



May 11, 2006

FLSA2006-8NA

Dear **Name***:

This is in response to your request for an opinion regarding whether your client's incentive pay plan satisfies the overtime requirements of the Fair Labor Standards Act (FLSA). From our discussion below, you will see that your plan satisfies the overtime requirements of the FLSA.

You state that your client, in an effort to reward productive employees, is implementing a bonus program based on production incentives set forth in the Incentive Pay Plan (Plan). The Plan is designed to provide nonexempt employees with incentives to maximize their productivity. Your client expects that the Plan will allow it to attract, retain, motivate, and reward employees who achieve production beyond that considered standard for positions covered by the Plan. Your description of the Plan indicates that the calculation of production-based incentive pay is related to the accomplishment of specific projects rather than the measurement of each employee's activity. Each employee is paid an hourly wage on a weekly basis, including any overtime earned during that workweek. You ask us to assume that the incentive pay is a nondiscretionary bonus for FLSA purposes.

The employer assigns an incentive bonus to each project. Each eligible employee working on the project is credited with a share of the incentive bonus upon completion of the project. At the conclusion of the monthly incentive pay period, total hourly wages paid to an employee are compared to the incentive bonuses earned on completed projects on which the employee worked. If the total incentive bonus amount is equal to or less than the hourly wages paid to the employee, then no incentive bonus is paid for the incentive pay period. If the total incentive bonuses exceed the hourly wages paid during the incentive pay period, the balance of the bonus is paid to the employee.

In the event an employee works overtime during an incentive pay period in which an incentive bonus is paid, overtime wages due are recalculated at the end of the incentive pay period to account for the incentive bonus paid. The employer totals the hourly wages earned, the overtime premium paid on any hours worked over 40 during any workweek, and any incentive bonus paid during the incentive pay period. This total is then divided by the total hours worked during that incentive pay period. One-half of the resultant average hourly rate is paid for each overtime hour worked.

You offered the following example to illustrate this payment system. This calculation assumes the employee is paid an \$8.00 hourly wage, worked five overtime hours during each week of the four-week incentive pay period, and was paid a \$68.00 incentive bonus.

$$\begin{aligned} & \$1,440 \text{ regular hourly pay} + \$80 \text{ OT premium pay} + \$68 \text{ incentive bonus} = \$1,588 \\ & \$1,588 \text{ divided by } 180 \text{ total hours worked} = \$8.82 \text{ regular rate} \\ & \$8.82 \times 0.5 \text{ halftime due for hours over forty per week} = \$4.41 \\ & \$4.41 \times 20 \text{ overtime hours} = \$88.20 \text{ additional overtime due} \\ & \text{Total wages paid to employee: } \$1,588 + \$88.20 = \$1,676.20 \end{aligned}$$

It would appear that the employer is unable to allocate the incentive bonus among the workweeks of the monthly incentive pay period in proportion to the amount of the incentive bonus actually earned each week. Therefore, "it may be reasonable and equitable to assume that the employee earned an equal amount of bonus each hour of the pay period and the resultant hourly increase may be determined by dividing the total bonus by the number of hours worked by the employee during the period for which it is paid. The additional compensation due for the overtime workweeks in the period may then be computed by multiplying the total number of statutory overtime hours worked in each such workweek during the period by one-half of this hourly increase." 29 C.F.R. § 778.209(b) (copy enclosed). In the example set out above, the employer would be in compliance with the FLSA if it divided the \$68 production bonus earned during the monthly incentive pay period by the 180 total hours worked during the pay period. This would result in an increase in the hourly rate of 38 cents for each hour worked. Pursuant to the regulations, the additional overtime premium due for the number of overtime hours worked is computed by multiplying the number of overtime



hours worked times one-half of the hourly rate increase, or $20 \times \$19 = \3.80 (less than the additional overtime computed using the methodology in your example). Thus, the FLSA requires, at a minimum, the payment of the additional overtime premium of \$3.80 on the bonus paid for the incentive pay period.

The FLSA requires inclusion in the regular rate of pay of all bonuses not otherwise excluded by section 7(e) of the FLSA, 29 U.S.C. § 207(e) (copy enclosed). The employer considers the incentive payment plan a nondiscretionary bonus and includes it in the calculation of the regular rate for purposes of calculating any overtime owed. *See* 29 C.F.R. § 778.208 (copy enclosed). After reviewing the information provided, the payment plan described appears to comply with the FLSA overtime requirements. It should be noted that the employer, by including the overtime premium payments already paid on the hourly wages in calculating the overtime premium owed on the bonus, is paying more than is required by the FLSA.

This opinion is based exclusively on the facts and circumstances described in your request and is given based on your representation, express or implied, that you have provided a full and fair description of all the facts and circumstances that would be pertinent to our consideration of the question presented. Existence of any other factual or historical background not contained in your letter might require a conclusion different from the one expressed herein. You have represented that this opinion is not sought by a party to pending private litigation concerning the issues addressed herein. You have also represented that this opinion is not sought in connection with an investigation or litigation between a client or firm and the Wage and Hour Division or the Department of Labor.

We trust that this letter is responsive to your inquiry.

Sincerely,

Barbara R. Relerford
Fair Labor Standards Team
Office of Enforcement Policy

Enclosures:

FLSA section 7(e)
29 C.F.R. §§ 778.208-.209

Note: * The actual name(s) was removed to preserve privacy in accordance with 5 U.S.C. § 552(b)(7)