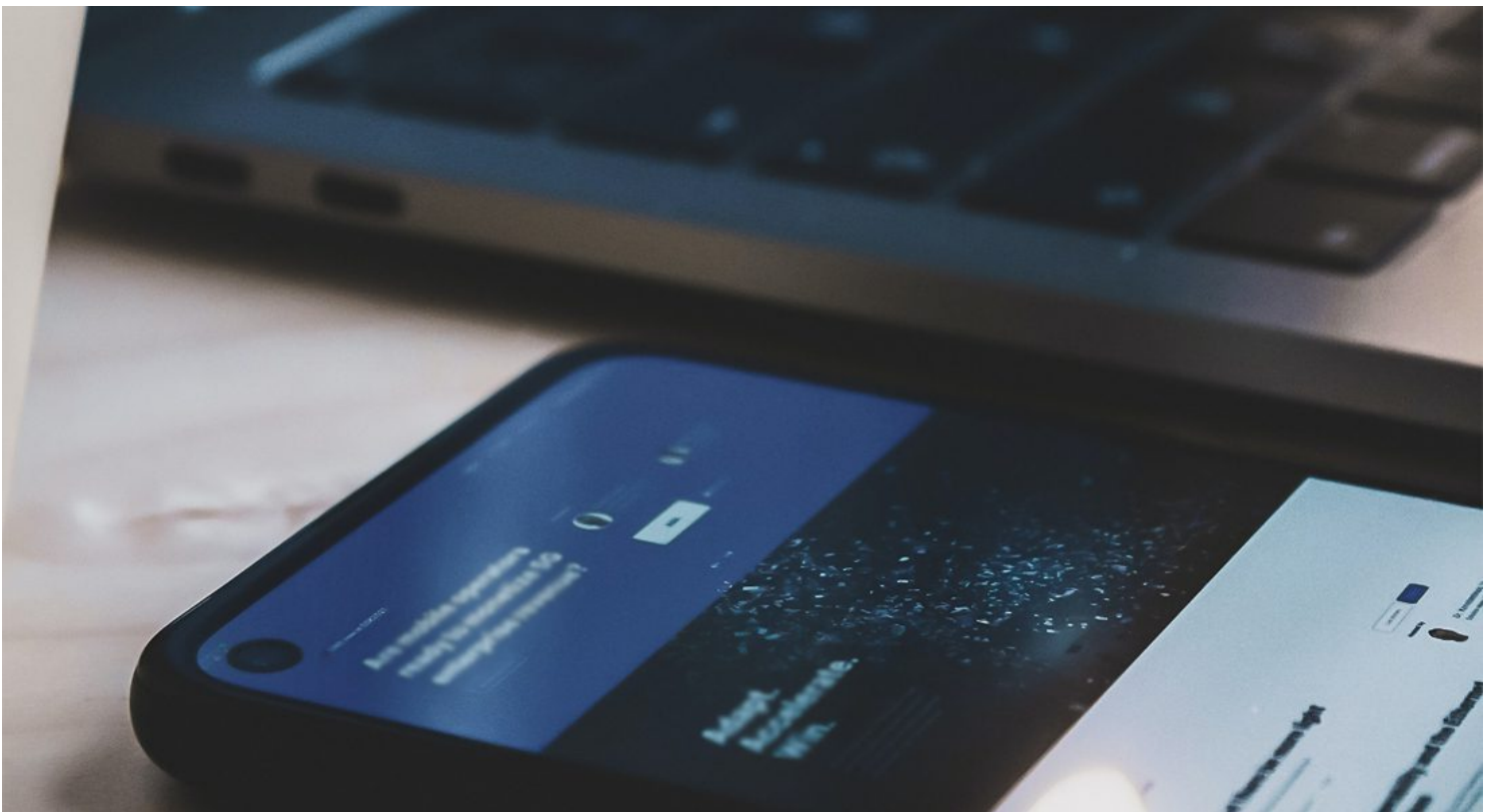


NEWS & INSIGHTS

Bonuses Paid by Third Parties May be Excluded from Employee Overtime Rates

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Appeals Court Ruling Clarifies That Calculation is Dependent on Employee-

Employer Agreement

The United States Court of Appeals for the Third Circuit recently held that payments an employee receives from third parties should be viewed differently than those received from an employer for purposes of determining overtime rates of pay under the Fair Labor Standards Act (FLSA). Employers should be mindful that when calculating the regular rate of pay, the understanding between the employer and employee is critical.

