No. 18-1541

In The Supreme Court of the United States

YASSINE BAOUCH, *et al.*,

Petitioners,

v.

WERNER ENTERPRISES, INC.,
d/b/a WERNER TRUCKING and
DRIVERS MANAGEMENT, LLC,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Eighth Circuit

REPLY BRIEF FOR PETITIONERS

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I. The Eighth Circuit Established Important Standards Under The FLSA That Conflict With The Standards In Other Circuits

The petition, quoting from the Eighth Circuit opinion, sets out three legal standards applied by the court of appeals. Pet. 24-26 (quoting App. 20a). The brief in opposition acknowledges each of those same three aspects of the court of appeals' opinion. Br.Opp. 11 (citing App. 20a). Werner, however, is unable to explain away this pivotal language of the court of appeals' opinion.

In some passages, Werner suggests that the court of appeals did not apply any legal standards at all, but just weighed the evidence. Br.Opp. i ("the Eighth Circuit ... determined ... based on the specific facts of this case"); *see id*. 8 ("the Eighth Circuit concluded that issue was a 'highly *fact-intensive* inquiry' that turned on a 'case specific *factual* inquiry' and *not* any bright line legal rules" (emphasis in original)). But this account cannot explain why the Eighth Circuit concluded the Payments were wages, not reimbursement, when the IRS Appeals Commission on the same facts reached the opposite conclusion. Werner seeks to reconcile the Eighth Circuit and IRS decisions by insisting that the court and the agency were applying different legal standards. Br.Opp. 7-8, 8, 10. But that can only be true if the Eighth Circuit was indeed applying *some* legal standard, and not just weighing the evidence.

Werner offers varying accounts of what legal standards, other than those set out at p. 20a of the

opinion, the court of appeals was applying. At p. 7 of its brief in opposition, Werner asserts that the Eighth Circuit opinion was "based *solely* on the FLSA regulations and the facts of this case." (Emphasis added). But Werner does not explain which FLSA regulation mandated the result or why. At p. 8, Werner states "the Eighth Circuit simply applied the text of the FLSA *and* its applicable regulations to the specific facts of this case...." (Emphasis added). But Werner does not explain what provision of the text supported the court of appeals' decision, or how, or why the text of the FLSA was a basis of the Eighth Circuit opinion on p. 8 when it was not on p. 7. Werner also comments that the court of appeals' decision was based on "established case law" (*id*. 8), but does not explain which cases established that law or what legal standards those decisions established. More vaguely, Werner asserts that the Eighth Circuit was merely applying "well-established legal standards" (*id*. 1), which would rule out reliance on any interpretation of the regulations or text that is not already widely recognized; but Werner does not explain what those "well-established legal standards" were or why they were not the very standards spelled out at p. 20a of the Eighth Circuit opinion. As the petition noted, Werner argued in the courts below that the three legal standards ultimately spelled out in the Eighth Circuit opinion were indeed established legal standards. Pet. 24-26.

Werner states that whether a payment constitutes wages or reimbursement under the FLSA "depend[s] on myriad factors." Br.Opp. 9, 12, 20 (quoting App. 13a). The factors that are relevant under the FLSA, Werner

asserts, are different than the factors relevant under the Internal Revenue Code and IRS regulations, which could explain how the IRS and the Eighth Circuit came to different conclusions. "There are legal differences and, in the case of a regular rate calculation, many additional factors at play." Br.Opp. 8 (quoting App. 9). So the key issue is what "factors" were relied on by the court of appeals that would not have been applicable in the tax proceeding. Werner does not say what those factors were, but the Eighth Circuit opinion clearly answers that question. At App. 20a-21a, after spelling out the three standards relied on in the opinion, the court of appeals explained "[e]ach of these factors additionally establish that the Payments were remuneration for employment rather than reimbursement for expenses."

