U.S.C. § 203(g).

A single individual can be an employee of two or more employers at the same time. When this happens, the employing entities may be "joint employers." Determining whether employers are joint depends upon the facts of the particular situation. "If all the relevant facts establish that two or more employers are acting entirely independently of each other and are completely disassociated with respect to the employment of a particular employee, . . . each employer may disregard all work performed by the employee for the other employer . . . in determining his own responsibilities under the [FLSA]." 29 C.F.R. § 792.2. Alternatively, if the facts establish that "employment by one employer is not completely

disassociated from employment by the other employer(s)," then the employers are "both individually and jointly" responsible for compliance with all applicable provisions of the FLSA, "including overtime provisions." Id.

As a practical matter, this issue arises when, among other instances, a single parent has different subsidiaries and an employee works for both.

On April 11, 2005, the WHD issued FLSA2005-15, which sought to clarify the joint employer regulation. There, a holding company with no employees owned both an acute care hospital and a nursing home. A nurse worked during the week at one and over the weekend at the other. The holding company wanted to know if the hours worked at both entities counted together towards the FLSA's forty hour work week, or if the employee's weekly overtime calculations should be made independently for the hours worked at each subsidiary.

The WHD concluded that the holding company was the employee's joint employer, so that the employee's weekly overtime calculation had to include hours worked at both subsidiaries. The WHD observed that the subsidiaries shared the same President and Board of Directors; the Vice President of Human Resources and other senior executives had responsibilities across the subsidiaries; HR staff consulted across entities; and job vacancies were cross-listed.

The joint employment relationship can also vex employers when employees use it to pull a separate entity with deep pockets into FLSA litigation. In *Zavala v. Wal-Mart Stores, Inc.*, No. 03-5309, 2005 U.S. Dist. LEXIS 22990 (D.N.J. October 7, 2005), the court relied on the joint employer theory to deny Wal-Mart's motion to dismiss plaintiffs' FLSA claims. In *Zavala*, a group of illegal immigrants sued Wal-Mart for, among other things, overtime pay. Wal-Mart did not hire the plaintiffs, who cleaned various Wal-Mart stores; a contractor did. Wal-Mart sought dismissal of the FLSA claim, reasoning it was not the plaintiffs' "employer" for FLSA purposes. Looking at the broad language of the FLSA and its remedial purposes, the court refused to dismiss the count. Plaintiffs had explicitly referred to Wal-Mart as their joint employer, and they pled that they had worked exclusively at various Wal-Mart locations, and that Wal-Mart had used its power to hire and fire plaintiffs as well as control their working conditions. At the motion to dismiss stage of the litigation, the court found the plaintiffs allegations sufficient to survive.

2. Donning, Doffing, Walking, and Waiting

Some employers improperly distinguish between non-compensable pre- and post- liminary work and compensable activities. The Portal-to-Portal Act provides in pertinent part that the following employee activities are not compensable:

> (1) walking, riding, or traveling to and from the actual place of performance of the principal activity or activities which such employee is employed to perform, and
>
> (2) activities which are preliminary to or postliminary to said principal activity or activities, which occur either prior to the time on any particular workday at which such employee commences, or subsequent to particular workday at which he ceases, such principal activity or activities. 29 U.S.C. § 254(a).

The Supreme Court has consolidated and agreed to decide two cases in which it will decide whether employees' walking to and waiting at safety equipment distribution centers is compensable, or if the Portal-to-Portal Act precludes that time from being compensable. In *Tum v. Barber Foods, Inc.*, 360 F.3d 274 (1st Cir. 2004), and *Alvarez v. IBP, Inc.*, 339 F.3d 894 (9th Cir. 2003), the courts came to opposite conclusions despite very similar scenarios.

In *Tum* and *Alvarez*, the employers, both are meat processing plants, and both require employees to don substantial amounts of safety equipment before they can begin processing meat. Some safety equipment is distributed to employees once and then replaced as needed. However, as one can imagine in a meat rendering plant, substantial amounts of equipment must be cleaned and replaced daily. Every day, employees must walk to and wait for distribution of this equipment. Depending on the job, employees can spend from 20 to 35 minutes per day both donning, and then at the ends of their shifts doffing, this equipment.

