Can A Salary "Build-In" Overtime Pay?

Insights
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One approach to the coming changes in the federal Fair Labor Standards Act's Section 13(a)(1) exemptions would be to abandon exempt status for at least some employees.

Of course, this will mean (among other things) that affected employees must receive the required FLSA overtime compensation for their hours worked over 40 in a single workweek. Some employers will probably contemplate paying such employees weekly salaries that "build-in" overtime compensation for up to a particular number of overtime hours.

As an illustration, assume that Tom's employer will no longer treat him as exempt once USDOL's revisions take effect, but management still wants to pay him a weekly salary.He always works between 40 and 45 hours in a workweek, unless he is sick, is off for a holiday, or takes vacation.

Tom's employer determines that the hourly equivalent of his current salary is $16 an hour.Management keys his new weekly salary to a 45-hour workweek, setting it at $760 [($16 × 40 ST hrs.) + ($16 × 1.5 × 5 OT hrs.)].If Tom works up to 45 hours in a workweek, he receives $760.If he works more than 45 hours in a workweek, he receives additional pay at a rate of (1.5 × $16) = $24 an hour for the extra worktime.

While this makes sense in many ways, it does not comply with the FLSA.

Fundamentals Must Be Observed
The FLSA does not require that non-exempt employees be paid on an hourly basis.They can instead be paid on a salary-plus-overtime basis.

But a bedrock FLSA principle is that overtime compensation must ultimately be based upon a rate-per-hour, that is, upon the "regular rate" of pay. This is usually computed by dividing an employee's total workweek remuneration by the total number of hours worked in the workweek for which that compensation was paid.*See*, *e.g.*, 29 C.F.R. § 778.109.In almost every situation, FLSA overtime pay must vary as the number of overtime hours worked varies.

In the hypothetical, Tom's pay for his hours worked between 40 and 45 in a workweek is exactly the same, whether he works one overtime hour or five.Consequently, neither the U.S. Labor Department nor a court would be likely to view *any* of Tom's $760 salary to be in the nature of overtime premium under the FLSA.

The Limited FLSA Exception

The *only* way to pay a fixed amount that includes overtime premium for varying numbers of overtime hours is to use a so-called "Belo" contract. This term comes from the 1942 U.S. Supreme Court decision in *Walling v. A.H. Belo Corporation*, which approved such an arrangement. However, Congress later amended the FLSA to restrict the conditions under which this may be done.

The FLSA's Section 7(f) authorizes paying a constant sum for varying amounts of overtime work *if*:

1. The employee's duties "necessitate irregular hours of work"; *and*
2. The employee is employed under an individual or union contract specifying a regular hourly rate (of at least the FLSA's minimum wage) for hours worked up to 40 in a workweek, plus 1.5 times that specified rate for hours worked over 40; *and*
3. The contract provides for a weekly guarantee of straight-time and overtime pay, based upon that specified rate, for not more than 60 hours.

Naturally, the employee must receive additional time-and-one-half overtime compensation for FLSA overtime hours worked beyond the number on which the guarantee is based.

On its face, this exception might seem to be easy to invoke.But the typical hurdle is that many employees' duties do *not* "necessitate irregular hours of work." The requirement is generally said to be that the person's hours worked in a workweek:

- Must vary appreciably *below 40* as well as above this threshold and must do so in a significant number of workweeks; and
- Must vary because of the *work requirements themselves*, rather than due to vacations, holidays, sickness, personal reasons, scheduled time off, and so on.

USDOL says that "minor" or "insignificant" hours variations are insufficient, and that even fluctuation that is more than "occasional, minor, or insignificant" is deemed to be inadequate if it occurs "exclusively or nearly so" in hours worked over 40 in a workweek.

The circumstances of Tom's work, which are by no means unusual, do not "necessitate irregular hours of work" within the parameters of these descriptions.

The Bottom Line

Adequate variation in hours worked is not the only requirement for, or potential pitfall of, a Belo plan. Suffice it to say that employers should move slowly and carefully in evaluating whether such a compensation method will pass muster under their particular circumstances.

It could also be that the applicable overtime requirements of another jurisdiction will *not* permit these plans, even in situations in which the FLSA will.

There are many alternative ways to compensate non-exempt employees consistently with the FLSA, but pay plans like these are unlikely to provide a reliable answer for most employers.