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## Court OKs FTD Penalties for Failure to File Electronically

After a business paid its taxes on time and in the correct amount but did not deposit the tax payments electronically as required by IRS regulations, a U.S. District Court upheld the failure-to-deposit (FTD) penalties imposed by the IRS [*Fallu Productions, Inc. v. U.S.*, No. 1:06-cv-13248, 2008 U.S. Dist. LEXIS 10194 (SD N.Y., 2-13-08)].

### Background

Fallu Productions, Inc. is a film production company wholly owned by the actor Joe Pesci. For six quarters in 2001 and 2002, Fallu failed to make its federal employment tax deposits electronically using the Electronic Federal Tax Payment System (EFTPS), as required by 26 C.F.R. §31.6302-1(h). It did, however, pay those taxes in full and on time by depositing the funds at an approved bank. The IRS imposed FTD penalties for each of the relevant quarters, pursuant to 26 USC §6656, and subsequently filed a tax lien against Fallu for the penalties owed.

Fallu argued that the IRS action in these circumstances was unconstitutional – depriving it of due process of law. Further, the company said that imposing FTD penalties for a “deficiency in the form of payment” exceeded the plain meaning of the statute and was arbitrary and capricious.

### Scope of §6656

26 USC §6656(a) provides that, “In the case of any

failure by any person to deposit (*as required by this title or by regulations of the Secretary under this title*) on the date prescribed therefor any amount of tax imposed ... there shall be imposed upon such person a penalty ... (emphasis added).” 26 C.F.R. §31.6302-1(h) requires that certain tax deposits be made electronically. The court said this penalty provision applies to a taxpayer’s failure to deposit taxes electronically when required to do so by regulation.

**Statutory construction: plain meaning.** The court said that the parenthetical in the statute, placed immediately following “failure ... to deposit” emphasizes that the deposit itself must satisfy the requirements of the Code and applicable regulations. “Even narrowly construed, the statute authorizes FTD penalties for violating a regulatory requirement that deposits be made electronically, even if payment is made in full and on time by other means.”

**Overall statutory scheme.** This plain reading of §6656(a) also fits with the broader statutory scheme, explained the court. Section 6302(h) states that the Secretary of the Treasury “shall prescribe such regulations as may be necessary for the development and implementation of an electronic fund transfer system which is required to be used for the collection of depository taxes.” With its direction that the Treasury Department implement an electronic tax deposit system

## Payroll Solutions

**Q.** Occasionally, employees turn in ideas for improvements in products or procedures that help our company's profitability. Management would like to encourage this practice by paying cash awards to employees who share their money-saving ideas. If we set up such an employee suggestion award program, would the payments be part of nonexempt employees' regular rate of pay?

**A.** FLSA regulations (29 C.F.R. §778.333) provide that prizes paid under a bona fide suggestion program may be excluded from a nonexempt employee's regular rate of pay for overtime purposes if the program meets all of the following requirements:

- The amount of the prize has no relation to the earnings of the employee at his/her job, but rather is geared to the value to the company of the suggestion which is submitted;
- The prize represents a bona fide award for a suggestion which is the result of additional effort or ingenuity unrelated to, and outside the scope of, the usual and customary duties of any employee of the class eligible to participate and the prize is not used as a substitute for wages;
- No employee is required or specifically urged to participate in the program or led to believe that he or she will not merit promotion or advancement (or retain his or her existing job) unless suggestions are submitted;
- The invitation to submit suggestions is general in nature, and no specific assignment is outlined to employees (either as individuals or as a group) to work on or develop suggestions;
- There is no time limit on the submission of suggestions; and
- The employer has, prior to the submission of a suggestion by an employee, no notice or knowledge of the fact that the employee is working on the preparation of a suggestion under circumstances indicating that the company approved the task and the schedule of work undertaken by the employee.

and prescribe regulations to govern its operation, Congress expressed its intent that the system be used and made obligatory for certain depository taxes.

### Due process

The Due Process Clause of the Fifth Amendment to the Constitution provides that "no person shall ... be deprived of life, liberty, or property, without due process of law." This clause has been interpreted to include a substantive component guarding an individual against the exercise of power *without any reasonable justification in the service of a legitimate governmental objective*. Here, the court said that imposing FTD penalties when taxes are not deposited electronically as required does not violate taxpayers' due process rights.

