Legal Update Article

Fifth Circuit Creates Circuit Split on FLSA's 'Regular Rate' Burden, Addresses Inclusion of Bonuses

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Wage and Hour

With specific, limited exceptions set forth in Section 207(e) of its regulations, the Fair Labor Standards Act (FLSA) requires that all compensation provided to a non-exempt employee must be included when determining the employee's "regular rate" for overtime pay purposes. But whose burden is it to demonstrate that one of these limited exceptions does, or does not, apply? A panel of U.S. Court of Appeals for the Fifth Circuit has concluded that burden falls on the employee. *Edwards v. 4JLJ, L.L.C.*, 2020 U.S. App. LEXIS 28053 (5th Cir. Sept. 2, 2020). In so holding, the Fifth Circuit has diverged from other circuit courts of appeal addressing the issue, thereby creating a circuit split.

The Fifth Circuit has jurisdiction over Louisiana, Mississippi, and Texas.

Background

The FLSA generally requires employers to pay non-exempt employees overtime pay at one-and-one-half times their "regular rate" for all hours worked over 40 in each workweek. The regular rate is defined, with few exceptions, as all "remuneration for employment paid to, or on behalf of, the employee," divided by the total number of hours worked during that week. The eight general types of exceptions to regular rate inclusion are set forth in Section 207(e) of the FLSA regulations and include, in part, such forms of compensation as "sums paid as gifts," "payments made for occasional periods when no work is performed due to vacation, holiday, illness, failure of the employer to provide sufficient work, or other similar cause," and

> sums paid in recognition of services performed during a given period [*i.e.* bonuses] if [] both the fact that payment is to be made and the amount of the payment are determined at the sole discretion of the employer at or near the end of the period and not pursuant to any prior contract, agreement, or promise causing the employee to expect such payments regularly[.]

29 U.S.C. § 207(e).

For decades, it has been undisputed that the burden of demonstrating that an individual or position is exempt from the minimum wage or overtime provisions of the FLSA falls on the employer. *See, e.g. Idaho Sheet Metal Works, Inc. v. Wirtz*, 383 U.S. 190, 209 (1966) (noting that "the burden of proof respecting exemptions is upon the company"). For example, the employer has the burden of demonstrating that an employee falls under the FLSA's executive, administrative, or professional exemption to minimum wage and overtime, as set forth in Section 213(a)(1) of the Act.

Making no distinction between the FLSA's minimum wage and overtime exemptions and the exceptions to regular rate inclusion found in Section 207(e), some circuit courts have placed the burden on employers to prove that some form of compensation paid to

employees falls under one of the enumerated exceptions. *See, e.g. Smiley v. E.I. DuPont de Nemours & Co.*, 839 F.3d 325 (3d Cir. 2016) ("We have recognized that there are several exceptions to the otherwise all-inclusive rule set forth in section 207(e), but the statutory exclusions are narrowly construed, and the employer bears the burden of establishing [that] an exemption [applies]."); *accord Newman v. Advanced Tech. Innovation Corp.*, 749 F.3d 33, 36 (1st Cir. 2014);*Acton v. City of Columbia*, 436 F.3d 969, 976 (8th Cir. 2006); *Lee v. Vance Exec. Prot. Inc.*, 7 Fed. Appx. 160 (4th Cir. 2001);*Local 246 Util. Workers Union v. Southern Cal. Edison Co.*, 83 F.3d 292 (9th Cir. 1996) (reversing judgment for employer and finding that it "failed to demonstrate that supplemental payments may be excluded from the regular rate of compensation").

The Fifth Circuit's Decision

a. The Burden of Proof on Regular Rate Inclusion

But the *exemptions* found in Section 213 and the *exceptions* to regular rate inclusion set forth in Section 207(e) are *not* the same, the Fifth Circuit explains. While it is true the employer has the burden to show that an employee is exempt from an FLSA requirement, "plaintiffs bear the burden to prove all elements of their claims." Thus, "because [Section] 207(e)(3) is merely a definitional element of the regular rate – and therefore merely a definitional element of the Employees' claim – it was their burden to show that bonuses were not discretionary according to the statute's terms." *Edwards*, 2020 U.S. App. LEXIS 28053, at *16-17.

b. The Bonuses at Issue

Having resolved that employees bear the burden of proving whether particular payments must be included in the regular rate of pay, the Court of Appeals then addressed the specific bonuses at issue in the case. The defendant provides oil well pump and fracking services. The plaintiff employees filed suit alleging that two of the bonuses offered by the employer – a "stage" bonus and a performance bonus – were improperly excluded from the regular rate calculation. The jury found that the employer was not required to include either bonus in the regular rate of pay. The Fifth Circuit affirmed that finding as to the stage bonus but reversed it as to the performance bonus.

Because the fracking of a well occurs in identifiable "stages," the company offered a bonus for each stage completed. However, the details of the timing and amount of the stage bonuses were never put into writing and the Court of Appeals therefore concluded that the plaintiffs failed to provide sufficient evidence the bonus was non-discretionary under the factors set forth in Section 207(e)(3). Thus, the jury properly had determined that the stage bonus did not have to be included in the regular rate calculation.

The company also offered a performance bonus, which*was* formalized and provided to employees in a written policy at the time of hire. Although the policy clearly indicated the bonus was "not to be expected, it is to be earned" and that if an employee was "here just to get a paycheck, and get by with as little work as possible, don't expect to get a performance bonus," the policy also set forth both specific criteria by which employees would be judged with respect to bonus consideration and a pay scale, of anywhere from 50 cents to $1.00 per hour depending on employee class, for such occasions when a bonus was deemed to have been earned.

The Court of Appeals held that the plaintiffs had in fact sufficiently demonstrated that the

performance bonuses should have been included in the regular rate calculation because, while the jury reasonably could (and did) conclude that the employer retained discretion as to whether the bonus would be paid (*i.e.* after evaluating the quarterly performance criteria), the employer did *not* retain discretion as to *how much* any such bonus would be. On the contrary, the policy provided for a specific, hourly bonus based on employee class. Thus, the exception requirements of Section 207(e)(3) were not met and the Court of Appeals reversed in favor of the employees.

The Takeaway

Whether the circuit split created by the Fifth Circuit's decision as it relates to the burden of proof will be resolved by the Supreme Court remains to be seen. Regardless, employers need to assess all forms of compensation provided to non-exempt employees and determine whether they should be included in or excluded from the regular rate of pay. With respect to bonuses, employers also should review any communications with employees describing the conditions necessary to earn the bonuses and how they will be calculated to ensure that if a bonus is intended to be at the employer's discretion, those communications do not inadvertently eliminate that discretionary nature.

If you have any questions about this decision, the regular rate calculation, or any other wage and hour issue, please consult the Jackson Lewis attorney(s) with whom you regularly work.