FLSA-794

August 11, 1981

Thank you for your letter of July 24, 1981, asking on behalf of a client if payments deposited into Individual Retirement Accounts (IRAs) for retirement benefit purposes, are excludabe from employees' regular rates of pay for the purpose of computing overtime compensation due under the Fair Labor Standards Act. Under Section 7(e)(4) of the Act such payments are excludable if they are "contributions irrevocably made by an employer to a trustee or third person pursuant to a bona fide plan for providing old-age, retirement, life, accident, or health-insurance or other similar benefits for employees." In order for an employer's contribution to qualify for this exclusion, certain requirements must be met as set forth in Section 778.214 and 778.215 of Part 778.

You state your client would establish an IRA for each employee who has earned eligibility to participate in the plan. The accounts would be established with a financial institution which would also serve as the trustee of the plan. Eligible employees include those on the seniority list prior to the effective date, September 27, 1980 (payments to these employees'IRAs would be retroactive to that date), new employees who complete a 90-day probationary period and, rehires who complete a 90-day probationary period. If an employee of either of the latter two groups terminates employment before completion of the probationary period, he or she would not receive any benefits. Your client will pay 62¢ for every hour of work performed by eligible employees into their IRA. Effective July 20, 1981, the hourly contribution would be increased by one cent for each year of employment for each employee with ten or more years of credited service. Years of service for this additional contribution will be computed on the payroll date ending nearest November 1st of each year, and only full years of service will be counted. Re-employed workers, however, forfeit any prior months or years of credited service for determining these additional hourly contributions.

We are concerned that the early withdrawal feature of IRA plans could convert your client's plan into just another source of cash compensation for employees and thus violate section 778.215(a)(4). However, inasmuch as Congress has provided for a 10% penalty tax, as well as for loss of the advantages of tax deferral, in order to discourage early withdrawals from the IRAs, we believe that under normal circumstances this risk is not great. Therefore, it is our opinion that contributions made by your client to a trustee for the establishment and maintenance of IRAs on behalf of its employees would not affect the regular rate of pay for the purpose of computing overtime compensation.

We grant this exception to our regulatory requirements contained in Section 778.215(b) of Part 778, because we do not believe these plans should receive less favorable treatment than other plans also approved by the Internal Revenue Service (IRS).

You also ask if our opinion would change if the contributions were found to exceed the contribution limits established by the Internal Revenue Code.

Whether employer contributions to a retirement plan qualify for exclusion from the computation of the regular rate of pay depends on the purpose of the plan and not on the amount of contributions an employer may make on an employee's behalf. Therefore, if the conditions of sections 778.214 and 778.215 are met, the plan may still be valid under the Act.

Sincerely,

William M. Otter
Administrator