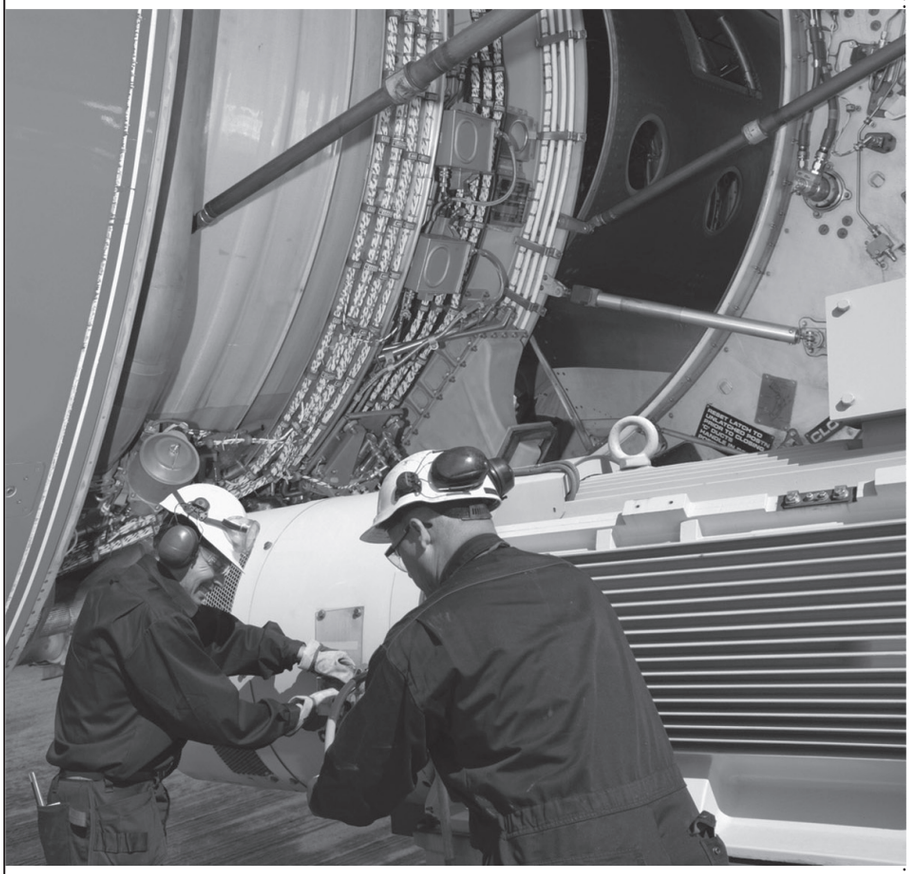
FLSA Myth Busters: Premium Pay Does Not Waive Exempt Status

by Robert Fugate



Does an employer waive the exempt status of its professional employees by providing them with "premium pay" for additional work? Many people believe the answer to this question is "yes." However, federal courts across the nation have unequivocally rejected the myth that premium pay waives exempt status under the Fair Labor Standards Act ("FLSA"). Yet the myth survives.

This myth tends to be stated as follows: "Monetary recognition premised upon hours worked may violate the salary basis for employees exempt from overtime." Because this myth has been uniformly rejected, employers are free to reward exempt employees with premium pay. Unlike non-exempt employees, who must be paid time-and-a-half for working more than forty hours per week, exempt employees are not entitled to any particular premium. Instead, premium pay rates for exempt employees can be set by the employer. This article provides a summary of the controlling authorities.

Throughout the article, "premium pay" means additional compensation paid to an exempt employee when he or she works more than forty hours per week. In the case of firefighters and other employees who do not work a forty hour week, "premium pay" refers to additional monies paid for working hours above and beyond normally scheduled hours. Likewise, the term "standard week" means the normal, expected work week for a given employee.

A short background on the FLSA will set the stage for analysis. The FLSA was enacted in 1938 "to compensate those who labored in excess of the statutory maximum number of hours for the wear and tear of extra work."[1] The FLSA "requires employers to pay their employees time-and-a-half for work performed in excess of forty hours per week."[2] However, the FLSA exempts "bona fide executive, administrative, or professional" employees from the overtime pay requirements.[3] In sum, the FLSA "requires employers to pay time-and-a-half overtime compensation to all employees who work more than 40 hours a week – except executive, administrative, and professional employees."[4] Employers bear the burden of proving that the exemption applies.[5]

In *Garcia v. San Antonio Metropolitan Transit Authority*, the Supreme Court held that the FLSA applies to state employers and their political subdivisions.[6] Thus, state and local government employers are obligated to pay their non-exempt employees overtime at the same rates as private employers.[7] But the focus of this article is on exempt employees. With this brief background, we turn to the substantive issue: Whether premium pay waives the exempt status of professional employees.

