Salary Considerations under the New DOL Standards

On December 1, 2016, the Department of Labor (DOL) will implement changes raising the minimum compensation for exempt employees to $47,476 annually. While salary is just half of a two-part equation that includes a duties test of essential job functions, scrutiny is under way to analyze compensation and find solutions to avoid conflict with the new rule.

Why not just have all employees work 40 hours and get approval for overtime?

The statutory definition of “employ” is “to suffer or permit to work.” The phrase “suffer or permit” to work does not mean “approve.” Hence, any time a nonexempt employee works, the employee must be compensated. A nonexempt employee cannot volunteer to work off the clock, so activities as innocuous as an employee arriving early and just starting their day become problematic. Common advice is to issue progressive discipline for employees who work unapproved overtime, but writing up a good employee for what they reasonably perceive to be initiative can open a new can of worms.

Employers further bear the burden of capturing and recording all time worked. Documenting compensable time is complicated when reviewing the variations of what constitutes work time. The non-exhaustive list includes:

- Waiting or on-call time when it is on the employer’s premises (for example, waiting for a shift replacement to arrive)
- Work-related training activities (including travel time if they are off-site)
- Eating meals while checking emails or answering phones
- Work travel outside of the employee’s normal commute
- Answering work emails or completing reports after work hours
- Attendance at required company functions, including volunteer activities and social events

Even with a sophisticated time-keeping system, capturing all hours is a challenge.

So what are some solutions?

Salary increase. If the duties test supports the classification of an employee as exempt, you can simply raise the employee’s salary to meet the minimum $913 weekly threshold.

Because budgets may not support across-the-board increases in salaries, Fair Labor Standards Act (FLSA) minimum salaries can be offset by:

- Communicating to employees that this new rate will be in lieu of all or part of any annual increase or cost of living changes
- Reducing end of year bonuses or other compensation
- Requiring additional hours of work (exempt staff are not bound by 40 hour limits)

Bonus or incentive. Alternatively, an employer could make use of the new rule that allows up to 10 percent of an employee's minimum salary to be paid through nondiscretionary bonuses, incentive pay, or commissions.

- "Nondiscretionary" means that the bonus or commission was in accordance with preannounced standards.
- Bonuses must be paid quarterly and they must be paid no later than one pay period after the end of the quarter to make up any shortfall.
- A bonus can be a flat rate or a percentage.
- The bonus can be used to account for up to $1,175 quarterly compensation.

Example 1: The use of the 10 percent bonus as part of minimum salary.

John Fry is the Shift Manager at the Happy Hamburger Hut. His annual salary is $42,728. This is approximately $4,748 short of the DOL minimum exempt salary of $47,476. As a manager, he is eligible for an incentive bonus of up to $4,000 per quarter, provided that he meets his sales goals. At the end of the quarter, he has met enough of his target to earn a $1,500 bonus, which he receives on his next paycheck. This meets the DOL standard.

- 10% of $ 47,476 equals $4,748 (the maximum bonus than can be used as part of minimum annual salary under the DOL's new rules)
- $4,748 divided by 4 equals $1,187 (the minimum that must be paid quarterly)
- $1,500 is well within the minimum bonus to offset the wage differential for this quarter

The extra $313 will also reduce the annual $4,748 liability and reduce the next quarter's minimum "must pay bonus" to $874).

Example 2: The use of commission to offset minimum salary.

Jane Dresser manages a women's clothing store. Her base salary is $833 a week, or $80 a week short of the minimum $913 a week required by the DOL. In addition to her exempt duties managing the business and staff of the store, Jane earns a commission on all garments she personally sells. In January, a slow month for the store, Jane earned only $75 a week in commission. February picked up and she earned $100 a week. March was clearance month so again, her commission dropped to $75 a week. Still, the commission from the three months made up the difference between her salary and the DOL required minimum salary:

- Jane's base salary is $43,316 ($833 x 52 weeks)
- Jane needs to make $4,160 in commissions in a year to make up the shortfall ($47,476 - $43,316)

- Her quarterly commission must be no less than $4,160
- Jane's commission for January through March is $1,075
  [$75 x 4 weeks in January] + [$100 x 4 weeks in February] + [$75 x 5 weeks in March]

In both examples, even though Jane and John made less than the $913 weekly minimum salary, their quarterly bonus and commission made up the difference. If either employee did not earn enough from the nondiscretionary bonus or commission payment in that quarter to meet the standard salary level, their employer may make a "catch-up" payment within one pay period of the end of the quarter. Any such "catch-up" payment would count only toward the prior quarter's salary amount and not toward the salary amount in the quarter in which it is paid.

What if we want to continue to pay all of our employees on a salary basis, even though they may not be "exempt" under the duties test of the DOL?

One of the most common misconceptions about the FLSA is that "salaried" is the same as "exempt." Paying someone a salary does not make them exempt nor does it make them ineligible for overtime. Employers may continue to pay all employees on a salary basis and nonexempt employees can certainly be paid less than $913 a week. This does not, however, release employers from their obligation to track and record all hours worked by nonexempt staff. Some considerations for paying nonexempt staff on a salary basis:

- If an employer has a good understanding of the number of actual hours a nonexempt employee works, the employer can describe the employee's overall compensation as a combination of regular pay plus overtime for a finite number of hours.

  For example: The Widget Company has been paying its (nonexempt) receptionist $855 a week. The company knows that the receptionist almost always works 42 hours a week to cover the switchboard during the hours it is open. The company also knows that, on at least two days, she eats at her desk because there is no lunch coverage for that half hour. The employer then knows that the receptionist works 40 regular hours and three overtime hours. In order to maintain her on a salary basis, The Widget Company might communicate to her that her salary is comprised of 40 hours at $18.00 an hour and five hours of estimated overtime (building in a buffer). The overtime component of her pay is five hours at time-and-a–half, or $135 ($27 x 5). The Widget Company would still be responsible for paying overtime if the receptionist worked more than 45 hours.

- Another method of compensating employees is on a fluctuating workweek basis. Under this method of payment, the non-exempt employee receives a guaranteed base salary each week regardless of the hours worked. Using this method:

  1. The employee must be paid a salary, which is a "fixed amount" regardless of how many hours are worked in a given week.

  2. The employee and employer must have a "clear mutual understanding" that the fixed salary is compensation for all hours worked in a week regardless of how many hours are worked in any given week.

  3. The weekly salary must be large enough such that the employee's hourly rate never falls below minimum wage.

4. The employee's hours must fluctuate from week to week.

This a good method to use for employees who may work 30 hours one week but 50 the next. There is still an obligation for overtime if the hours worked cause the hourly rate to drop below minimum wage and the employer is still required to track time worked.

7/29/16