

COMMISSION SYSTEM EXEMPT FROM FLSA OVERTIME LAWS

A recent decision was just issued that highlights the importance of paying very close attention to commission pay structures. If you are an employee, you want to make sure you are being compensated fairly and according to the federal and state labor laws. If you are an employer, you want to be certain that you are in strict compliance with the laws in order to retain qualified and quality professionals. The court below weighed in on whether NutriSystem Inc. had a legally sound commission-based pay scheme in place, or whether it had been violating the federal labor laws.

The Third Circuit U.S. Court of Appeals, in *Parker v. NutriSystem Inc.*, held that NutriSystem's compensation plan based on commissions is exempt from the Fair Labor Standards Act (FLSA).

Under the FLSA, generally speaking, a non-exempt employee who works greater than 40 hours per week is entitled to overtime pay, which is time and a half of the employee's standard hourly wage. Certain states impose further restrictions on employers, but this discussion will be limited to the federal law. There are certain recognized exemptions from the overtime pay requirements, such as the "retail commission exception", which is at issue in NutriSystem.

The United States Department of Labor's (DOL) view is that the amount of compensation paid to an employee must be "proportionally related" to the amount charged to the customer. In NutriSystem, the plaintiffs argued that because the employees at NutriSystem's call center are paid a "flat rate" for each order, regardless of the size of the order, their pay is comparable to the "piecework" wages paid to many factory workers. U.S. District Court Chief Judge Harvey Bartle III rejected this view, noting that the NutriSystem sales associates better compared to many other workers paid by commission because their wages depend on the whims of customers. Bartle went on to explain, "NutriSystem's payments to its sales associates are sufficiently proportional to the cost of the products it sells to qualify as commissions".

Two amicus briefs in support of the plaintiffs were filed in this case; one from the Department of Labor and the other from a coalition of workers' rights groups including the National Employment Lawyers Association (NELA), Friends of Farmworkers and the Southern Poverty Law Center. Labor Department attorney Laura Moskowitz argued in the brief that "the Section 7(i) retail or service establishment exemption for employees paid on a commission basis does not apply to flat-fee payments that bear no relationship to the cost of the goods sold." Moskowitz argued that NutriSystem's commission payment plan for paying its call center workers doesn't qualify as a true commission, because the flat fees they are paid for each sale are unrelated to the dollar value of the sale.

The Third Circuit U.S. Court of Appeals found this argument unpersuasive, stating, "we decline to adopt a test that requires a commission, under Section 7(i), to be strictly based on a percentage of the end cost to the consumer," U.S. Circuit Judge D. Michael Fisher wrote in an opinion joined by Judge D. Brooks Smith. In his dissent, Senior U.S. Circuit Judge Robert E. Cowen wrote that the Labor Department's opinion letters "express the department's consistent and reasonable position that Section 7(i) requires a proportional relationship between employee compensation and customer costs. While neither the plaintiffs nor the [Labor] Department suggests that a commission must be based on a strict percentage of

the end cost to the consumer, the flat-rate payments in this case do not correspond at all with the end cost to the consumer," Cowen wrote.

On appeal, writing for the majority, Judge Fisher began by noting that the FLSA does not include a statutory definition of "commission." "Because we cannot unlock the meaning of 'commission' based on the plain language in this context, we consider legislative history and statutory purpose," Fisher wrote.

Although the agency has maintained its position that to qualify as a commission for purposes of Section 7(i) of the FLSA, the payment must be "linked to the cost of the product sold or services provided to the customer," Judge Fisher was not persuaded, writing that "although the [Labor] Department may have more 'specialized experience' than we do in the day-to-day administration of the FLSA, we do not find that the opinion letters at issue here provide sufficiently thorough reasoning, consistency, or factual similarities to the instant case to warrant deference." Judge Fisher concluded, based on the purposes behind the FLSA, that the commission compensation scheme "does not offend" the law and its overtime provisions.

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