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Calculating Overtime Pay: Using the Fluctuating Workweek Method Can Save Employers Money

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It is well known that salaried executive, administrative and professional employees are exempt from having to be paid overtime when they work more than 40 hours a workweek. There are, however, categories of salaried employees who work considerable amounts of overtime but are not exempt, or whose categorization as exempt would be questionable. In some cases, these individuals have technical skills or other qualifications that warrant a substantial salary. Therefore, paying them at the standard overtime rate (one and one-half times their regular rate of pay for all hours worked over 40 in a workweek) can amount to a lot of money.

There is, however, a lawful means by which employers can pay this category of employees significantly less in overtime. Under the fluctuating workweek method, the employee's salary is set at a fixed amount, regardless of how many hours he or she works in a week. The time worked can vary above and below 40 hours per workweek, but the salary itself does not change. The concept is that by being paid a fixed amount for all hours worked, the employee is already being paid for hours worked over 40 at straight time. Therefore, the only additional compensation that the employee is entitled to is one-half (not one and one-half) the regular rate of pay for hours worked over 40 during a workweek.

Calculating the Savings

To understand the potential savings, consider a non-exempt employee who earns an annual salary of $52,000 ($1,000 a week). Using the conventional method of calculating overtime, that employee would be paid by calculating his or her regular hourly rate for the workweek ($1,000 / 40 hours = $25 an hour) and multiplying the hours worked over 40 by one and one-half times that rate ($25 x 1.5 = $37.50 an hour), as illustrated in the following chart:

Hours Worked	Regular Rate	Overtime Rate	Week's Compensation
40	$25.00	No overtime	$1,000.00
50	$25.00	$37.50	$1,375.00
60	$25.00	$37.50	$1,750.00

Take the same facts, except assume there is a mutual understanding that the employee makes $1,000 a week regardless of how many hours he or she works. Under the fluctuating workweek method of calculation, the employee would be paid as follows:

Hours Worked	Regular Rate	Overtime Rate	Week's Compensation
40	$25.00	No overtime	$1,000.00
50	$20.00	$10.00	$1,100.00
60	$16.67	$8.33	$1,166.66

Under the fluctuating workweek method, an employee earns a correspondingly lower overtime rate as the hours worked increase. This is because when calculating overtime, the fluctuating workweek method considers that the employer has already compensated the employee for all hours worked in the week, including those hours over 40. As a result, the regular rate decreases as the employee works more hours, which causes the "half time" rate for the hours worked over 40 to also become lower. As illustrated in the chart above, when the employee works 50 hours in a week, the employer pays $275 less by using the fluctuating workweek method. Clearly, this approach can lead to substantial savings over the course of a year.

Potential Downsides

As attractive as the fluctuating workweek method might seem, there are many instances where it may not actually benefit the employer. For example, under this compensation method, the employee receives the same fixed amount even if he or she works less than 40 hours in a given week. Over time, if the employee works under 40 hours as much as or more than he or she works over 40 hours, the employer may derive no benefit from using the fluctuating workweek method. In other words, an employer saves money only if the employee is expected to work large amounts of overtime on a consistent basis.

There are also a number of requirements that must be met in order for an employer to use the fluctuating workweek method. First of all, the hours worked must actually fluctuate. If the employee is told that he or she is expected to work 50 hours each week and the amount does not vary, then the fluctuating workweek method cannot be used.

There must also be a "clear mutual understanding" that the fixed salary is compensation for all hours worked in a workweek, regardless of how many hours the employee actually works. This does not mean that a formal agreement is required, but an employer must be able to show that there was a clear and explicit communication with the employee about the compensation method being used.

Other Questions

Can the fluctuating workweek method be used if the employee never works less than 40 hours in a week? In *Urnikis-Negro v. American Family Property Service*, decided August 4, 2010, the Seventh Circuit Court of Appeals in Chicago indicated, as it had in an earlier decision, that even if the workweek only fluctuated above the statutory 40-hour maximum (rather than below it), the fluctuating workweek method still could be applied.

Is the employee's salary considered "fixed" if he or she is also entitled to additional bonuses or premiums that vary weekly pay? Some courts have taken the view that the "fixed salary" requirement for applying the fluctuating workweek method is not met if an employee's weekly earnings vary because he or she is entitled to a bonus or premium (other than overtime pay). An employer utilizing the fluctuating workweek method, therefore, should avoid offering such additional pay entitlements. By the same token, the U.S. Department of Labor does not allow an employer utilizing the fluctuating workweek method to make deductions from an employee's salary for absences in a given week, including deductions for illness, sick leave and personal business.

Although the fluctuating workweek method can save an employer money, implementation can be complex, and there are a number of rules and potential downsides to consider.

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