**U.S. Department of Labor**
Employment Standards Administration
Wage and Hour Division
Washington, D.C. 20210

**March 10, 2006** **FLSA2006-9**

Dear **Name***:

This is in response to your letter requesting an opinion regarding the application of section 7(i) of the Fair Labor Standards Act (FLSA) to payments made to membership directors employed by your client, a private health club/fitness facility. You seek this opinion for employment in states other than California. Our response will cover the application of the FLSA in all states, including California. Note, however, that no provision of the FLSA preempts a state law or municipal ordinance that provides greater benefit to employees. *See* 29 U.S.C. § 218(a) (copy enclosed).

You state that your client runs a health club/fitness facility and explain the duties of the membership directors as enlisting members and selling them additional services. Membership directors must: meet production goals; conduct presentations and tours of the facilities; discover prospective members' fitness goals, motivation for joining, and objectives; develop leads and solicit referrals; and provide other customer services and engage in other sales related activities. The health club/fitness facility is a for-profit establishment that sells memberships to the general public. Your client receives more than 75% of its annual sales volume from the sale of services that are not for resale. In another letter regarding this employer, you state that you believe your client "is clearly a service establishment."

You describe the payment of membership directors as a mixture that includes (a) a base pay amount, (b) commissions, (c) a draw against commissions, and (d) bonuses. The fitness club pays its membership directors on a semimonthly basis (the 7th and the 22nd of the month) as follows:

- On the first payday they receive (a) base pay for the second half of the preceding month, and (b) a draw that will be counted against commissions earned from the previous month.
- On the second payday they receive (a) base pay for the first half of the current month, and (b) commissions earned from the previous month (less the amount of the draw they received on the first payday of the month).

You also state that the amount of the draw remains the same each month, but do not discuss the relative amount of the draw compared to the amount of the commissions earned. You also do not provide information about how the "base pay" is determined (for example, whether it is based on a salary or an hourly rate) or the amount of the base pay relative to the commissions.

You further state that the membership directors' "commission" payments may include one quarterly and two monthly bonuses:

- Quarterly incentive bonuses based on sales in excess of the quarterly quota;
- A "performance bonus," which is a fixed dollar amount paid to the employees with the highest sales in the month and the highest overall "closing" rate for the month; and
- A "pooling bonus" that varies from month to month. You state that each club has a specific "target" for the month and that, if the target is met, a pool of between $1,000 and $2,000 is distributed among the membership directors according to each individual's contribution toward meeting the goal for the month.

Lastly, you state that the regular rate of pay for membership directors exceeds one and one-half times the minimum wage rate and that more than half of their compensation for a representative period of at least a month consists of "commissions/bonuses" on services. Although your letter does not provide sufficient detail to perform the calculations needed to verify that the requirements are met, the following guidance is provided to assist your client in making the calculations needed to determine the exempt status of each membership director.

The application of the section 7(i) exemption to individual employees depends in part upon their specific earnings. *See* 29 U.S.C. § 207(i) (copy enclosed). Accordingly, we cannot opine about the exemption based upon the general earnings information you provide. That would require specific earnings information for each employee. However, we can explain how to evaluate the types of payments your client makes to its employees to determine whether they qualify for the exemption.

To qualify for the section 7(i) exemption from the overtime provisions of the FLSA, three conditions must be met:

1. The employee must be employed by a retail or service establishment;
2. The employee's regular rate of pay must exceed one and one-half times the applicable minimum wage under section 6 of the FLSA; and
3. More than half of the employee's total earnings in a representative period must consist of commissions on goods or services.

It is the employer, not the employee, who must satisfy the first element of this test. *See* 29 C.F.R. § 779.411 (copy enclosed). In order to qualify as a "retail or service establishment" under section 7(i), an employer must engage in the sale of goods or services, at least 75% of the annual dollar volume of sales of goods or services must not be for resale, and the sales must be recognized as retail sales or service in the particular industry. *Id*. The health club/fitness facility engages in the sale of health and fitness services. Additionally, sales of these services are not for resale, so the second requirement is met. Finally, health club/fitness facilities are recognized as retail service establishments because they (1) service the everyday needs of the community, (2) are at the end of the distribution stream, (3) do not take part in the manufacturing process, and (4) provide services for the comfort and convenience of the public by opening membership to members of the general public. 29 C.F.R. § 779.318 and Field Operations Handbook § 21b03(a) (copies enclosed). Therefore, it is our opinion that the health club/fitness facility qualifies as a retail or service establishment.