Employees claim that the time they spend walking to and from safety equipment distribution centers, as well as time spent waiting for the equipment to be distributed, is compensable. They argue, in essence, that this walking and waiting time is essential to their work and, therefore, compensable. Employers counter that their employees' principal activities are not donning and doffing safety equipment, nor walk to and waiting for it to be distributed, but rather meat processing. In any event, they argue, walking, riding, or traveling to and from the actual place of performance of the principal activity are explicitly excluded from compensability by the Portal-to-Portal Act. Moreover, they argue that legislative intent shows that Congress intended to preclude this sort of travel time from compensability.

The Supreme Court is expected to issue its ruling in this consolidated appeal later this year or early in 2006.

3. Compensability of Bonuses

Bonus arrangements remain popular forms of non-traditional payments to employees; failure to ensure they meet the "discretionary" test can result in unforeseen overtime pay liability. Generally, the FLSA divides bonuses into discretionary and non-discretionary bonuses. Only the former are excludable from the regular rate.

Bonuses made in recognition of services performed during a given period qualify as discretionary if:

- both the fact that the payment will be made <u>and</u> the amount of the payment are determined at the sole discretion of the employer; <u>and</u>

- the payment is not made pursuant to any promise, agreement, or contract causing employees to expect such payments regularly. <u>See</u> 29 U.S.C. § 207(e)(3); 29 C.F.R. § 2278.211.

If an employer decides early in a year to pay a bonus at the end of the year and conveys this decision to employees, the bonus is not considered discretionary even if the employer retains discretion as to amounts. Discretion as to payment and amounts must be retained until at or near the end of the period the bonus covers. Payments made in the nature of gifts at holidays or other special occasions are excludible

from the regular rate, provided the amount is not based on production, efficiency or hours worked. This is so even if they are paid regularly.

Non-discretionary bonuses must be included in the regular rate. Examples of includable bonuses are:

- those announced to employees to entice them to work more steadily, rapidly and/or efficiently;
- bonuses to remain working for the employer;
- attendance bonuses; and
- bonuses for productivity, quality/accuracy of work, safety, etc. See 29 C.F.R. § 778.211(c)

Generally, profit-sharing bonuses qualify for exclusion from the regular rates if made pursuant to a bona fide profit-sharing plan. See 29 U.S.C. § 207(e)(3)(b).

A few years ago, a federal district court determined that "longevity bonuses" were non-discretionary and includible in the regular rate. *Theisen v. City of Maple Grove*, 41 F.Supp.2d 932 (D. Minn. 1999).

Calculation of overtime due on an includible bonus can be confusing, particularly where the bonus is deferred over a period of time longer than a workweek (e.g., a calendar quarter or year) and paid after the work period to which it applies.

In the case where an includible bonus, such as a production bonus, is deferred, the employer can ignore it until such time as the bonus amount can be ascertained. Once it can be ascertained it must be apportioned back over the workweeks in the period it may be said to have been earned. The employee must then receive for each statutory overtime hour one half of the hourly rate of pay allocable to the bonus (which itself constitutes straight pay for all hours in the workweeks) for which it is paid. If a bonus is not allocable to particular workweeks but covers a longer period (e.g., calendar quarter), it may be assumed that any equal amount applies to each workweek in the bonus period. See 29 C.F.F. § 778.209.

By way of example, suppose an employee worked in 2004 and was paid an hourly rate of "$23.05. He regularly worked a 40 hour workweek (2080 for the year) and also worked 787.5 hours of overtime, or a total of 2867.5 hours during 2004. Prior to payment of his annual bonus, he received ($23.05 x 2867.5 hrs., or $66,095.87) + ($23.05/2 x 787.5 hrs., $9,075.94) = $75,171.81. His regular rate was the same as his hourly rate.

