

FLSA-1301

March 28, 1995

This is in response to your request pursuant to the regulations at 29 CFR Part 549, seeking approval of a proposed profit-sharing plan covering certain employees employed by your client, ***. Attached to your letter, you include what appears to be an outline of your client's proposed profit-sharing plan. Our review of the plan outline raises several concerns about potentially disqualifying provisions that should be clarified.

The plan outline provides that all employees employed in *** U.S. Operations are eligible to participate in the plan except for those individuals who are covered under a collective bargaining agreement or who participate in a management incentive plan. The outline also provides that depending upon the target profit level attained, eligible employees may receive up to 3% of their base salary.

Section 7(e)(3)(b) of the Fair Labor Standards Act permits exclusion from the regular rate of pay, upon which overtime compensation is calculated, sums paid to employees pursuant to a bona fide profit-sharing plan or trust meeting the requirements of the Department's regulations at 29 CFR Part 549. Section 549.1(d)(1) of the regulations provides that eligibility must extend to all employees subject to the minimum wage and overtime provisions of the FLSA. However, participation in an employer's profit-sharing plan may be limited to particular classifications of employees if specific approval is obtained from the Administrator. This approval may be granted to exclude certain employees from the profit-sharing plan after such employees, including their representatives, have been given notice and an opportunity to present their views on the issue. See 29 CFR §549.1(d)(2).

To assist you in meeting these requirements for approval, a draft notice to affected employees is enclosed together with a copy of the regulations. Once a finalized profit-sharing plan is completed, your client should prepare sufficient copies thereof and post them together with copies of the profit-sharing plan. The notices should be posted for not less than 15 workdays. At the conclusion of the posting period, *** should attest that these requirements have been met by providing a listing of the places and dates of posting including notification given to bargaining representatives, and submit such attestation to this office.

We are also concerned that the "target" feature of the plan, without further explanation, may run afoul of 29 CFR § 549.2(b) of the regulations. This section provides that a plan is not a bona fide profit-sharing plan "[i]f the amount to be paid periodically by the employer into the fund ... to be distributed to the employees is a fixed sum." It appears that under your client's plan, distributions to eligible employees will be made based on the attainment of specific percentage of the profit amount targeted. In theory the company could designate an arbitrary "target" amount which bears little or no relation to profits, and pay a predetermined percentage to employees. There is nothing in the plan outline which explains the method that the company uses to reach its determinations of the

allocation amount, i.e., how the profit pool is determined. Stated another way, the company has complete discretion with regard to the amount of money that it allocates as its profit target amount. It may or may not be a fixed sum. Nevertheless, without more information, we cannot conclude that this section or provision of the plan does not implicitly contain the disqualifying provision set forth in 29 CFR §549.2(b).

Additionally, we are concerned that the "Payment Determination" section of your client's proposed plan may be disqualified by 29 CFR §549.2(d) of the regulations. This regulation provides that a plan will not be deemed to meet the requirements of a bona fide profit-sharing plan "[if] any individual employee's share ... is set at a predetermined fixed sum or is so limited as to provide in effect for the payment of a fixed sum." The plan outline calls for a percentage of the employee's base salary to be paid out as the employee's share of the profits. For example, under the plan, if 100% of the target amount is attained, the employee will receive 2% of his base salary. Arguably, this payment could be viewed as a predetermined rate or fixed sum prohibited by the regulation.

Finally, we note that there is not provision in the plan outline for distributions to employees who may separate or are terminated from their employment. Pursuant to 29 CFR § 549.1(g) of the regulations all profit-sharing plans must provide for the right of an employee to receive his or her share of distributed profits which must not be based on the employee's continued employment with the employer after the period for which the determination of profits has been made.

The concerns raised herein should be addressed before your client's profit-sharing plan is made final. We trust that the foregoing is responsive to your request.

Sincerely,

Maria Echaveste
Administrator