

## Ninth Circuit Rules That Cash-In-Lieu Of Benefits Payments Must Be Included In Regular Rate Of Pay

In *Flores v. City of San Gabriel*, 2016 WL 3090782 (9<sup>th</sup> Cir. June 2, 2016), the Ninth Circuit ruled in a case of first impression that the employer (a California city) improperly excluded cash payments made to employees in lieu of health benefits from their regular rate of pay under the Fair Labor Standards Act (FLSA). This ruling will affect employers that provide a cash benefit to employees who waive the employer's health coverage. The payment of unused benefits must be included in the regular rate of pay for purposes of calculating overtime compensation.

### Facts

The City provided to its employees a Flexible Benefits Plan (a cafeteria plan under Section 125 of the Internal Revenue Code) and made contributions for each employee for the purchase of medical, vision, dental and other benefits, such as disability insurance. Employees were required to purchase the City's dental and vision coverage using the City's contributions, but could waive the City's health coverage if they provided proof of other coverage.

Employees who waived the City's health coverage, and those whose coverage elections cost less than the amount of the City's contribution, received a taxable cash payment of the excess amount each month. The City designated its cash-in-lieu of benefits payments as "benefits" that were excluded from its calculation of the employees' regular rate of pay for purposes of overtime compensation.

### Cash-In-Lieu Of Benefits Payments Were Improperly Excluded From The Regular Rate Of Pay

The City argued that its cash-in-lieu of benefits payments were subject to Section 207(e)(2) of the FLSA, which excludes from the regular rate of pay such items as vacation pay, reimbursable travel expenses and "other similar payments to an employee which are not made as compensation for his hours of employment." The City argued that the payments qualified for the exception because payments to employees of unused benefits were not tied to hours worked by employees and hence were not compensation for hours worked.

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The Ninth Circuit disagreed. Relying on Department of Labor regulations, the Court held that a payment may not be excluded from the regular rate of pay if it is “generally understood as compensation for work, even though the payment is not directly tied to specific hours worked by an employee.” (Slip Op. pp. 12-13.) The Ninth Circuit explained that the question is whether the payment is a form of compensation for performing work; not whether a particular payment is tied to an hourly wage.

The Court also rejected the City’s contention that its cash-in-lieu of benefits payments could be excluded under Section 207(e)(4), which excludes from the regular rate of pay “contributions irrevocably made by an employer to a trustee or third person pursuant to a bona fide plan” for providing health insurance and similar benefits. But, because the City paid the unused benefits directly to its employees and not to a third party or trustee, the Ninth Circuit held that the cash-in-lieu of benefits payments could not be excluded under Section 207(e)(4).

The Ninth Circuit further concluded that the City’s Flexible Benefits Plan was not a “bona fide plan” under Section 207(e)(4). The cash payments (which constituted 40 percent or more of the City’s total contributions paid directly to employees rather than received as benefits) could not be deemed an “incidental” part of the cafeteria plan. Because the City’s cafeteria plan was not a “bona fide” plan, the City’s payment of unused benefits must be included in the regular rate of pay for overtime purposes.

### **FLSA Violation Was Deemed "Willful," Even In The Absence Of Controlling Authority**

Significantly, the Ninth Circuit held there was no evidence demonstrating that the City – and its human resources department in particular – had taken any affirmative steps to determine that the cash-in-lieu of benefits payments were classified appropriately as a “benefit” under the FLSA for exclusion from the regular rate of pay. Without such a showing, the City failed to establish that it acted in good faith to comply with the FLSA.

Moreover, the Ninth Circuit deemed the City’s FLSA violation to be “willful.” The Court was not persuaded by the fact that there was no controlling case authority in this circuit regarding the proper treatment of cash-in-lieu of benefits payments. Rather, the Court stated that “the absence of controlling case authority cannot be dispositive when the City has put forth no evidence that it ever looked to see whether such authority existed.” (Slip. Op p. 29.) Because the City’s FLSA violation was deemed to be willful and without any showing of good faith compliance, the plaintiffs were entitled to an extended 3-year statute of limitations as well as liquidated damages.

### **Employer Take Away**

The calculation of employees’ regular rate of pay may be subject to more scrutiny as a result of *Flores*. Employers that provide cash payments to those who waive the employer’s health insurance coverage must include such payments in the employees’ regular rate of pay for overtime purposes. In addition, employers must act with caution with their human resources departments when making determinations to exclude any payments from the regular rate of pay.

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