The court noted that the government, in its case, described various efficiencies of EFTPS, including faster receipt of payments and reduced processing costs. Fallu, on the other hand, did not identify any difficulties the system poses over the bank depository system for taxpayers in its position.

Efficiency provides a "reasonable justification" for requiring that certain deposits be made using EFTPS, in service of the "legitimate IRS objective" of collecting taxes, concluded the court. Moreover, in light of the significant benefit to the government that comes from compliance with a more efficient collection system, the use of a penalty to enforce a method of deposit required by regulation (and authorized by statute) is neither arbitrary nor unreasonable. ■

## DHS, DOJ Increase Civil Fines Against Employers for Immigration Violations

The Department of Homeland Security (DHS) and the Department of Justice (DOJ) have jointly issued final regulations adjusting for inflation the civil money penalties assessed or enforced by one or the other department under 8 USC §§1324a, 1324b, and 1324c (Immigration and Nationality Act).

The adjustments are effective for violations occurring on or after March 27, 2008 [73 F.R. 10130, 2-26-08; <http://a257.g.akamaitech.net/7/257/2422/01jan20081800/edocket.access.gpo.gov/2008/pdf/E8-3320.pdf>].

### Adjustment calculations

The Federal Civil Penalties Inflation Adjustment Act of 1990 (Pub. L. No. 101-410) provides for the regular evaluation of civil money penalties. The amounts of the adjustments are determined according to a detailed formula specified in the Adjustment Act that incorporates a "cost-of-living adjustment" calculated with reference to the Consumer Price Index (CPI) and is subject to rounding under specified standards.

The penalties currently being imposed were last adjusted for inflation in 1999. The current inflation adjustment –

calculated with reference to the CPI for June 1999 and June 2007, as required – works out to 25.35%.

• **Hiring, recruiting, and referral/unlawful employment of aliens/unfair immigration-related employment practices, per person:**

- first order – current minimum penalty of \$275 is increased to \$375 and current maximum penalty of \$2,200 is increased to \$3,200;

- second order – current minimum penalty of \$2,200 is increased to \$3,200 and current maximum penalty of \$5,500 is increased to \$6,500;

- subsequent order – current minimum penalty of \$3,300 is increased to \$4,300 and current maximum penalty of \$11,000 is increased to \$16,000.

• **Violation relating to participating employer's failure to notify DHS of final nonconfirmation of employee's employment eligibility:**

- current minimum penalty of \$500 is increased to \$550 and current maximum penalty of \$1,000 is increased to \$1,100.

- **Document fraud (§1324c(a)(1)-(4)):**

- first order – current minimum penalty of \$275 is increased to \$375 and current maximum penalty of \$2,200 is increased to \$3,200;

- subsequent order – current minimum penalty of \$2,200 is increased to \$3,200 and current maximum penalty of \$5,500 is increased to \$6,500.

- **Document fraud (§1324c(a)(5)-(6)):**

- first order – current minimum penalty of \$250 is increased to \$275 and current maximum penalty of \$2,000 is increased to \$2,200;

- subsequent order – current minimum penalty of \$2,000 is increased to \$2,200 and current maximum penalty of \$5,000 is increased to \$5,500. ■

## TIGTA Report Finds Unfiled Forms 941 Not Identified

In a recently issued report, the Treasury Inspector General for Tax Administration (TIGTA) presents the results of a review of the IRS Return Delinquency Program, which identifies taxpayers that have not filed a tax return by the return due date [TIGTA Audit Rpt. 2008-30-027, 12-20-07; [www.treas.gov/tigta/auditreports/2008reports/200830027fr.pdf](http://www.treas.gov/tigta/auditreports/2008reports/200830027fr.pdf)].

*Note:* The Return Delinquency computer program identifies a return as delinquent when a filing requirement exists on a taxpayer's record that does not have the specified return posted. The IRS issues notices requesting such returns – more than 1.6 million were issued to business taxpayers in calendar year 2006.

### 'Serious weakness' in IRS computer program

TIGTA's review identified a "serious weakness" when the Return Delinquency computer program did not identify an unfiled Form 941 (*Employer's Quarterly Federal Tax Return*) when a Form 940 (*Employer's Annual Federal Unemployment (FUTA) Tax Return*) was filed.

The Return Delinquency computer program should identify taxpayers with a Form 941 or a Form 940 filing requirement and no return posted to the taxpayer's record for a specified tax period. However, the current computer program does not cross reference both forms to identify a related return that is due but not filed. As a result, "a significant amount of dollars" may not be collected on accounts where related Forms 941 were not filed.

