



July 9, 2003

FLSA2003-5

Dear **Name***,

This is in response to your request for an opinion as to whether a particular compensation system you described complies with the "salary basis" test required for exemption as an executive, administrative or professional employee under the Fair Labor Standards Act (FLSA) pursuant to 29 C.F.R. § 541.118.

Your request relates to a client that is one of the nation's largest producers of energy. The client is considering acquiring power plants and related facilities that engage in compensation practices as described below. The potential acquisitions (the "Company") involve regulated utilities that typically operate 365 days per year and 24 hours per day.

Some of the Company's exempt employees work rotating 12-hour shifts. Other exempt employees work eight-hour shifts. The exempt employees are paid an annual salary computed on a biweekly basis at rates that exceed the minimum amount required by 29 C.F.R. Part 541 (e.g., more than \$250 per week). The Company also pays additional compensation, often referred to as "overtime," to many of its exempt employees at the straight-time rate for hours worked in excess of 40 per week. Exempt employees typically are provided with sufficient information based on their annual salary in order to calculate their hourly pay rate in the event that they perform overtime or premium-time work.

The Company has a formal, written pay policy that states that employees may be required to record and report their time and associated tasks each week. This is so for two principal reasons. First, when a Company is regulated, it is usually important for rate-making purposes to know the amount of time each exempt (and non-exempt) employee devotes to various tasks. Second, when a Company has voluntarily elected to provide overtime or premium pay to exempt personnel, those employees must account for their regular as well as their overtime hours each week.

Exempt and non-exempt employees may use the same time-entry codes when they enter their time. For example, using these codes, employees can report time as regular-time, overtime, or premium-time work. Employees also can report time away from work as vacation, sick, jury/military duty, or personal leave, among other things.

The payroll system generates biweekly pay checks for all employees. In order to be paid, each employee must enter the employee's time into the system either directly or through a timekeeper. In some cases, employees may be paid initially only for the amount of time entered on employee time-sheets, and according to the pay code they select to describe that time, such as regular-time, overtime, premium time, or vacation leave.

Employee time-entry errors or omissions may occur. For example, exempt employees may under-report their time. In such circumstances, such errors or omissions may result in an initial payment to employees of less than 1/26th of their annual salary. The Company has a pay adjustment process for correcting employee time-entry errors or omissions. Moreover, the Company's formal, written pay policy expressly prohibits partial day dockings and exempt employees are expected to report at least 80 hours of time each biweekly pay period.¹

In requesting my opinion, you asked that I assume that the "duties" test requirements of the exemption provisions are satisfied. You also asked that I assume that, under the compensation system, reductions in pay may occur as the result of time-entry errors or omissions and not as the result of a variation in the

¹ The Company may also pay employees monthly. The analysis contained in this letter is the same for employees paid monthly as for those paid biweekly. Exempt employees are paid on a weekly or less frequent basis. 29 C.F.R. § 541.118(a). See also 29 C.F.R. § 541.117(a) (indicating required salary amounts for biweekly, semimonthly, and monthly periods).



quantity or quality of work performed by an employee, e.g., due to partial day absences, a shortage of cash, a shortage of work, jury/military duty, discipline, etc.

Before generalizing on this compensation plan overall, we caution that, because of the structure and wording of the exemption tests, they must be applied employee-by-employee. Determining the exempt status of any particular employee requires considering the specific conditions of the actual employment experience of each individual employee who must be evaluated under all the applicable tests.

If a pay system compensates employees who are claimed to be exempt on the basis of hourly wage rates computed from their actual hours worked each week, it is necessary to determine whether a salary guarantee is in effect and operational. Payment on an hourly basis without an operative salary guarantee does not qualify as a "salary basis" of payment within the meaning of the regulations. See, e.g., Brock v. Claridge Hotel and Casino, 846 F.2d 180, 184-85 (3d Cir. 1988) (purported guaranteed "salary" did not amount to payment on a salary basis because it bore "no relation to the method of paying the supervisor," the guaranteed minimum payment was unrelated to the employee's income and compensation correlated to and depended upon the number of hours each employee worked); and Martin v. W.E. Monks & Co., 805 F. Supp. 500, 505 (S.D. Ohio 1992) (employees were not paid on a salary basis because they did not receive any guaranteed salary, they were paid less than a full period's pay when they worked less than forty hours in a week, were paid less for days when they worked less than a full day, and the pay policy correlated the employees' pay amount to the hours the employees worked), aff'd, 1 F.3d 1241 (6th Cir. 1993).