The final two elements of section 7(i) depend upon payments to the employees and not the establishment for which they work. To qualify as a commission, payments must be based on the provision of "goods or services which the establishment sells." 29 C.F.R. § 779.413(b) (copy enclosed). "The whole premise behind earning a commission is that the amount of sales would increase the rate of pay. Thus, employees may elect to work more hours so they can increase their sales, and in turn, their earnings. When a commission plan never affects the rate of pay, the purpose behind using a commission rate also fails." *See Erichs v. Venator Group, Inc*., 128 F. Supp. 2d 1255, 1260 (N.D. Cal. 2001) (quoting *Herman v. Suwannee Swifty Stores, Inc*., 19 F. Supp. 2d 1365, 1371 (M.D. Ga. 1998)). Note that all of the compensation plans found in 29 C.F.R. § 779.413(a) "except for the 'straight salary or hourly rate' may qualify as 'bona fide commission' plans under §207(i)." *Viciedo v. New Horizons Computer Learning Ctr. of Columbus, Ltd*., 246 F. Supp. 2d 886, 896 (S.D. Ohio 2003). Straight salary and hourly payments do not qualify as commissions.

Over the representative period, the employer must ensure that the employee's commissions represent more than half the employee's total pay. See 29 C.F.R. § 779.417 (copy enclosed). Analysis of the various payments made to your client's membership directors indicates some, but not all, qualify as commissions under section 7(i).

The base payment is clearly not commissions, whether paid on an hourly or a salary basis. The performance, pooling, and quarterly incentive bonuses, whether individual or group, will qualify as commissions under section 7(i), provided they are based on the level of sales of health and fitness services.

A straight commission with draws qualifies as a commission if it results "from the application of a bona fide commission rate." 29 U.S.C. § 207(i). The proportion of commission payments and the amount paid as a draw against future earnings must be closely scrutinized by the employer to assure this requirement is met. As explained in the regulations, a commission plan is not bona fide if, in fact, the formula for computing commissions is such that an employee always earns the same fixed amount of compensation each pay period. If an employee's commission seldom or only infrequently exceeds the draw, serious doubts would arise regarding the substance of the commission agreement. The relationship of draws to commissions is specifically discussed at 29 C.F.R. § 779.416 (copy enclosed). *See* WH Opinion Letters July 14, 1982, and April 24, 1998 (copies enclosed). If the individual employee's commission meets the requirements listed above, it is our opinion that the membership directors' compensation plan would comply with the requirements of section 7(i).

This opinion is based exclusively on the facts and circumstances described in your request and is given based on your representation, express or implied, that you have provided a full and fair description of all the facts and circumstances that would be pertinent to our consideration of the question presented. Existence of any other factual or historical background not contained in your letter might require a conclusion different from the one expressed

herein. You have represented that this opinion is not sought by a party to pending private litigation concerning the issue addressed herein. You have also represented that this opinion is not sought in connection with an investigation or litigation between a client or firm and the Wage and Hour Division or the Department of Labor. This opinion is issued as an official ruling of the Wage and Hour Division for purposes of the Portal-to-Portal Act, 29 U.S.C. § 259. *See* 29 C.F.R. §§ 790.17(d), 790.19; *Hultgren v. County of Lancaster,* 913 F.2d 498, 507 (8th Cir. 1990).

We trust that the above is responsive to your inquiry.

Sincerely,

Alfred B. Robinson, Jr.
Acting Administrator

Enclosures: FLSA §§ 7(i) and 18(a)
29 C.F.R. 779.411
29 C.F.R. 779.318
FOH 21b03
29 C.F.R. 779.413
29 C.F.R. 779.416-7
WH Opinion Letters July 14, 1982 and April 24, 1998

**Note: * The actual name(s) was removed to preserve privacy in accordance with 5 U.S.C. § 552(b)(7)**