The review sample of 150 cases from tax year 2005 included 20 Return Delinquency inquiries for Form 940. However, analysis of IRS records for 13 of these taxpayers showed that no related Form 941 was filed and no delinquency inquiry was ever generated for the delinquent quarterly forms. The analysis "not only identified a systemic weakness in the computer selection of Form 941 Return Delinquency cases but also a need for a change in the requirement for [IRS] employees to perform a full compliance check to ensure taxpayers file all required tax returns."

Three of the 13 taxpayers reported a combined total of

more than \$177,000 in taxable Form 940 wages. However, these taxpayers did not file the related delinquent Form 941 returns, and no Return Delinquency case was computer-generated for these taxpayers. Because the FUTA tax is imposed on only the first \$7,000 in wages paid to each employee during the calendar year, the potential amount of unreported wages paid and corresponding taxes reported on Forms 941 could significantly exceed the FUTA wages. As a result, "the liabilities on these missing Form 941 returns could be significant."

TIGTA analyzed IRS computer records to determine the potential universe of taxpayers that filed Forms 940 but did not file any quarterly Forms 941 for tax year 2005. The analysis identified 28,933 taxpayers that had not filed any Forms 941 during tax year 2005 but filed tax year 2005 Forms 940 reporting a combined total of more than \$3 billion in FUTA wages. Without knowing the total amount of wages paid and potential amounts withheld, TIGTA noted that the amount of Form 941 wages could far exceed the \$3 billion reported on the Forms 940 and that the related unpaid tax could be significant.

TIGTA's report concluded that IRS management's decision, effective September 2006, to no longer require tax examiners to perform full compliance checks contributed to the Forms 941 not being filed.

### IRS response

The IRS agreed to implement TIGTA's recommendation that managers ensure that random or targeted sample cases are appropriately selected for technical review and that technical case reviews are completed timely. IRS officials advised that changes to the Return Delinquency computer program will enable cross checking of Forms 940 and 941 beginning in April 2008. Finally, the IRS noted that procedures requiring full compliance checks of "in business" employers when a FUTA tax return has been filed were implemented in November 2007. ■

## Owner of Dallas Employee Leasing Company Sentenced to Prison, Ordered to Make Restitution for Over \$4 Million in Unpaid Payroll Taxes

The Department of Justice has announced that Bruce Alexander Brown, the former owner of an employee leasing business, Excell Personnel, Inc., has been sentenced to 36 months in prison and ordered to pay \$4,235,670.16 in restitution to the IRS. The court order covered payroll taxes owed and unpaid in all quarters of Excell's operation from 1996 through 2003 [DOJ Press Release, 1-15-08].

From 1996 to 2003, Brown was the owner and sole stockholder of Excell, which "leased" employees to companies that did not want to directly hire their workers. Excell would locate, hire, and train employees, and then provide them to the businesses that were its customers. The customers did not

directly pay the employees that Excell provided, but rather paid a fee to Excell that included the gross wages that would be owed to the employees for their labor, plus an administrative fee from which Excell received its profit and out of which it was obligated to pay indirect costs of the employees and overhead expenses. Excell, in turn, paid the employees their wages, making deductions for withholding of income and FICA taxes that were required to be paid to the IRS.

According to U.S. Attorney Richard B. Roper, Brown admitted that he was aware of his legal obligations, and that he knowingly and deliberately chose not to pay over to the IRS taxes owed for Excell's employees. ■

## Capitol Hill Update

The following are some recent payroll-related legislative developments. All information is current through March 1, 2008.

### Tax Technical Corrections Act of 2007: designated Roth contributions

The Tax Technical Corrections Act of 2007 (Pub. L. No. 110-172), enacted on December 29, 2007, includes a provision clarifying the treatment of elective deferrals for social security and Medicare (FICA) tax purposes.

Beginning in 2006, employees making elective deferrals under §401(k) plans or §403(b) annuities could designate some or all of those contributions as contributions to a Roth IRA – a plan where distributions are not usually taxed (see *The Payroll Source*®, p. 4-79). Under IRC §3121(v)(1)(A), elective deferrals are included in FICA wages at the time they are made. The Act clarifies that the same treatment applies to designated Roth contributions.

### Renewable Energy and Energy Conservation Tax Act: bicycle commuters

H.R. 5351 was passed by the House of Representatives (236-182) on February 27, 2008. It is now in the hands of the Senate Finance Committee.