Eighth Circuit – *Fife v. Harmon*

In *Fife v. Harmon*, municipal employees claimed the City of St. Louis violated the FLSA by failing to pay them at time-and-a-half rates for hours worked in excess of forty per week.[8] The employees worked as Airfield Operation Specialists ("AOS") at the Lambert-St. Louis International Airport.[9] They served as the "eyes and ears of senior management."[10] When an AOS employee worked more than forty hours per week, he or she was given a choice of either being paid overtime at their regular rate or "banking" an hour of paid vacation for each extra hour worked.[11] St. Louis contended the employees were exempt and, therefore, not entitled to time-and-a-half rates.[12]

The Eighth Circuit began by considering whether the employees were paid on a salary basis.[13] The FLSA requires that employees working in exempt categories must be paid on a salary basis in order to be treated as exempt.[14] "An employee is paid 'on a salary basis' if he or she receives a predetermined amount of compensation each pay period that is not subject to being *reduced* because of

the quality or quantity of the work."[15] However, the district court had found that the AOS employees were not paid on a salary basis because "when they worked more than forty hours in a week, they were paid overtime at an hourly rate, a form of compensation that is 'inherently inconsistent' with being salaried."[16] The Eighth Circuit rejected the district court's analysis as "an error of law."[17]

After noting that the Secretary of Labor had broad authority to define the three categories of exempt employees, the Eighth Circuit said: "The Secretary 'has unequivocally and consistently declared that additional compensation in the form of hourly overtime payment does not defeat exempt status under the salary-basis test.'"[18] "Because the salary-basis test is a creature of the Secretary's own regulations, his interpretation of it is . . . controlling unless plainly erroneous or inconsistent with the regulation."[19] In this case, the district court fostered the myth that salaried employees could not receive premium pay.[20] The Eighth Circuit set the record straight.[21]

Ninth Circuit – *Boykin v. Boeing Co.*

In *Boykin v. Boeing Company*, a group of engineers alleged that Boeing violated the FLSA by failing to pay them overtime at a rate of time-and-a-half.[22] The engineers were compensated according to a collective bargaining agreement ("CBA").[23] Under the CBA, the engineers had a "standard workweek" of forty hours.[24] Boeing could require the engineers to work "spot overtime" necessitated by unanticipated demands; Boeing did not have to compensate the engineers unless the overtime exceeded an additional eight hours per week.[25] If the overtime did exceed an additional eight hours per week, Boeing paid a "premium rate" equal to "straight time" plus $6.50 per hour.[26] Boeing also paid the premium rate for anticipated or planned periods of overtime for large projects or short-term fluctuations in the production cycle.[27]

In addition to the engineers, the proposed class of plaintiffs included management, professional, and administrative employees.[28] Managers received overtime compensation for all hours in excess of a standard forty hour work week at either the premium rate or time-and-a-half.[29] Professional and administrative employees received the premium rate for overtime.[30]

After the parties filed cross-motions,, the district court granted summary judgment in favor of Boeing.[31] On appeal, the employees asserted that the FLSA required Boeing to pay them time-and-a-half for any hours they worked over forty hours per week.[32] The principal issue on appeal was whether the class of Boeing employees received compensation on a salary basis.[33]

The DOL has unequivocally and consistently declared that additional compensation in the form of hourly overtime payment does not defeat exempt status under the salary-basis test.

