

## FLSA REGULATIONS: THE IMPACT OF IMPROPER SALARY DEDUCTIONS

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(Part 3 of the Wage-Hour Compliance Series)

In this second part of our series, we explain how to avoid improper salary deductions that could destroy the overtime exemption of an employee who otherwise meets the applicable “duties test” for one of the so-called “white collar” exemptions.

The federal Fair Labor Standards Act (“FLSA”) exempts *bona fide* executive, administrative and professional employees from its minimum wage, overtime and timekeeping requirements. U.S. Labor Department regulations further subdivide these exemptions into categories for certain computer professional employees and certain highly compensated employees meeting particular requirements. One requirement for most of these exemptions is that the employee must be paid at least in part on a “salary basis”.

Currently, the minimum salary amount for most of these employees is \$455 per week. However, the amount of the employee’s salary is not the only requirement. The **way in which the employee is paid also is important.**

**Being paid on a “salary basis”, means that the employee receives a pre-determined amount of compensation each pay period that is not subject to reduction (due to variations in the quality or quantity of the employee’s work).**

Subject to certain exceptions, the employee must receive *his or her full salary* for every workweek in which the employee performs any work, without regard to the number of days or hours worked. In most circumstances, salary deductions may not be made for absences occasioned by the employer or by the employer’s operating requirements for time when work is not available or for reasons of work quality.

There are specific rules covering whether and under what circumstances the employer can deduct from an exempt employee's salary based on the quantity or quality of his or her work. U.S. Labor Department, FLSA regulations, allow salary deductions for:

- *Proportional deductions for whole-day absences due to personal reasons other than sickness or disability.*
- *Proportional deductions for whole-day absences due to sickness or disability (including work-related accidents) if this is done in accordance with a bona fide plan, policy or practice providing compensation for salary loss due to such sickness or disability.*
- *Offsets against the salary for any amounts received by the employee as jury fees, witness fees or military pay for the particular workweek.*
- *Salary deductions made as penalties imposed in good faith for infractions of safety rules of major significance.*
- *Salary deductions made for unpaid disciplinary suspensions of one or more full days imposed in good faith for infractions of workplace conduct rules. This encompasses suspensions imposed under written policies applicable to all employees regarding serious work-related misconduct such as sexual harassment, violence, drug or alcohol violations or violations of the law.*
- *Paying a proportionate part of the employee's full salary for the time actually worked in the first workweek of employment or in the last workweek of employment.*
- *Paying a proportionate part of the employee's full salary for the time actually worked in the workweek when the employee takes unpaid leave under the federal Family and Medical Leave Act.*

Deductions for absences not fitting within the above rules can be made from a vacation allowance, a sick leave bank, other paid-time-off ("PTO") account, and so on without undercutting the salary basis, provided that the employee still receives his or her full salary amount (even after the PTO allotment is exhausted).

## ***THE IMPACT OF IMPERMISSIBLE DEDUCTIONS***

So what happens if an **employer makes improper salary deductions from exempt employees?** The answer depends on a variety of considerations, starting with what the facts show about whether the employer did or did not intend to pay the employees on a salary basis.

The U.S. Labor Department says that an “actual practice” of making improper salary deductions demonstrates that the employer did not so intend and that the exemption is lost. Among the factors relevant to this question are:

- The number of improper deductions, particularly as compared to the number of similar instances in which a deduction might have been made
- The time period over which the deductions were made
- The number and location of the affected employees
- The number and location of managers responsible for the deductions
- Whether there is a clearly communicated policy permitting or prohibiting improper deductions

An actual practice of making improper deductions causes the exemption to be lost (a) during the timeframe in which they were made (b) for employees in the same job classification and (c) working for the same managers responsible for the actual deductions.

It is possible to avoid this outcome in some circumstances. For one thing, improper deductions which are only isolated or inadvertent will not cause the exemptions to be lost if the employer reimburses the employees affected.

The exemptions can also be salvaged under a “safe harbor”. This protection is available if:

- The employer has in place a clearly communicated policy prohibiting the improper pay deductions specified in the general salary basis rule
- This policy includes a complaint mechanism through which employees can bring to the employer’s attention deductions that they believe to have been impermissible
- The employer undertakes to investigate such complaints and, upon concluding that improper deductions were made, both reimburses the employees and makes a good-faith commitment to comply with the salary basis rules in the future

The employer loses the safe harbor protection by failing to reimburse employees for improper deductions or by willfully violating the policy by continuing to make impermissible deductions after receiving employee complaints about them. If that happens, the exemptions probably will be lost during the timeframe over which they were made for employees in the same job classification working for the same managers responsible for the actual improper deductions.

Employers can improve wage-hour compliance, and bolster potential defenses, by adopting and publishing such a safe harbor policy.

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