The Court of Appeals issued an August 20 decision in [Secretary, U.S. Department of Labor \(DOL\) v. Bristol Excavating, Inc.](#), et al. (DOL v. Bristol Excavating) that rejected the DOL's position that payments from third parties, such as incentive bonuses, are always considered remuneration for employment and subject to inclusion in the "regular rate of pay," regardless of the agreement or understanding between employer and employee.

DOL v. Bristol Excavating

In the case of DOL v. Bristol Excavating, a small excavating company entered into a master service agreement with Talisman, a large natural gas production company, to provide equipment, labor and other services at drilling sites in Pennsylvania. Talisman sponsored an employee bonus program, including for contract employees, to incentivize safety, efficiency and completion of work. Bristol Excavating undertook the clerical work necessary for its employees to receive bonuses. However, Bristol Excavating did not include the Talisman bonuses in the regular rate of pay when calculating overtime compensation for its employees.

During a routine inspection, a DOL auditor determined that the Talisman-paid bonuses must be included in the calculation of Bristol Excavating employees' regular rate of pay. When Bristol Excavating refused to do so, the DOL filed an FLSA lawsuit. The trial court concluded that Bristol Excavating violated the FLSA.

The Court of Appeals reversed part of the trial court's conclusion. In doing so, it reasoned that the employer's and employees' understanding should be the focus of determining remuneration rather than a blanket assumption that all incentive bonuses are considered remuneration. It cautioned, however, that regular pay "cannot be funneled through third parties" to avoid additional overtime pay, and "employers are protected from being on the hook every time a third party chooses to add to an employee's income."

The agreement between employer and employee need not be explicit. Citing Clark Griswold's unmet expectations of a bonus in National Lampoon's Christmas Vacation, the Court of Appeals acknowledged that the parties' agreement "may be implied through an employer's significantly facilitating regular compensation that reaches the employee."

Takeaways for Employers

The Court of Appeals described several circumstances that bear on whether an implicit agreement exists, summarizing, "the question is whether there has been a course of dealing sufficient to characterize the payment as one that is legitimately expected by the employees and legitimately understood as being sponsored in a meaningful way by the employer." Accordingly, with respect to the bonus payments at issue in DOL v. Bristol Excavating:

- Where the facts showed that employees knew the requirements and amount of bonus, and the employer engaged in substantial facilitation of the bonus program, the court found bonus payments qualified as remuneration; but
- where the facts did not demonstrate that the employees understood the bonus or had expectations of receiving it, and moreover the third party had control and discretion to change or cancel the bonus program, the court found bonus payments may not be considered remuneration.

Employers must therefore remain vigilant about overtime calculations, even where third party bonuses are concerned. Employers who participate in third-party bonus programs for their employees may need to include bonus payments in overtime calculations, depending upon the bonus structure.

The Court of Appeals did acknowledge the need for predictability for employers, stating, “it does damage to the employment relationship to force employers to include promised bonuses from third parties as remuneration in the regular rate of pay, unless and until the evidence demonstrates that those bonuses have become part of the pay calculation agreed to in some fashion by the employer and employee.” More broadly, the court observed, “imposing unexpected costs on employers does not work to the long-term benefit of employees.”

Saxton & Stump’s attorneys are available to discuss how your organization may be impacted by this recent interpretation of the FLSA. Saxton & Stump’s [Labor and Employment Law Group](#) can review your company’s wage calculation practices to ensure compliance with the FLSA, Pennsylvania Minimum Wage Act, and Pennsylvania Wage Payment and Collection Law.

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