The employees contended that they were not paid on a salary basis because "in addition to their fixed salary, Boeing [paid] them for their overtime work."[34] The Ninth Circuit rejected this contention, saying:

> The employees' argument, however, disregards the DOL's interpretation of its own regulation. The DOL has unequivocally and consistently declared that additional compensation in the form of hourly overtime payment does not defeat exempt status under the salary-basis test.[35]

The Court then quoted the relevant regulation saying, "additional compensation besides the salary is not inconsistent with the salary basis of payment."[36] The Court also quoted the district court, saying: "it is difficult to perceive the alleged injury to a salaried employee who receives some form of hourly overtime compensation without fear of having compensation docked on some basis."[37] Rather, "the focus of the regulations is to prohibit employers from claiming that their employees are compensated on a salary basis when the employees are subject to *deductions* in pay."[38] Accordingly, the Ninth Circuit concluded, "Boeing did not violate the FLSA by failing to pay the employees time and one-half for overtime work."[39]

Fifth Circuit – *York v. City of Wichita Falls*

In *York v. City of Wichita Falls*, the parties disputed – among other things – whether premium pay for fire captains and battalion chiefs waived their status as exempt employees.[40] The City introduced evidence that the captains and chiefs were salaried.[41] But the firefighters argued that captains and chiefs were paid on the same hourly basis as other employees.[42]

The evidence showed that the captains and chiefs were paid overtime when called to duty outside of their regular schedules.[43] Further, sick leave and vacation time were deducted in one-hour increments.[44] The evidence also showed that if a captain or chief took an hour off of work, his compensation remained the same and the time was deducted from sick leave or vacation time on an hourly basis.[45] But the "relevant regulations provide that such deductions do not establish that a person is paid on a wage basis."[46] With regard to premium payments, the Fifth Circuit explained, "Paying an hourly rate for each hour worked beyond the regular schedule does not defeat the executive exemption."[47]

Sixth Circuit – *Acs v. Detroit Edison Co.*

An employee group at Detroit Edison argued they satisfied the legal definition of hourly employees and, therefore, were en-

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Robert Fugate is a Senior Assistant City Attorney in Arlington, Texas. His practice is devoted to civil litigation, including civil rights, land use, personal injury, and a mishmash of other matters. He is board certified in civil appellate law, graduated magna cum laude from the University of Houston Law Center, and has an undergraduate degree in civil engineering.

titled to time-and-a-half overtime compensation.[48] The Sixth Circuit started its analysis by noting that Detroit Edison paid all of its 8,500 employees – whether classified as salaried (exempt) or hourly (non-exempt) – under a single payroll system.[49]

Under this system, all employees "from the CEO on down" were required to report the hours that they worked each week.[50]

The salaried employees received a notice each year advising them of their annual salary and exempt status.[51] The notices also explained that weekly salaries were calculated by dividing annual salaries by fifty-two and rounding to the nearest dollar.[52] To receive their full annual salary, exempt employees were required to report at least forty hours each week.[53] However, Detroit Edison's pay policy also stated that "an exempt employee's pay may not be reduced because of an absence of less than one full day."[54]

Detroit Edison had several business reasons for tracking employee work on an hourly basis.[55] First, many of its salaried employees received straight time "hourly payments for hours worked over 40 in a workweek."[56] An hourly system also allowed Detroit Edison to "record accrual and use of the various kinds of leave time (such as, vacation, sick and personal)."[57] Last, the State of Michigan required public utilities, like Detroit Edison, to provide data on specific types of labor costs for rule-making purposes.[58]

Although Detroit Edison employees generally worked forty hour work weeks, the company's pay policy recognized that "alternative work schedules may be uniquely designed to meet an organization's needs."[59] The employee-plaintiffs worked a "variety of daily shifts" of eight, ten, or twelve hours, or a mixed combination of hours.[60] For example, an employee assigned to a twelve hour shift could work thirty-six hours one week and forty-eight hours the following week.[61] To ensure that its twelve hour shift employees received their full salary, Detroit Edison instructed them to report forty hours per week even when they only worked thirty-six hours.[62]

Employees occasionally forgot to report the "free" hours.[63] However, Detroit Edison had implemented safeguards to prevent under payment.[64] In addition to instructing employees not to under-report, Detroit Edison had a computerized time-entry program that generated a pop-up screen warning if reported fewer than forty hours.[65] The employee paychecks also listed the hours worked each week, providing employees a means to verify that they were properly paid.[66] Detroit Edison also provided forms to correct pay shortages when errors occurred.[67]

"[A]dditional compensation besides the salary is not inconsistent with the salary basis of payment. What matters is that deductions may not be made for time when work is not available if the employee is ready, willing, and able to work."

