



SAINTS BOUNTY SCANDAL A WAKE-UP CALL FOR EMPLOYERS TO EXAMINE THEIR OWN PERFORMANCE BONUSES

Most employers may not yet get the connection, but the shocking penalties just levied by the NFL on the New Orleans Saints for operating a “bounty system” that rewarded Saints players for “knock-out” and “cart-off” hits on opposing players are a wake-up call to examine your own bonus programs to make sure you don’t experience your own fall from grace. Unlike the Saints’ “bounty system,” there’s nothing sinister about the typical workplace performance bonus program, unless you’re using it to reward employees for sabotaging your competition, but there are still plenty of potential pitfalls for you to navigate to stay within the law and out of hot water.

Impact on Overtime

At the top of the list of potential bonus-related land mines is the federal wage and hour law, the Fair Labor Standards Act (“FLSA”). You know the FLSA requires you to pay nonexempt employees for overtime, or hours worked in excess of forty in a 7-day work week. You also know that overtime pay is one and one-half times, or 150%, of an employee’s base rate. But did you know that performance bonuses and other incentive compensation must be included in an employee’s base rate when computing overtime compensation? That’s right. An employee’s base rate includes his regular hourly rate and all other performance-based compensation other than overtime or other premium pay of at least 150%. So if you pay nonexempt employees a bonus based on monthly, quarterly, or annual performance, and the employees worked overtime during the period covered by the bonus, the FLSA requires you to refigure their base rates and resulting overtime compensation and pay them the difference between what they actually were paid for overtime without including the bonus in the base rate and what they would have been paid if the bonus had been included. The same holds true for attendance, referral, safety (but see discussion below), and other types of performance or incentive bonuses.

Here’s a simple example of how it works: Let’s take an employee who makes \$10.00 an hour, and let’s say he gets an extra \$100 a week if he or the company achieves certain production goals. And let’s say he works 50 hours in a week in which he also receives the \$100 production bonus. In that case, his base rate for overtime purposes is \$600 [(50 hours x \$10.00/hour) + \$100.00 bonus] ÷ 50 hours = \$12.00/hour. So his overtime rate becomes 150% of \$12.00/hour instead of 150% of \$10.00/hour.

Of course refiguring an employee’s base rate and adjusting his overtime pay becomes more problematic when performance bonuses are paid on a less frequent basis, such as quarterly or annually, as is more often the case. But employers who fail to make the required adjustments leave themselves exposed to liability for unpaid overtime wages, civil money penalties, and liquidated damages (a form of punitive damages equal to the amount of unpaid overtime). And when performance bonuses are paid across the board to large groups of eligible employees, the failure to include bonus payments in the overtime calculus can lead to serious class-wide liability.



One bonus method used by some employers to avoid the headaches of having to refigure the base rate for overtime purposes is paying bonuses based on a percentage of total compensation, including overtime compensation. A performance bonus based on a percentage of total compensation satisfies the FLSA overtime requirement because it automatically adjusts both an employee's base rate and overtime compensation by the same percentage increase.

Bonuses that are purely discretionary and gratuitous, such as Christmas or holiday bonuses that are not contingent or based on employee or company performance, are not included in an employee's base rate and, therefore, do not have to be counted when calculating overtime pay. But if you are paying any kind of performance-based incentives or bonuses, you must include such compensation in the overtime calculus to avoid running afoul of the FLSA.

Some Types of Safety Bonuses Frowned on by OSHA

Safety bonuses are another potential bonus trouble spot for employers. The Occupational Safety and Health ("OSH") Act prohibits employers from discriminating or retaliating against employees for reporting injuries or illnesses. The Occupational Safety and Health Administration ("OSHA"), which administers the OSH Act, takes the position that any employer policy or practice that discourages workers from reporting injuries or illnesses, even if unintentional, is a form of prohibited discrimination and/or retaliation.

Examples of such policies and practices cited by OSHA as potentially unlawful are employer-sponsored programs in which all employees who incur no injuries over a set period of time receive a "safety bonus" or perhaps are entered in a drawing for a "safety prize." Other examples are programs under which teams of employees might be awarded bonuses or prizes if none of the team members incurs a work-related injury over a set period of time. According to OSHA, while such programs may be well-intentioned to encourage safe practices, they also may have the result of discouraging employees from reporting injuries since reporting an injury may disqualify an employee or entire team of employees from receiving a prize or bonus. In examining such policies and practices, OSHA will look to whether the incentive or bonus offered under the program is of such magnitude that the failure to receive it might dissuade reasonable workers from reporting injuries. If so, the policy or practice will be considered discriminatory or retaliatory by OSHA.

OSHA also takes a dim view of management and supervisory bonuses that are linked to lower reported injury rates, which the Agency believes increase the potential for unlawful discrimination and retaliation against workers who report injuries. Employers who are not recording reportable injuries as a result of such programs, or other bonus programs that discourage employees from reporting injuries, also could be cited for record-keeping violations. On the other hand, OSHA encourages employer-provided incentives that promote employee participation in safety-related activities, reward employees for reporting potential hazards, or otherwise encourage safe work practices.

The point for employers is that not all safety bonuses are considered unlawful by OSHA, but any bonus program that has the potential to dissuade reasonable employees from reporting injuries is inherently suspect and should be avoided if you want to stay in good graces with OSHA.



Partial or Pro-Rata Bonuses

Another potential bonus trap for employers is when your bonus policy isn't as clear as it should be about the criteria required for eligibility. For instance, when an employer's policy or practice is to pay an annual bonus, usually at the end of the year, based on profits, but without being specific about when profits are determined or whether an employee must be employed at the time profits are determined to be eligible, many courts have ruled that employees who leave before the end of the year are entitled to partial or pro-rata shares of the bonuses they would have received had they remained employed through the end of the year. And if you fail to pay a partial or pro-rata bonus under such circumstances, many states tack on extra penalties. For example, in Louisiana, employers who fail to pay departing employees all amounts due under the terms of their employment also can be liable for penalty wages of up to 90 days of pay. Thus, if it's your intent to pay annual bonuses only to employees who actually are employed at the end of the year when the bonuses are determined and paid, you need to be sure your bonus policy is clear and specific and leaves no room for any unintended consequences.

Bottom Line

Bonuses and other incentive compensation that reward employees for their contributions and for helping achieve your performance and productivity goals are a great way to boost morale and build employee loyalty. At the same time, if not done by the book then, like the Saints, you could be flagged for a flagrant foul.

—[H. Mark Adams](#)



Remember that these legal principles may change and vary widely in their application to specific factual circumstances. You should consult with counsel about your individual circumstances. For further information regarding these issues, contact:

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