Despite this language, Werner denies that the Eighth Circuit opinion (at App. 20a) was delineating what factors are legally relevant under the FLSA; rather, Werner argues, this aspect of the opinion was merely "statements of fact ... [in] the Eighth Circuit's discussion of the facts supporting the District Court's conclusion." Br.Opp. 11. But if those facts supported the District Court's conclusion that the Payments were wages, why didn't the same facts support the Tax Examiner's similar conclusion that the Payments were wages? Werner asserts that the three considerations set out at App. 20a were merely "facts [that] indicated the Payments at issue here were wages." *Id.* But if they indicated that "here," why didn't those facts indicate the same thing in the IRS audit? The answer can only

be that the three listed considerations, as the Eighth Circuit expressly stated, are legal factors applied under the FLSA, even though those factors would not be utilized under the Internal Revenue Code and regulations.[1]

Werner rejoins that, even if those three considerations are legal "factors," they still are not "distinct legal standards." Br.Opp .9. Werner does not explain what the difference is between a legal factor and a legal standard. Werner may be suggesting that the three factors are not each per se rules – not "bright line legal rules" (Br.Opp. 10) – but are only considerations that a court would weigh in an FLSA case (although not in a tax case). The Eighth Circuit opinion on its face describes these standards as per se rules, each sufficient on its own to mandate a finding that the payments were wages: "[*e*]*ach* of these factors ... establish that the payments were remuneration for employment rather than reimbursement...." App. 20a-21a (emphasis added). But even if the three factors were only relevant (but not conclusive) considerations, that would have prohibitive consequences for any employer in the Eighth Circuit whose employees might assert overtime claims. Such an employer, for example, could not mention in an on-line job posting that it paid per diem or reimbursed expenses, because that statement would

[1] Werner argues that Baouch failed to prove that the Payments "approximated actual expenses." Br.Opp. 13. But Werner does not claim that the court of appeals relied on this ground. To the contrary, the Eighth Circuit held that the amount of the payments was "based on a reasonable estimation of travel expenses." App. 21a.

constitute evidence that the payments were used "to attract new employees" (App. 20a) and thus were part of the employee's regular rate, substantially raising the employer's overtime exposure. *See* Pet. 29-34.

Werner does not deny that no other circuit applies the three standards set out at p. 20a of the Eighth Circuit opinion. *See* Pet. 34-38.

II. The Petition Correctly Describes The Facts In This Case

Werner's objections to the petition's summary of the facts do not raise significant issues. Werner argues that the question before the IRS was not whether the payments were wages, but whether the payments satisfied the IRS requirements for an accountable plan. Br.Opp. 4. But those two issues (in this context) are the same; the accountable plan rules delineate what are and are not wages for tax purposes. The brief in opposition objects that the petition failed to acknowledge that statements made by Werner to the IRS "were made in the context of the IRS Accountable Plan rules." Br.Opp. 4-5. To the contrary, the petition specifically described both the accountable plan rules (Pet. 7-8) and the administrative proceeding under them. Pet. 13-16. Werner objects that the petition "suggest[ed]" that Werner misled the IRS about the fact that it was treating the payments as wages for FLSA purposes. Br.Opp. 4. In fact, the petition made clear that the IRS was well aware that Werner was doing so, and that Werner's action in this regard was one of the key grounds of the Tax Examiner's decision. Pet. 14-16.

Werner asserts that the petition's description of the financial effect of the plan (Pet. 10-12) was inconsistent with the district court finding that the "primary effect" of the plan was to increase take home pay. Br.Opp. 6 (quoting App. 28a). There is no inconsistency here. The district court finding was about experienced drivers, who earned far more than student drivers. App. 26a-31a. The petition, on the other hand, describes the effect of the plan on the poorly paid student drivers, the petitioners here. Pet. 10-12. The brief in opposition does not actually disagree with the observation in the petition that student drivers would not be subject to the 15% withholding described in the company materials, and thus would at least usually lose money under the plan. Pet.12 n.11.