Based on these facts, the district court concluded that the employees were guaranteed a "predetermined amount" and that the occasional shortfalls from employee time-entry errors did not amount to prohibited dockings."[68] The Sixth Circuit affirmed.[69]

In addressing the premium pay issue, the Sixth Circuit explained that Detroit Edison did not *reduce* employees' salaries even if they worked less than forty hours per week.[70] "That Detroit Edison chooses to pay what it terms 'straight-time' overtime compensation – in other words, additional compensation at the exempt employee's 'hourly' rate for hours worked beyond 40 in a work week – does not violate the salary-basis test."[71] The Sixth Circuit relied, in part, on the relevant regulation which acknowledged that "additional compensation besides the salary is not inconsistent with the salary basis of payment."[72] "What matters is that deductions may not be made for time when work is not available if the employee is ready, willing, and able to work."[73]

Eastern District of Virginia – *Hartman v. Arlington County*

In *Hartman v. Arlington County*, fire shift commanders sought "overtime compensation" for hours worked over the statutory maximum.[74] The shift commanders were paid on a salary basis with paychecks issued every two weeks without regard to the number of hours actually worked.[75] No deductions were made from the commanders' pay except those permitted under the regulations.[76] The commanders argued that they were "not salaried because they receive additional pay at an hourly rate for each hour worked beyond their regular schedule."[77] The Court rejected the argument because the practice is "expressly permitted" and does not defeat the executive exemption."[78]

Western District of Texas – *Anunobi v. Eckerd Corp.*

In *Anunobi v. Eckerd Corp.*, a pharmacist was paid "additional monies" as "premium pay" when he worked more hours than forty hours per week.[79] The pharmacist argued that he was not paid on a salary basis and, further, that he "did not perform professional duties as that term is defined under the FLSA regulations."[80] Eckerd countered "that Plaintiff, as a salaried pharmacist, was exempt as a professional under the FLSA."[81] Unsurprisingly, the district court rejected plaintiff's contention that his work – as a registered pharmacist – did not qualify for exempt status.[82]

Turning to the "premium pay" issue, the court noted that the premium pay rate was set on an hourly basis as the pharmacist's base rate (weekly salary divided by forty) plus five additional dollars.[83] The district court held that the "voluntary payment by an employer of 'overtime' or additional compensation does not change the status of an employee from exempt to hourly."[84] Further, the pharmacist was a salaried worker "because he received a predetermined amount for his regularly scheduled hours on a weekly basis."[85] The predetermined amount was not reduced if the pharmacist was late to work or

left early.[86] The fact that the payroll data referenced forty hours of work did not alter the fact that the pharmacist always received a predetermined amount of compensation.[87] The court concluded: "The employer's premium pay plan does not negate Plaintiff's salary status."[88]

As an aside, Eckerd also had a policy of allowing pharmacist to "cash-in" vacation time for a lump sum payment in lieu of taking vacation.[89] Like voluntary premium pay, the cash-for-vacation policy did not affect the FLSA salary test.[90]

Opinion Letter from the Department of Labor

As noted in the *Fife* case, the Department of Labor clearly rejected the myth that exempt employees cannot be paid premium pay.[91] In a 1997 opinion letter, the Acting Administrator responded to a concern that premium pay would waive a salaried employee's exempt status, explaining:

> With respect to your questions on the proper interpretation of the requirements for exemption from the FLSA as a "professional" employee, we do not interpret our regulations to require time-and-a-half compensation for hours worked over 40 in a week by *bona fide*, salaried professional employees who are otherwise exempt, merely because the employer provides additional compensation for the additional hours. The Department has consistently held that, standing alone, extra hourly compensation for working more than 40 hours in a week does not defeat an otherwise applicable FLSA exemption for a professional employee, provided the employee meets all of the regulatory tests relating to duties, responsibilities, and compensation including the requirement for payment of a *bona fide* guaranteed salary as defined in the Department's regulations on "salary basis" of pay in 29 CFR § 541.118.[92]

Thus, it is clear that the Department of Labor has rejected the myth that premium pay waives exempt status.

Conclusion

In each of the cases, the plaintiff-employees fostered the myth that premium pay waives exempt status. The employees generally argued that the premium pay they received for work beyond a standard week showed that they were not salaried employees. In essence, these employees were "looking a gift horse in the mouth." Because the employees were exempt, they were not *entitled* to premium pay at time-and-a-half rates or otherwise under the FLSA.

It is equally true that the FLSA does not prevent employers from paying premium to exempt employees. Employers maintain the flexibility to provide exempt employees with premium pay for "going the extra mile." Premium pay for exempt employees could be: (1) a set stipend, (2) compensatory time, or (3) additional pay at "straight time," "time and-a-half," or any other rate. Employers who choose to reward exempt employees are not prohibited from doing so by the FLSA. In short, premium pay remains a tool that is available to municipal and other employers for motivating and rewarding exempt employees.

