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DOL Places Further Limits on Employers' Use of the Fluctuating Workweek Method of Payment

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The fluctuating workweek method of payment has the potential to save employers money. It allows an employer, under certain circumstances, to pay a non-exempt employee a fixed salary for an agreed-upon number of hours, and half-time for hours worked over 40 in a workweek. However, on April 5, 2011, the U.S. Department of Labor (DOL) published a final rule, which took effect on May 5, 2011, that it claims has the effect of establishing that employers cannot pay bonuses and non-overtime premiums (*e.g.*, attendance or safety bonuses, shift differentials for working undesirable hours, etc.) to employees being compensated under the fluctuating workweek method of payment. Nevertheless, the DOL made no substantive changes to the regulation at issue, and its position is merely stated in the preamble to the final rule. Moreover, the DOL based this position, at least in part, on its own interpretation of Supreme Court precedent, which is not necessarily binding on courts.

The Fluctuating Workweek Method

The fluctuating workweek method allows an employer to pay "a salaried employee whose hours of work fluctuate from week to week … a fixed amount as straight-time pay for whatever hours he is called upon to work in a workweek, whether few or many … ." *Condo v. Sysco Corp.*, 1 F.3d 599, 601 (7th Cir. 1993); 29 C.F.R. § 778.114(a). Under this method, the employee's "regular rate" for overtime purposes will vary each week as it is determined by dividing the actual number of hours worked during the workweek into the fixed salary amount. This calculation produces a straight-time hourly rate, which is then multiplied by 50% to produce the overtime rate that must be paid for every hour worked beyond 40 during that workweek. Under the fluctuating workweek method, half-time payments for hours worked over 40 "satisfies the overtime pay requirement [of the FLSA] because such hours have already been compensated at the straight time regular rate, under the salary arrangement." 29 C.F.R.
§ 778.114(a). In other words, the fixed sum paid to an employee on the fluctuating workweek method represents the employee's entire straight-time pay for the week, no matter how many hours the employee worked.

Employer Options

For obvious reasons, an employer may not simply opt to pay an employee on the fluctuating workweek method — and consequently at the lower overtime rate. The regulation requires that four conditions be met before the fluctuating workweek method can apply:

- The employee's hours must fluctuate from week to week;
- The employee must receive a fixed salary that does not vary with the number of hours worked during the week (excluding overtime premiums);

- The fixed amount must be sufficient to provide compensation every week at a regular rate that is at least equal to the minimum wage; and
- The employer and employee must share a "clear mutual understanding" that the employer will pay that fixed salary regardless of the number of hours worked.

29 C.F.R. § 778.114(a), (c).

Because the employee's hours must actually fluctuate from week to week in order to take advantage of the fluctuating workweek method of payment, this arrangement is often used by employers in the restaurant, hospitality and retail industries. For example, an employee who works banquets or catered events for which there is generally no fixed schedule would be an ideal candidate for the fluctuating workweek method of payment.

In the Courts

A number of federal courts have held that the payment of certain types of additional compensation to employees paid under the fluctuating workweek method violated 778.114 on the grounds that, when these additional payments were taken into account, the employee was not being paid "a fixed salary that does not vary with the number of hours worked during the week." *See, e.g., O'Brien v. Town of Agawam*, 350 F.3d 279 (1st Cir. 2003) (shift differential payments and extra non-statutory "overtime" payments result in inability to use FWW); *Ayers v. SGS Control Servs., Inc.*, 2007 WL 646326 (S.D.N.Y. Feb. 27, 2007) (additional payments for shifts spent working offshore or on employee's scheduled day off precluded application of FWW); *Dooley v. Liberty Mut. Ins. Co.*, 369 F.Supp.2d 81 (D. Mass. 2005) (premium rate for Saturday work when less than 40 hours worked precluded application of FWW).

In 2008, in the wake of these cases, the DOL proposed to modify the regulatory language of § 778.114 to provide that "bona fide bonus or premium payments do not invalidate the fluctuating workweek method of compensation." *See* 73 Fed. Reg. 43,662 (July 28, 2008). In issuing this proposed rule, the DOL stated that "[p]aying employees bonus or premium payments for certain activities … is a common and beneficial practice," and the proposed rule was intended to support this practice. *Id*. The DOL also stated that this "proposed clarification" was "consistent with the Supreme Court's decision in *Overnight Motor Transportation Co. v. Missel*, 316 U.S. 572 (1942), in which the Supreme Court established the legality under the federal law of the fluctuating workweek method of payment.

Update

Almost three years later, in April 2011, after having considered the comments received during the notice and comment period from those both for and against the proposed rule, the DOL did an about-face and decided not to make the proposed change to the regulation. Instead, the DOL stated that allowing employers to pay bonuses and non-overtime premiums to employees paid on the fluctuating workweek method would invalidate the arrangement. Although the DOL still acknowledged that "the payment of bonus and premium payments can be beneficial for employees in many other contexts," it nonetheless stated in the preamble to the final rule that its rationale for deciding against revising the regulation as set forth in the proposed rule was that "the basis for allowing the half-time overtime premium computation under the fluctuating workweek method is the mutual understanding between the employer and the employee regarding payment of a fixed amount as straight time pay for whatever hours are worked each workweek, regardless of their number" and the payment of bonuses and non-overtime premiums would be

"inconsistent" with this requirement. 76 Fed. Reg. 18850 (April 5, 2011). Contrary to its assertion in 2008, DOL stated in the preamble to the final rule that it "now believes" that the proposed rule would have been inconsistent with the Supreme Court's decision in *Missel*. *Id*.

Thus, the DOL's stated position is that the fluctuating workweek pay method is invalid for employees who receive bonuses and other non-overtime premium payments. However, this final rule has yet to be upheld by any courts at the time of this writing. Indeed, at least one court has held that the DOL's April 2011 pronouncement did not affect its decision that providing a discretionary bonus to employees did not invalidate the use of the fluctuating workweek method of payment. *See Smith v. Frac Tech Services, LLC*, No. 4:09CV00679, 2011 U.S. Dist. LEXIS 64079 (D.Ark. June 15, 2011). The court noted that it had based its decision on its own interpretation of the Supreme Court's decision in *Missel* and that it was not bound by the DOL's interpretation of Supreme Court cases. *Id*. at *7.

Nonetheless, employers need to be aware of the DOL's position and tread carefully when considering paying additional compensation to employees working on a fluctuating workweek. If a court were to determine that the fluctuating workweek method of payment for an employee had been cancelled by the payment of a bonus or non-overtime premium payment, the court could require that the employer pay the employee(s) at issue for all hours worked over 40 during the applicable limitations period at a rate of time and one half. Thus, instead of saving money through the use of the fluctuating workweek method of payment, an employer could end up paying dearly.

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