The House version of the bill includes a provision adding a “qualified bicycle commuting reimbursement fringe benefit” as a qualified transportation fringe benefit under IRC §132, effective for taxable years beginning after December 31, 2008. This benefit is defined as any employer reimbursement of an employee for reasonable expenses incurred by the employee for the purchase and repair of a bicycle, bicycle improvements, and bicycle storage, provided that the bicycle is regularly used for travel between the employee’s residence and place of employment.

The maximum amount that could be excluded from

income for a calendar year is equal to \$20 x the number of the employee’s “qualified bicycle commuting months” for that year. A qualified month is any month for which the employee does not receive any other qualified transportation fringe benefit and during which the employee *regularly* uses a bicycle for a *substantial portion* of travel between his/her residence and place of employment.

### Cell phones as ‘listed property’

H.R. 5450, introduced in the House on February 14, 2008, would amend IRC §280F to remove cell phones from the items designated as “listed property.” The bill is now in the hands of the House Ways and Means Committee. *Note:* An identical bill, introduced in the Senate as S. 2668 on February 26, 2008, is now in the hands of the Senate Finance Committee.

Listed property includes items obtained for use in a business but lending themselves easily to personal use. A recent letter from the IRS Office of Chief Counsel discusses the tax treatment of cell phones (see **PAYROLL CURRENTLY, Issue No. 23, Vol. 15**), explaining that in order to ensure that an employee’s business use of an employer-provided cell phone is excludable from gross income, the employee must keep a record of each call and its business purpose.

### Foreign earned income exclusion

H.R. 4752, introduced in the House on December 17, 2007, would amend the IRC to eliminate the limitation on the foreign earned income exclusion. The bill is now in the hands of the House Ways and Means Committee.

### FUTA surtax

H.R. 5294, introduced in the House on February 2, 2008, would amend the IRC to repeal the 0.2% FUTA surtax with respect to “remuneration paid after December 31, 2007.” The bill is now in the hands of the House Ways and Means Committee. ■

## Employee Seeking Alcoholism Treatment Was Not Entitled to FMLA Leave

Krzysztof Chalimoniuk, an employee of Interstate Brands Corporation (IBC), had a history of alcoholism. After leaving work on July 28, 2000, he consumed a large quantity of alcohol. He was scheduled to work on July 31, August 2, and August 3, but was absent. On August 4, Chalimoniuk was admitted to a hospital for treatment for alcohol abuse and dependence, where he stayed through August 10. When Chalimoniuk returned to work on August 15, IBC terminated his employment because his unexcused absences on July 31, August 2, and August 3 placed him over the company’s limit of allowable absences under its absenteeism policy. Chalimoniuk sued IBC for interfering with his rights under the Family and Medical Leave Act (FMLA) and lost.

The court explained that substance abuse may be a serious health condition that entitles an employee to FMLA

leave, but FMLA leave may only be taken for treatment. Absence because of the employee’s use of the substance, rather than for treatment, does not qualify for FMLA leave.

While Chalimoniuk contacted his physician on July 29 seeking treatment for alcohol abuse, calling to make an appointment does not constitute treatment for FMLA purposes, said the court. Treatment includes examination to determine if a serious health condition exists and evaluation of that condition, but here there was no indication that Chalimoniuk was examined or evaluated until August 4. Accordingly, Chalimoniuk had no right to FMLA leave on the three days in question (before his hospitalization) and IBC’s termination of his employment for excessive absences was not wrongful [*Darst v. Interstate Brands Corp.*, No. 04-2460, 2008 U.S. App. LEXIS 489 (7th CA, 1-11-08)]. ■

## Employer Did Not Have Reasonable Cause for Not Paying Employment Taxes Timely

A Better Plumbing Service, Inc. (ABP), a plumbing services company based in Conyers, Georgia, was not entitled to a refund of penalties imposed by the IRS for failure to timely file, pay, and deposit employment taxes because it did not have “reasonable cause” for its action [*A Better Plumbing Service,*

*Inc. v. U.S.*, No. 1:07-CV-0279-RLV, 2008 U.S. Dist. LEXIS 8015 (ND Ga., 1-30-08)].