Notes

1. Acs v. Detroit Edison Co., 444 F.3d 763, 764 (6th Cir. 2006) (quoting Bay Ridge Operating Co. v. Aaron, 334 U.S. 446, 460, 68 S.Ct. 1186, 92 L.Ed. 1502 (1948)).
2. *Id.* at 764-765 (quoting Schaefer v. Ind. Mich. Power Co., 358 F.3d 394, 399 (6th Cir. 2004)).
3. *Id.* (quoting Auer v. Robbins, 519 U.S. 452, 454, 117 S.Ct. 905, 137 L.Ed.2d 79 (1997) (quoting 29 U.S.C. § 213(a)(1))).
4. *Id.* at 767 (citing 29 U.S.C. § 213(a)(1)).
5. *Id.* at 767.
6. Garcia v. San Antonio Metro. Transit Auth., 469 U.S. 528, 554-557, 105 S.Ct. 1005, 83 L.Ed.2d 1016 (1985); *see also* York v. City of Wichita Falls, 944 F.2d 236, 237 (5th Cir. 1991).
7. *Id.*
8. Fife v. Harmon, 171 F.3d 1173, 1174 (8th Cir. 1999).
9. *Id.*
10. *Id.*
11. *Id.*
12. *Id.*
13. *Id.* at 1175.
14. *Id.*
15. *Id.* (*emphasis added*).
16. *Id.*
17. *Id.*
18. *Id.* (quoting Boykin v. Boeing Co., 128 F.3d 1279, 1281 (9th Cir. 1997); *see also* D.O.L. Wage & Hour Division Opinion Letter, 1997 WL 998013 (March 17, 1997)).
19. *Id.* (quoting Auer v. Robbins, 519 U.S. 452, 461, 117 S.Ct. 905, 911, 137 L.Ed.2d 79 (1997)).
20. *See id.* at 1175.
21. *See id.*
22. Boykin v. Boeing Co., 128 F.3d 1279, 1280 (9th Cir. 1997).
23. *Id.*
24. *Id.*
25. *Id.*
26. *Id.*
27. *Id.*
28. *Id.*
29. *Id.*
30. *Id.*
31. *Id.*
32. *Id.* at 1281.
33. *Id.*
34. *Id.*
35. *Id.*
36. *Id.* at 1282.
37. *Id.*
38. *Id.*
39. *Id.*
40. York v. City of Wichita Falls, 944 F.2d 236, 241-242 (5th Cir. 1991).
41. *Id.* at 242.
42. *Id.*
43. *Id.*
44. *Id.*
45. *Id.*
46. *Id.* (citing 29 C.F.R. § 541.118(b)).
47. *Id.*
48. Acs v. Detroit Edison Co., 444 F.3d 763, 765 (6th Cir. 2006).
49. *Id.*
50. *Id.*
51. *Id.*
52. *Id.*
53. *Id.*
54. *Id.* at 765-766.
55. *Id.* at 766.
56. *Id.* at 766-768.
57. *Id.* at 766.
58. *Id.*
59. *Id.*
60. *Id.*
61. *Id.*
62. *Id.*

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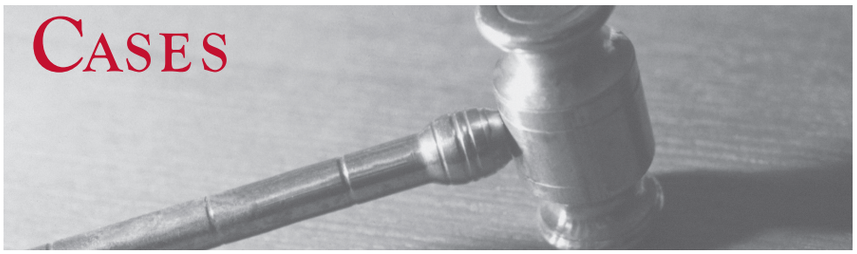
Cases



by Erich R. Eiselt, Assistant General Counsel

First Amendment: City Hall "Holiday Display" is Protected Governmental Speech

The Freedom From Religion Foundation requested that the City of Warren, Michigan remove a nativity scene from the City's annual winter holiday display in the atrium of its civic center. The City refused, leaving the nativity scene among the other secular and religious symbols in the display—a lighted tree, a snowman, a nutcracker, a "Welcome Winter" sign and so on.