He now receives a performance bonus of $3,400 for the year. His new regular rate is: ($23.05 x 2867.5 hrs. + $3,400) /2867.5 hrs. = $24.23. His regular rate increased from $23.05 to $24.23 (by $1.18 an hour) because of the bonus, and he is additionally entitled to half of that hourly increase for each overtime hour. Thus, he would be due ($1.18/2 x 787.5 hours) = $464.63 more for overtime for the year.

Note that as an alternative to retroactive calculation of overtime due on a bonus, FLSA allows an employer to pay the bonus as a percentage [of] total earnings – straight time and overtime earning for the bonus period. See 29 C.F.F., § 778.210 in the way the bonus is simultaneous payment of overtime due on the bonus. So, for example, an employer may decide in 2005 that it is paying an annual bonus of 5%

for 2004. The employer calculates the bonus by multiplying a non-exempt employee's total earnings, including overtime premium, paid in 2004 by 5%.

In a recently released opinion letter, DOL stated that a percentage-of-total earnings bonus paid early in the current year for the previous calendar year constitutes earnings for the calendar year for which it was paid (i.e., the previous year). The bonus would not need to be considered as earnings for the current year when the employer calculates a percentage of earnings bonus for the next year. See FLSA 2005-22, 8/26/05.

4. Compensability of Training Time

Employers continue to have trouble determining when training time is compensable. Time spent by employees attending training is compensable unless all of the following criteria are met:

- Attendance occurs outside the employee's regular working hours;
- Attendance is voluntary (i.e., it is not voluntary if required by the employer or the employee is led to believe that non-attendance will adversely affect his working conditions or employment standing);
- The employee does no productive work while attending; and
- The program [training] is not directly related to the employee's job (i.e., it is considered related if it aids him/her in better handling his/her present job, but not where it prepares him/her for advancement or another job.) See 24 C.F.R. § 785.27-.29.[2]

Generally, time spent voluntarily taking a correspondence or home study course, or attending an independent institution of learning (e.g., high school, college, etc.) outside of work hours, is not compensable. See 29 C.F.R. § 785.30; W&H Op. Letter 207 (11/29/63). If a course or program corresponds to one offered by an independent institution of learning, an employer's establishing the course/program and paying for it do not make attendance compensable. See 29 C.F.R. § 785.31. The Wage and Hour Administration opined that training for licensed vocational nurses, although clearly job-related, was not compensable outside working hours because it corresponded to courses offered by an independent bona fide institution of learning. See 1999 WL 1788164 (Dept. of Labor, 9/30/99.)

Suppose, for example, an employer decided to offer an English literacy/fluency course to its non-exempt workforce, onsite but outside of work hours. No productive work would be performed. Participation would be voluntary, but increased fluency would benefit the employer's operation.

If the employer offers the English literacy/fluency classes outside employees' work hours, and the course follows a syllabus and uses materials which would be standard for such a course at an educational institution, the training time will not need to be counted as hours worked provided the employer is able to

[2] These rules also apply to attendance at meetings and lectures.

establish that participation or non-participation is voluntary – i.e., has or had no affect on present working conditions or the employment status of employees.

Note that DOL rendered at least one opinion letter concluding that attendance at remedial courses such as reading, English, writing and math offered during off hours to manufacturing employees did not appear to be in fact voluntary. W&H Op. Letter (10/18/94). However, the opinion did not provide facts regarding the voluntariness factor.

5. Technology and Recordkeeping

With increasing frequency, employers are using electronic systems to monitor and track employees' work. Global positioning systems (GPS) technology is being used to monitor workers' activities in and outside the workplace, with tracking devices being placed in computers, cell phones and vehicles. In the telecommunications, healthcare, catalog sales and similar industries, all center computer systems needed to accomplish work are also being used to record and calculate time worked.

Employers' failure to ensure electronic systems are properly capturing work time has resulted in significant financial liability under the FLSA. In July, 2005, DOL announced a $1 million settlement with Humana, Inc. resolving allegations that workers were shortchanged for time spent waiting for computer equipment to power on, logging onto the network, and brining up programs necessary for their work. Cingular Wireless agreed earlier in 2005 to pay $5.1 million, and in late 2003 T-Mobile USA agreed to pay $4.8 million, in each case to settle similar allegations. See 134 DLR A-1, July 14, 2005.