☞ **WHAT THE LAW SAYS** – Under IRC §6651(a)(1) (file), IRC §6651(a)(2) (pay), and IRC §6656(a) (deposit), additions to tax may be excused if the failure to perform the required

action was the result of “reasonable cause” and not willful neglect. To demonstrate reasonable cause, a taxpayer must show that it exercised “ordinary business care and prudence” but (1) was nonetheless unable to file the return (or pay or deposit the taxes) within the prescribed time or (2) would have suffered an “undue hardship.”

One federal appellate court case – *Brewery Inc. v. U.S.*, 33 F.3d 589 (6th CA, 1994) – said that a taxpayer’s financial difficulties can *never* constitute reasonable cause. However, other federal appellate courts use a “multifactor” approach to assess the facts and circumstances to determine whether the taxpayer exercised ordinary business care and prudence in attending to its payroll tax obligation. Courts applying the multifactor approach look to a taxpayer’s expenditures before and after the taxpayer failed to pay withholding taxes, as well as the taxpayer’s treatment of other creditors in comparison with the IRS.

### Analysis

The court concluded that ABP did not exercise ordinary business care and prudence in balancing its IRS obligations against competing financial commitments under the multifactor approach.

In 2001, ABP hired Suzanne Baker to do its bookkeeping and pay its employer and payroll taxes. Baker was in charge of filing ABP’s payroll tax returns and paying and depositing

the taxes due. She had the authority to write checks on ABP’s behalf. After ABP’s business slowed in 2002, Baker began embezzling funds to support a prescription drug habit, and stopped filing payroll tax returns and depositing employment taxes.

ABP could not establish that it had suffered undue hardship. The company continued to pay creditors over the government, and the mere fact that the company did not have the money to pay both creditors and the government did not constitute undue hardship.

There was no evidence that the money ABP failed to pay the government would have been used to maintain the company’s viability. Baker chose to pay creditors over the government so she could use the money that otherwise would have been used for taxes to finance her drug addiction.

Baker’s theft did not leave ABP unable to comply with its tax obligations. Although Baker was responsible for ensuring that ABP remained in compliance with its tax and reporting obligations, Rick Ingram, the president and sole shareholder of ABP, had ultimate responsibility for satisfying ABP’s tax obligations. The company could not use its reliance on an agent (Baker) to show an inability to comply with its tax obligations, even though Ingram may have been unsophisticated about specific tax obligations and reporting requirements. ■

## IRS Corrects Error in Announcement of Cents-Per-Mile 2008 Maximum Car Value

The IRS has issued an announcement [Ann. 2008-15, 2008-9 IRB 511] correcting errors in an earlier revenue procedure that provided the 2008 maximum value of employer-provided vehicles for which the cents-per-mile valuation rule may be applied (see [PAYROLL CURRENTLY, Issue No. 4, Vol. 16](#)). *Note:* Under the vehicle cents-per-mile method of valuing an employee’s personal use of a company-provided car, the IRS’s standard business mileage rate is multiplied by the personal miles driven by the employee. This method can be used only if a vehicle’s fair market value does not exceed specified maximum amounts.

Maximum values for vehicles put into service in 2008 are as follows:

- Passenger automobile ... \$15,000; and
- Truck or van ... \$15,900.

Maximum values for vehicles under the fleet-average valuation rule, applicable to an employer with a fleet of 20 or more vehicles if none of them exceeds its maximum allowable value, are as follows:

- Passenger automobile ... \$19,900; and
- Truck or van ... \$20,800. ■

## Employer Ordered to Pay Over \$75,000 in Back Overtime to Three Employees

A U.S. District Court has awarded \$78,472 to three employees for violations of the Fair Labor Standards Act’s (FLSA) overtime provisions [*Ochoa v. Alie Brothers, Inc.*, No. 6:06-cv-609-Orl-DAB, 2007 U.S. Dist. LEXIS 69249 (MD Fla., 9-19-07)].

### Background

Salvador Ochoa, Filiberto Ricardo, and Miriam Medina worked for Alie Brothers, Inc., a commercial laundry business serving airlines, hotels, and theme parks in Orlando, Florida. Regardless of how many hours they worked in a workweek, they received only straight-time compensation. The company paid them each week with two checks – the first representing payment for 40 hours of work, and the second for hours worked over 40. The first set of checks was issued by the company’s controller, who did the payroll, but the second set of checks was issued separately and signed by Rayman Alie, the company president and sole shareholder, and Alie’s sister.

The employees were forced to sign time cards with reduced hours under the threat of not receiving a check.

