U.S. Department of Labor
Wage and Hour Division

U.S. Wage and Hour Division
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Fact Sheet 17U: Nondiscretionary Bonuses and Incentive Payments (Including Commissions) and Part 541 Exempt Employees

Section 13(a)(1) of the FLSA provides an exemption from the federal minimum wage and overtime pay requirements for employees employed as bona fide executive, administrative, professional, and outside sales employees. These exemptions are sometimes referred to collectively as the "white-collar" exemptions, and are defined in the Department's regulations located at 29 C.F.R. Part 541. To qualify for one of these exemptions, employees generally must (1) be paid a predetermined and fixed salary that is not subject to reduction because of variations in the quality or quantity of work performed ("salary basis test"); (2) be paid at least a specified weekly amount ("salary level test"); and (3) primarily perform executive, administrative, or professional duties as defined by the regulations ("duties test"). Job titles alone do not determine exempt status, and neither does the receipt of a particular salary. In order for an exemption to apply, an employee's specific job duties and earnings must meet all of the applicable requirements.

The Department revised the regulations located at 29 C.F.R. Part 541 and issued a Final Rule on September 27, 2019 with an effective date of January 1, 2020. The Final Rule sets the standard salary level at $684 per week (or $35,568 annually for a full-year worker). The Final Rule also sets the total annual compensation level for highly compensated employees (HCE) at $107,432.

Under the Final Rule, employers may use nondiscretionary bonuses and incentive payments (including commissions) to satisfy up to 10 percent of the standard salary level. Such payments may include, for example, nondiscretionary incentive bonuses tied to productivity and profitability. For employers to credit nondiscretionary bonuses and incentive payments toward a portion of the standard salary level, the Final Rule requires such payments to be paid on an annual or more frequent basis and permits the employer to make a "catch-up" payment at the end of each 52-week period.

Up to 10 Percent of the Standard Salary Level

Employers may satisfy up to 10 percent of the standard salary requirement ($68.40 per week) with nondiscretionary bonuses, incentive payments, and commissions. Each pay period an employer must pay the exempt executive, administrative, or professional employee on a salary basis at least 90 percent ($615.60 per week) of the standard salary level. The remaining portion of the required salary level (up to 10 percent) may be fulfilled through payment of nondiscretionary bonuses or incentive payments so long as the payments are paid at least annually. The Department recognizes that some businesses pay significantly larger bonuses; where larger bonuses are paid, however, the amount attributable toward the standard salary level is limited to 10 percent of the required salary amount for the workweek. Note that this does not mean bonuses are capped. It only means that the amount an employer may credit against the weekly standard salary level is limited to 10 percent of the required salary amount.

Example

Employee A meets the duties test for an executive employee. Employee A receives a salary of $616 per week and two production bonuses; $1300 in June and $2500 in December. As a result, Employee A's total salary for the year is:

$616 (salary) x 52 weeks = $32,032 amount paid in salary on a weekly basis.

$32,032 (salary paid) + $3,800 (Bonuses earned) = $35,832 (salary plus nondiscretionary bonuses paid).

Employee A received $616 per week on a salary basis, which exceeds $615.60 (90 percent of the standard salary level required). Employee A's salary and nondiscretionary bonuses total $35,832, which exceeds the standard salary level of $35,568 ($684 x 52 weeks) for that period. Because the employee meets the duties test for an exempt executive and met the salary level requirements, Employee A is exempt from overtime pay for the year.

U.S. Territories with Special Salary Levels

Employers may similarly use nondiscretionary bonuses, incentive payments, and commissions to satisfy up to 10 percent of the special salary levels for certain U.S. territories. Under the Final Rule, the Commonwealth of the Northern Mariana Islands, Guam, Puerto Rico, and the U.S. Virgin Islands have a special salary level of $455 per week. Thus, nondiscretionary bonuses, incentive payments, and commissions paid at least annually can be used to satisfy up to $45.50 of the weekly salary level in these territories. American Samoa has a special salary level of $380 per week. Thus, nondiscretionary bonuses, incentive payments, and commissions paid at least annually can be used to satisfy up to $38 of the weekly salary level in American Samoa. See Fact Sheet #17T.