III. The DOL and IRS Regulations Use Identical Language To Delineate What Payments Are Not Wages

The linchpin of the Eighth Circuit's decision is its assertion that the standard governing whether a payment is wages rather than reimbursement under the FLSA is different than the standard governing the same distinction in a tax case. The relevant language of the FLSA and IRS regulations, however, is essentially the same.

Under the FLSA regulations, the critical language is that a payment is not wages – not part of a worker's "regular rate" – if it is "reimbursement for" certain expenses, such as travel expenses.

> (a) General rule. Where an employee incurs expenses on his employer's behalf or where he is required to expend sums solely by reason of action taken for the convenience of his employer, section 7(e)(2) is applicable to *reimbursement for* such expenses. Payments made by the employer to cover such expenses are not included in the employee's regular rate if the amount of the reimbursement reasonably approximates the expenses incurred....
>
> (b) Illustrations. Payment by way of *reimbursement for* the following types of expenses will not be regarded as part of the employee's regular rate:
>
> * * *
>
> (3) The actual or reasonably approximate amount expended by an employee, who is traveling "over the road" on his employer's business, for transportation (whether by private car or common carrier) and living expenses away from home, other travel expenses, such as taxicab fares, incurred while traveling on the employer's business.

29 C.F.R. § 778.217 (emphasis added).

The IRS regulations use an essentially identical phrase.

> Except as provided in paragraphs (d)(2) and (d)(3) of this section, an arrangement meets the requirements of this paragraph (d) if it provides advances, allowances, (including per diem allowances, allowances only for meals

> and incidental expenses, and mileage allowances) or *reimbursement only for* business expenses that are allowable as deductions under part VI (section 161 and the following), subchapter B, chapter 1 of the Code....

26 C.F.R. § 1.62-2(d)(1) (emphasis added); *see* 26 C.F.R. §§ 1.62-2(d)(2), 1.62-2(f)(2).

The phrase "reimbursement for" (or "reimbursement only for") is susceptible to a number of different interpretations. It might refer to the economic reality of the transaction, to the intent of the employer and/or the employee, to the manner in which the payment was labeled, or to some combination of these considerations. But nothing in the text of the regulations suggests that the phrase should have a different meaning under the Department of Labor regulations than it has under the IRS regulations.

Werner's position in the tax proceeding and in the later FLSA case focused on this very language. In the course of the tax proceeding, "Werner represented to the IRS ... that the Payments at issue were reimbursements for travel expenses...." App. 4a. But several years later in the FLSA litigation, "Werner ... represent[ed] that ... these ... Payments are *not* reimbursement for reasonable travel expenses...." App. 5a (emphasis in original). The Eighth Circuit opinion is an interpretation of this critical phrase, common to both sets of regulations. Each of the three factors set out at p. 20a of that opinion, the court held, established that the "payments were remuneration for

employment rather than reimbursement for expenses." App. 20a-21a.

IV. This Court Is The Only Appropriate Forum In Which To Resolve Whether The FLSA and Tax Law Standards Are Different

When litigation turns on the inter-relationship between two statutes administered by separate federal agencies, this Court can be the only forum in which the views and interests of both federal agencies could be considered. That is the situation in the instant case. Although the IRS was legitimately concerned about the legality under the FLSA of Werner's practices, the IRS in the context of an administrative proceeding would not have known the views of the Department of Labor. When, in the subsequent FLSA litigation, issues about federal tax law arose, the IRS could not have been expected to know about or participate in the judicial proceedings. In this Court, however, the Solicitor General could advance the views and interests of both affected agencies.

In its brief in opposition, Werner raises an important issue of federal tax law. Under the accountable plan rules, payments can only be excluded from wages if they are a reasonable approximation of employee expenses. Werner in this Court insists that a taxpayer can meet that burden based solely on a *prediction* about what those expenses will be. Where (as here) the payments are an existing practice, Werner insists a prediction will still suffice, regardless of whether the actual expenses were similar in amount to the

payments in question. "An employer can satisfy the IRS accountable plan requirement simply by prospectively estimating the expenses the employer *expects* employees will incur ... , *without proof of the expenses actually incurred.*" Br.Opp. 5 (emphasis in original). The IRS might well interpret the regulation otherwise; the wording of the regulation in question on its face requires that the payment be reasonable in light of the actual expenses. *See* 26 C.F.R. § 1.62-2(f)(2).