### Overtime

An exact calculation of the overtime due was difficult because Rayman Alie and Alie Brothers, Inc. failed to produce accurate and comprehensive records, and, in fact, acted to keep two sets of records. What records the company did produce were spotty and inconsistent. In addition, when the business relocated from Orlando to Daytona Beach, the payroll records from the Orlando location were destroyed. The employees did not keep separate records because the total hours represented by the two checks they received each week matched the total hours for which they expected to receive pay.

The court explained that where an employer’s records cannot be trusted and the employee lacks documentation, if an employee proves that he or she has performed work that

was not properly compensated and the amount of work and extent of the work can be established “as a matter of just and reasonable inference,” the court may approximate the amount due and award damages to the employee. Here, there were random payroll records from the company supporting the employees’ claims of the hours they really worked, and the court used these to approximate their overtime pay.

### Willfulness

An employer that willfully violates the FLSA is subject to a three-year statute of limitations on violations instead of the usual two-year limit. Here, the court applied a three-year limitations period because of the company’s use of separate

time card reports and two sets of checks for the same pay periods.

### Liquidated damages

An employer that violates the FLSA is automatically subject to “liquidated damages” (i.e., an additional equal amount) unless it can show a good faith basis for its actions. Here, the court said liquidated damages were warranted because the company did not act in good faith when it paid its employees straight time for overtime hours. And Rayman Alie made no effort to determine the overtime provisions of the law and how they applied to employees hired by his company. ■

## Time Spent Donning and Doffing Police Uniform Was Compensable

The city of San Leandro, California, required its officers to be in uniform and properly equipped at the start of a shift. The uniform consisted of items including an undershirt, uniform shirt, shoulder patch, badge, name tag, uniform trousers, and trouser belt. Officers were also required to carry certain equipment such as a gun, handcuffs, taser, tear gas, and a radio. Other equipment was optional.

Officers could change into and out of their uniforms and equipment at home but most chose to change at the police station. Officer Greg Lemmon sued the city, saying that its failure to compensate him for time spent “donning and doffing” his uniform and equipment violated the Fair Labor Standards Act (FLSA).

**WHAT THE LAW SAYS** – Time spent by an employee to get ready for work or to get ready to leave work is not worktime unless the activities engaged in are essential to the employee’s principal work activity. A principal activity includes all activities that are “integral and indispensable” to the principal activity (see *The Payroll Source*®, p. 2-58).

### Ruling

Here, the court said the time Lemmon spent donning and doffing his police uniform and required equipment was compensable worktime because it was: (1) necessary to his principal work, and (2) done for the benefit of his employer. *Note:* This decision is contrary to the decision in the recent case of *Martin v. City of Richmond* (see **PAYROLL CURRENTLY, Issue No. 21, Vol. 15**).

**Necessary to the principal work performed.** The authority conferred by a uniform is essential to the performance of police work, and although police officers can perform some duties without uniforms, they cannot perform all of their required duties without them. Police uniforms are special, said the court, because “the uniform itself forms part of the equipment.” Moreover, officers’ uniforms function as an integrated whole with required equipment, which is clearly necessary for their law enforcement duties.

Time spent by employees changing into and out of

uniforms is compensable if the employer requires the changes to be done on its premises. However, it did not matter that in this case officers had the option of putting on their uniforms at home. Most officers donned and doffed their uniforms at the police station and this, along with the fact that the city provided lockers for changing clothes, indicated that donning and doffing at the police station was a de facto job requirement.

**Benefit of the employer.** The donning and doffing of protective gear benefits the employer if it helps the employer: (1) comply with legal requirements, and (2) avoid work slowdowns and problems that would arise because of injuries to employees. Both factors showed that the donning and doffing by the officers benefited the city.

For example, California law requires employers to do everything reasonably necessary to protect the safety of employees. Wearing a uniform and certain equipment minimizes the potential for injury to police officers, which enables a healthy and ready police force. A healthy and efficient police force in turn benefits the city, which would not require uniforms otherwise.

The fact that the city provided lockers to officers so they could don and doff their uniforms at the police station emphasized the benefit to the city. For example, officers donning and doffing at the police station were more likely to be in complete uniform and on time when reporting for duty and would be less likely to leave an essential piece of equipment at home.