As before the use of technology had become prevalent, employers remain subject to specific recordkeeping requirements under FLSA. See 29 U.S.C. § 211(c); 29 C.F.R. Part 516. With respect to non-exempt employees, employers particularly should ensure that accurate and complete records of each employee's work hours and compensation are maintained, since good records can be critical to the outcome of a DOL wage and hour audit—or an FLSA lawsuit alleging underpayment of the minimum wage or overtime compensation. The reliability and accuracy of an employer's records correlates closely with the legal concept of burden of proof (i.e., necessity or duty of affirmatively proving a fact(s) in dispute) in an FLSA case.

The U.S. Supreme Court explained the burden of proof in an FLSA case in *Anderson v. Mt. Clemens Pottery Co.,* 328 U.S. 680 (1946). In such a case, the employee who brings suit has the burden of proving that he performed work for which he was not properly paid. In *Anderson*, the court noted that the remedial nature of FLSA and public policy remediate against making the burden an impossible hurdle for the employee. Due regard must be given to the fact that the law requires the employer to keep proper records of hours, wages, other conditions, and practices of employment, and that the employer is in the best position to know and produce the most probative facts concerning work performed. The court also stated that if an employee produces sufficient evidence to show the amount and extent of work as a matter of reasonable inference, the burden shifts to the employer to provide evidence of the precise amount of work performed or evidence negative to the reasonableness of the inference from the employee's evidence.

An employee's proof need be nothing more than credible sworn testimony. *Arias v. U.S. Service Industries, Inc.,* 80 F.3d 509 (D.C. Cir. 1996). And, if an employer fails to meet its recordkeeping

responsibilities, courts will not penalize an employee by denying recovery on the ground that the employee is unable to provide the precise amount or extent of alleged uncompensated work. Rather, the burden then becomes the employer's to disprove conclusions that can be made from whatever evidence the employees does produce.

The burden-shifting described by the Supreme Court in *Anderson* will occur only if the employer has failed to create or preserve accurate or complete records in accordance with the FLSA. If the employer has kept such records, but the employee fails for whatever reason to make use of those records in presenting his or her case, the employee may be held not to have met his or her burden of proof. *Myers v. The Copper Cellar Corp*., 192 F.3d 546 (6th Cir. 1999).

In cases where they are using technology that tracks when and how much employees are working, employers are advised to ensure that records of hours works used to compensate employees are in sync with computer data. Employers should also make certain that to the extent they are using computer technology to capture hours worked, their computer procedures are not failing to capture all time worked.

In its recent investigations and related lawsuits involving call centers, DOL officials reported finding that computer systems and procedures were geared such that more than de minimis work time was not being captured at the beginning or end of the shift, or was being spent before or after the shift began. The time not captured was typically required to be spent by the employee in principal activities integral to same.

Examples included:

- Employees in call centers had to perform preparatory activities (boot up, review daily instructions, read email, open multiple programs) before they started dealing with ("being on cue for") customers. At the end of the day, an employee might take a call from a customer two minutes before the end of a shift, spend ten minutes talking to the person and another fifteen minutes shutting down and completing some related paperwork. The preparatory activity time and time at the end of the day beyond the end of the shift were compensable, but were often not being captured by employers for pay purposes.

- In one call center case, the employer did not assign employees seats, and had a sort of general admission/first come-first serve seating policy for workers. This caused employees to show up and start work early, and to spend time every day getting their generic work station prepared for use, and more than de minimis work time was not being captured and paid.

- Employers were incenting their managers to ignore preparatory/extra time being spent (as required by the employers' procedures) by rewarding the managers for keeping overtime at a minimum and for increasing the number of calls handled and "productive time" spent with customers. While keeping costs down and increasing productivity were reasonable goals, they could not be achieved by failing to accurately capture time worked by employees.