Werner assures this Court that it did not represent to the IRS that the level of *actual* driver expenses ranged from $59 to $65 a day. Werner asserts that the affidavit at issue, from Werner's Chief Financial Officer, was only "prospectively estimating the expense the employer *expects* employees will incur" (Br.Opp. 5) (emphasis in original), and "does not speak to the expenses *actually incurred* by drivers...." Br.Opp. 6 (emphasis in original). But the IRS may well have understood that the affidavit was describing actual rather than predicted expenses, because it was worded in the present (not future) tense.

> I ... understand, ... , that the estimated business expenses over-the-road drivers (including student drivers) *currently incur* range from $59 to $ 65 dollars per day.... For example, I understand, ... , that [what] over-the-road drivers (including student drivers) *incur* include, among other things, deductible and nondeductible meal and incidental expenses because these drivers generally *eat* meals and purchase incidental items at truck stops....

App. 1905 (emphasis added).

The brief in opposition states that "the Department of Labor has never questioned Werner's treatment of the Payments as wages." Br.Opp. 6. It is unclear whether Werner is asserting that DOL is well aware of that practice, and has concluded that it is legal, or is only noting that DOL has done nothing because it is simply unaware of the scheme at issue. The Department of Labor itself could clarify its position.

The brief in opposition takes positions that are at odds with Werner's positions in the earlier IRS proceeding. In the tax proceeding, Werner defended the payments as legitimate reimbursements for driver expenses. Pet. 18. But in its brief in opposition, Werner describes those payments as only "*ostensibly* for meals and other incidental expense[s]" (Br.Opp. 2) (emphasis added), as if denoting the payments as reimbursements in the company's tax filings was just a ruse to reduce the firm's taxes. To support its position in the tax proceeding, Werner provided the IRS with documentary evidence about the level of driver expenditures. Pet. 21-22. (In the subsequent FLSA litigation, Baouch introduced that same evidence in an effort to prove the payments were really reimbursements, not wages. Pet. 22). But the brief in opposition denigrates Werner's own IRS documentation as insufficient to constitute "*any* evidence of drivers' actual expenses in this case" (Br.Opp. 13) (emphasis in original), citing the portion of the district court opinion that (at Werner's behest) attacked the reliability of the documentation Werner had earlier submitted to the IRS. App. 71a-72a.

The petition spelled out a series of instances in which specific quoted representations that Werner had made to the lower courts conflicted with representations Werner had earlier made to the IRS. Pet. 18-22. The brief in opposition does not attempt to explain how those facially inconsistent statements could be reconciled. At least some of Werner's representations in the lower courts, and in this Court, would probably come as a surprise to the IRS.

This case is of exceptional practical importance. Werner advised both the IRS and the courts below that the practices at issue are followed throughout the entire United States trucking industry. If this litigation upholds the ability of employers to treat payments as reimbursements for tax purposes, but as wages for FLSA purposes, it will spawn any number of ingenious tax avoidance schemes. The practical consequence of such schemes is to enable an employer to meet its payroll expenses by diverting funds that would otherwise have been paid to the Treasury as income taxes, Social Security taxes, or FUTA taxes. Conversely, to the extent that standards under the Internal Revenue Code and regulations are consistent with the FLSA standards, the IRS, the DOL, and employees proceeding under the FLSA can play valuable complementary roles.

CONCLUSION

For the above reasons, a writ of certiorari should issue to review the judgement and opinion of the Court

of Appeals for the Eighth Circuit. In the alternative, the Solicitor General should be invited to file a brief expressing the views of the United States.

Respectfully submitted,

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