**Noncompensable activities.** On the other hand, donning and doffing optional equipment was noncompensable, even if it benefited the city, said the court. And the time spent between donning and doffing and the next principal activity was also noncompensable, so that officers who donned and doffed their uniforms and equipment at home were not entitled to compensation for commuting to or from the station while in uniform [*Lemmon v. City of San Leandro*, No. C 06-07107 MHP, 2007 U.S. Dist. LEXIS 90278 (ND Cal., 12-7-07)]. ■

## Firearms Instructors Were Not FLSA-Exempt Teachers

The Court of Federal Claims has ruled that firearms instructors at the Federal Law Enforcement Training Center (FLETC) in Glynco, Georgia, do not qualify for exemption under the Fair Labor Standards Act (FLSA) as teachers because they are not employed by an “educational establishment” [*Astor v. U.S.*, No. 05-248C, 2007 U.S. Claims LEXIS 361 (Ct. of Fed. Cl., 11-13-07)].

### Background

FLETC is a bureau within the Department of Homeland

Security that trains state and federal law enforcement agency personnel in the safe handling, proficient application, and justifiable use of firearms, in a variety of basic and advanced courses. FLETC instructors follow prescribed lesson plans and conform to established operating procedures governing punctuality, uniforms, and safety.

The instructors sued to recover overtime for hours worked over 40 in a workweek for which they received only regular pay. FLETC said the instructors were exempt from the FLSA’s

overtime pay requirement because they were “teachers” and therefore exempt professional employees.

**WHAT THE LAW SAYS** – Under FLSA regulations, an exempt professional employee includes any employee with a primary duty of imparting knowledge through teaching, tutoring, instructing, or lecturing who is employed and engaged in this activity in an educational establishment by which the employee is employed (29 C.F.R. §103(a)).

An “educational establishment” includes not only elementary and secondary schools and institutions of higher education, but also special schools and post-secondary career programs. It does not matter whether a school is public or private, or whether it is operated on a for-profit or not-for-profit basis. Factors considered in determining whether a “postsecondary career program” is an educational institution include whether it is licensed by a state agency responsible for the state’s educational system or accredited by a nationally recognized accrediting organization for career schools (29 C.F.R. §541.204(b)).

#### **Educational establishment**

The court said that various nontraditional schools – such as prison schools, not-for-profit corporations offering continuing education programs for professionals like attorneys and accountants, and even a tractor-trailer driving school – have been found to be educational establishments. In each of these cases: (1) the enrolled students either sought an educational degree or its equivalent, a type of license, or continuing education credits; (2) the accreditation of the establishment was strong; and (3) the teaching personnel possessed certification, education, or experience. FLETC did not meet these standards.

First, FLETC did not offer high school or college degrees or firearms licenses upon completion of training. Nor did

it offer continuing education credits. The fact that FLETC courses were a prerequisite for employment at many federal agencies and served as refresher courses for law enforcement agency personnel did not make FLETC a “postsecondary career program.”

Second, unlike other institutions, which are state chartered or government licensed, FLETC had a solitary accreditation that it earned in March 2006, from a newly created agency, the Federal Law Enforcement Training Accreditation (FLETA). Although it was an independent agency, FLETA was located in the same facility as FLETC and was not a nationally recognized accrediting organization for career schools.

Finally, FLETC instructors were not required to possess any teaching credentials, such as degrees in education or teaching experience. They were simply required to have a high school education, firearms experience, and experience demonstrating the ability to “train and/or instruct.”

#### **Liquidated damages**

An employer violating the FLSA (i.e., required to pay back minimum wages and overtime) must pay an additional equal amount in liquidated damages unless it can show a good faith basis for its violations. Here, the court said liquidated damages were not warranted because the government acted in good faith or with reasonable grounds to believe that the instructors should be classified as exempt teachers because of their job description (which was to “provide high quality training to federal agency law enforcement officers and to instill the technical and analytical knowledge and skills needed for the highest possible proficiency” and included duties such as the development of lesson plans, research, and evaluation of student performance), and in view of the instructors’ daily duties (the training of law enforcement officers to use firearms properly, safely, and proficiently). ■

## **Convenience Store Manager Was FLSA-Exempt Executive**

The Sixth Circuit Court of Appeals has affirmed that a store manager in charge of a gas station/convenience store was not entitled to overtime compensation under the Fair Labor Standards Act (FLSA) because she was an exempt executive employee [*Thomas v. Speedway SuperAmerica, LLC*, 506 F.3d 496 (6th CA, 10-30-07)].