In 2011, the Foundation changed its stance. It requested the right to place "an attractive sandwich board" in the middle of the holiday display, bearing the following message:

At this season of
THE WINTER SOLSTICE
may reason prevail.
There are no gods, no devils, no angels, no Heaven or hell.
There is only our natural world,
Religion is but myth and superstition
That hardens hearts
And enslaves minds.

Placed by the Freedom From Religion Foundation
On Behalf of its State Members
frff.org

State/Church
KEEP THEM SEPARATE
Freedom From Religion Foundation
frff.org

The City's Mayor declined, responding in a lengthy letter. He pointed out that the proposed sign "is antagonistic to all religions and would serve no purpose during this holiday season except to provoke controversy and hostility..." He added "Everyone has a right to believe or not believe...but no organization has the right to disparage the beliefs of Warren and U.S. citizens. . . ."

The Foundation sued, alleging that allowing a nativity scene while rejecting the Foundation's sign violated the Establishment, Free Speech and Equal Protection clauses. The district court granted summary judgment for the defendants, finding that as a matter of law, hosting the holiday display and refusing the Foundation's sign did not violate the Constitution.

On appeal, the Sixth Circuit affirmed: the City did not violate the Establishment Clause by including a nativity scene in a holiday display or by refusing to allow the anti-religion sign.

The First Amendment prohibits any law "respecting the establishment of religion." There are two general safe harbors to this rule. First, a government may allow a benefit to faith-based entities so long as the same benefit is available to secular entities. Second, a government may invoke the divine through words and symbols if they have religious *and* historical meanings or faith-based *and* solemnizing effects, and offer at most incidental benefits to a faith.

These tests have produced a clear answer in the holiday display context, beginning with *Lynch v. Donnelly*, 465 U.S. 668 (1984). There the Court found that a Pawtucket, Rhode Island winter display which included a crèche and many other secular items including a clown, teddy bear and Santa Claus House was permissible. In the context of all the components of the display, the crèche was not an endorsement of religion but merely "depicts the historical origins of this event long recognized as a National Holiday." Five years after *Lynch*, the Court again applied the test, this time to uphold a combined religious and secular mix of symbols in one public area while prohibiting a stand-alone nativity scene in another public space. (*Cnty of Allegheny v. American Civil Liberties Union*, 492 U.S. 573 (1989).

The Sixth Circuit relied on *Lynch* and *Allegheny*. It also cited a long-standing Supreme Court maxim, more than sixty years old, to defend the language in the Mayor's letter, which the Foundation alleged was an implicit promotion of religion, "We are a religious people, whose institutions presuppose a Supreme Being." *Zorach v. Clauson*, 346 U.S. 306, 313 (1952).

The Circuit Court disagreed with the Foundation's Free Speech argument. "As the Foundation reads the First Amendment, it requires the City, having opted to create a holiday display, to include competing messages and viewpoints. As we read the First Amendment, it does not." The Sixth Circuit outlined the parameters of "governmental speech." The City, and every government in the nation, is free to promote its own messages, so long as they are not otherwise constitutionally flawed, without having to grant exposure to contrary views. "When the government speaks, 'it is entitled to say what it wishes and to 'favor or disfavor' all kinds of policies or points of view." (citations omitted).

The critical element is that "governmental speech" must truly be the expression of the government. In *Pleasant Grove City v. Summum*, 555 U.S. 460 (2009) the City had installed in a public park various monuments depicting the City's heritage. This included a Ten Commandments monument. Although many of the monuments had been privately-donated, the City had selected them and desired to convey the messages associated with them. It therefore did not need to allow a Gnostic Christian sect to include its own monument in the same park. And where a federal campaign promoting beef consumption was initiated by the Department of Agriculture, with every word of the promotion being approved by the Agriculture Secretary, there was no requirement to give equal time to opposing views merely because private industry representatives had participated in producing the ad. *Johanns v. Livestock Mktg. Ass'n*, 544 U.S. 550 (2005).

Here, the City had fully controlled the content of the holiday display. So long as it did not violate the Establishment Clause, the display was governmental speech, not requiring access by competing viewpoints. *Freedom From Religion Foundation, Inc. v. City of Warren*, No. 12-1858 (6th Cir. Feb. 25, 2013).