Catch-Up Payment

If at the end of the 52-week period the sum of the salary paid plus the nondiscretionary bonuses and incentive payments (including commissions) paid is less than the required salary level, the employer has one pay period to make up for the shortfall for the 52-week period. Any such catch-up payment will count only toward the prior 52-week period's salary requirement and not toward the 52-week period's salary requirement in which it is paid. If the employer chooses not to make the catch-up payment, the employer will not have met the salary requirement for the preceding year, and the employee would be entitled to overtime pay for any overtime hours worked during the previous 52-week period.

Example

Employee B meets the duties test for the professional exemption and is paid a salary of approximately 90 percent of the standard salary level ($616) in each workweek for the year. At the end of the year, the employer tallies Employee B's nondiscretionary bonuses and commissions for the year, which amount to $3,300.

$616 (salary) x 52 weeks = $32,032 amount paid in salary on a weekly basis.

$32,032 (salary paid) + $3300 (bonuses earned) = $35,332 (salary plus nondiscretionary bonus paid).

Employee B must be paid a total of $35,568 per year to meet the salary level requirement ($684 x 52 weeks). Because the total of salary and bonuses paid ($35,332) is less than $35,568, the employer must, within one pay period, make a catch-up payment to Employee B to meet the salary level requirement in order to maintain the exemption. As shown below, the amount of the catch-up payment is $236.

$35,568 (required salary for 52 weeks) – $35,332 (total paid) = $236 (required catch-up payment).

If the employer does not make the catch-up payment, the employee is entitled to overtime pay for any overtime hours worked during the previous 52-week time period.

Discretionary versus Nondiscretionary Bonuses

As noted above, effective January 1, 2020, employers will be able to use nondiscretionary bonuses to satisfy up to 10 percent of the standard salary level. Promised bonuses such as those announced to employees to induce them to work more efficiently or to remain with the firm are considered nondiscretionary. *See* 29 C.F.R. 778.211(c). Examples include bonuses based on a predetermined formula, such as individual or group production bonuses, bonuses for quality and accuracy of work, retention bonuses, and commission payments based on a fixed formula.

Conversely, employers may not use discretionary bonuses to satisfy any portion of the standard salary level. A discretionary bonus is one in which the employer retains "discretion both as to the fact of payment and as to the amount until a time quite close to the end of the period for which the bonus is paid." 29 C.F.R. 778.211(b). The amount of a discretionary bonus is "determined by the employer without prior promise or agreement." *Id.* For example, a surprise holiday bonus is considered a discretionary bonus.

Nondiscretionary Bonuses for Highly Compensated Employees

The white-collar regulations contain a special rule for highly compensated employees (HCE) who pass a minimal duties test. Under the Final Rule, to be exempt as an HCE, in addition to passing the HCE duties test, an employee must receive total annual compensation of at least $107,432 and must also receive at least the new standard salary amount of $684 per week on a salary or fee basis.

The Department has not made changes to how employers may use bonuses to meet the salary level component of the HCE test. While nondiscretionary bonuses and incentive payments (including commissions) may be counted toward the HCE total annual compensation requirement, *see* 29 C.F.R. 541.601(b)(1), the HCE test does not allow employers to credit these payment forms toward the standard salary level component of the HCE test. HCEs must receive at least the full standard salary level amount ($684 per week) each pay period on a salary or fee basis without regard to the payment of nondiscretionary bonuses and incentive payments.

Example

Employee C is compensated at $111,000 annually and customarily and regularly performs at least one or more of the exempt duties or responsibilities of an executive, administrative, or professional employee. Employee C must be paid at least $684 per week on a salary or fee basis in order to meet the HCE exemption. Nondiscretionary bonuses and incentive payments cannot be used to reach the $684 per week amount but can be used to satisfy the total annual compensation requirement. If Employee C receives a salary of $1,500 per week and nondiscretionary bonuses and commissions over the year totaling $33,000, Employee C is an exempt highly compensated employee.

Effective Date

The effective date of the Final Rule is January 1, 2020.

For additional information, visit our Wage and Hour Division Website: www.wagehour.dol.gov and/or call our toll-free information and helpline, available 8 a.m. to 5 p.m. in your time zone, 1-866-4-USWAGE (1-866-487-9243).

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