#### **Background**

Speedway SuperAmerica, LLC operated gas station/convenience stores, each of which was run by a store manager. Although she was a Speedway store manager, Mabel Kay Thomas spent nearly 60% of her time on non-managerial tasks such as stocking merchandise, cleaning bathrooms, and operating the cash register. She was expected to work 50 hours per week, but often worked more.

To qualify for the FLSA’s executive exemption, an employee must meet several criteria (see *The Payroll Source*®, p. 2-12), one of which is a primary duty of management. Here, the question for the court was whether Thomas satisfied the primary duty test.

#### **Analysis**

The court explained that an employee who spends less than 50% of his or her time on management duties can still be considered to have a primary duty of management if certain factors support that conclusion, such as: (1) the relative importance of managerial duties as compared with other types of duties; (2) the frequency with which the employee exercises discretionary powers; (3) the employee’s relative

freedom from supervision; and (4) the relationship between the employee’s salary and the wages paid to other employees for the kind of nonexempt work performed by the employee. Here, all of these factors indicated that Thomas’ primary duty was management.

Thomas’s managerial duties were clearly more important to Speedway than her non-managerial duties, said the court. These duties included hiring and training employees, assigning weekly work schedules, resolving employee complaints, evaluating employee performance, and making compensation recommendations for employees (most of which were accepted by the district manager to whom she reported). “If Thomas failed to perform her non-managerial duties, her Speedway station would still function, albeit much less effectively. ... If, however, Thomas failed to perform her managerial duties, her Speedway station would not function at all because no one else would perform these essential tasks.”

Thomas interviewed and hired employees, granted and scheduled employee vacations, decided whether to order additional inventory in anticipation of high demand, and resolved safety issues in the store. The court concluded that she exercised discretion over important managerial matters frequently enough that management was her primary duty.

Thomas enjoyed relative freedom from supervision. Her district manager, who supervised between 10 and 12 Speedway stores, visited only once a week, communicating more frequently by phone and e-mail. Thomas was the most

senior employee at the station, so that on a day-to-day basis there was no supervisor monitoring her every move. The court explained that the primary duty component of the executive exemption requires only *relative* freedom from supervision.

Finally, Thomas received a base salary of \$522 per week,

as well as bonus compensation based on the gross profit margin of her store, which could be as much as \$2,500 per month. In her final seven months of employment, Thomas earned nearly \$22,000, while the next highest paid employee at her store earned only around \$14,000. ■



## STATE AND LOCAL NEWS

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### Georgia

**Employer's withholding guide revised.** The Department of Revenue (DOR) has revised the *Employer's Tax Guide* (download at [www.dor.ga.gov/taxguide/TSD\\_Employers\\_Withholding\\_Tax\\_Guide\\_February\\_2008.pdf](http://www.dor.ga.gov/taxguide/TSD_Employers_Withholding_Tax_Guide_February_2008.pdf)). The guide contains 2008 withholding tax due dates for monthly, quarterly, and annual filers. Withholding tables have not been revised [DOR *Employer's Tax Guide*, rev. 2-08].

### Maine

**Mandatory electronic filing of withholding returns, 2008 thresholds.** Mandatory electronic filing of all original quarterly withholding returns and annual reconciliation returns for 2008 applies to: (1) employers with 75 or more employees in 2008 that are subject to Maine income tax withholding; (2) third-party filers or payroll processors preparing withholding returns for an employer with 75 or more employees in 2008 who are subject to Maine income tax withholding; (3) third-party filers or payroll processors with 75 or more client employers in 2008 that are required to file withholding returns or make Competitive Skills Scholarship Fund or unemployment compensation insurance payments; and (4) non-wage payers with 75 or more payees in 2008 that are subject to Maine income tax withholding. Beginning in 2009, these thresholds will decrease to 50 or more employees, client employers, or payees [Code Me. R. §§18-125-104, 18-125-803; Maine Revenue Services *Maine Tax Alert*, 2-08].

### Nevada

**Mandatory electronic UI payments, threshold established.** Effective 7-1-08, employers must make electronic payments of unemployment insurance (UI) taxes, interest, or penalties that amount to \$10,000 or more in the aggregate. Agents that enter into an agreement with one or more employers are required to make electronic UI tax payments if the amounts total \$10,000 or more [S.B. 517, L. 2007].

### Texas

**Lump sum child support payments, two new electronic methods.** The Office of the Attorney General of Texas has developed two new electronic methods (an online form and a data transfer system) for employers to submit lump sum payment notifications for child support withholding purposes. To access these methods, visit <http://employer.oag.state.tx.us>.

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