Your letter, however, indicates that the exempt employees are guaranteed that they will be paid at least 1/26th of their annual salary every other week. Accordingly, based on our review of the Company's compensation system you described, it is our opinion that it meets the salary basis requirements of 29 C.F.R. § 541.118, subject to the following discussion.

The salary basis requirement of the FLSA allows employees to enter and describe their time on a weekly basis to generate a biweekly paycheck equal to at least 1/26th of their annual salary. Employees paid according to a pay plan under which they are, in fact, guaranteed to receive no less than 1/26th of their annual salary each biweekly pay period, except for deductions otherwise expressly permitted by 29 C.F.R. § 541.118 (e.g., employee personal absences for a full day or more), are paid on a "salary basis" within the meaning of the regulations. Provided that employees regularly receive each biweekly pay period under the employment agreement no less than 1/26th of their annual salary (except those deductions expressly permitted), their exempt status is not affected by the actual number of hours that are entered for a particular pay period or for each separate week within that pay period, or by how the time is described when it is entered into the payroll system (e.g., regular time, overtime, holiday pay, sick leave, personal leave or other codes). In other words, the tracking or accounting of actual hours worked by exempt employees does not violate the "salary basis" requirements. See, e.g., Douglas v. Argo-Tech Corp., 113 F.3d 67, 71 (6th Cir. 1997); Renfro v. Indiana Michigan Power Co., 233 F. Supp. 2d 1174, 1182 (W.D. Mich. 2002); Schaefer v. Indiana Michigan Power Co., 197 F. Supp. 2d 935, 940-41 (W.D. Mich. 2002); and Cooke v. General Dynamics Corp., 993 F. Supp. 50, 53-55 (D. Conn. 1997).

An employee's time-entry error or omission or other clerical or mechanical error or omission that results in an initial payment by the Company to an employee of less than 1/26th of the employee's annual salary in a biweekly pay period is not an unlawful "docking" or deduction in the typical sense (e.g. such as a prohibited disciplinary deduction), does not call into question the Company's intention to pay on a salary basis, and does not affect exempt status. Any shortage that results from the employee's error or omission may be adjusted by completing an adjustment form (a process that is consistent with the window of correction contained in 29 C.F.R. § 541.118(a)(6)). The fact that an adjustment process exists to correct such errors indicates that any initial underpayments caused by time-entry errors, like clerical and mechanical errors, are inadvertent and may be part of any payroll system that is subject to human error.

You also ask about payment of overtime to exempt employees. "[E]xtra compensation may be paid for overtime to an exempt employee on any basis. The overtime payment need not be at time and one-half,



but may be at straight time, or at one-half time, or flat sum, or on any other basis.” Boykin v. Boeing Co., 128 F.3d 1279, 1281 (9th Cir. 1997) (quoting Wage & Hour Division Opinion Letter No. 1738 (April 5, 1995)). See also Aaron v. City of Wichita, Kan., 54 F.3d 652, 658 (10th Cir. 1995) (recording of hours on pay stubs and payment of hourly overtime are not inconsistent with payment on a salary basis).

This opinion is based exclusively on the facts and circumstances described in your request and is given on the basis of your representation, explicit or implied, that you have provided a full and fair description of all the facts and circumstances which would be pertinent to our consideration of the question presented. Existence of any other factual or historical background not contained in your request might require a different conclusion than the one expressed herein. You have also represented that this opinion is not sought on behalf of a client or firm that is under investigation by or in litigation with the Wage and Hour Division or the Department of Labor.

Sincerely,

Tammy D. McCutchen
Administrator

*Note: * The actual name(s) was removed to preserve privacy.*