

NEWS & INSIGHTS

Salary shock: PTO is not part of employee salary

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Paid time off hours are not considered part of an employee's salary under the Fair Labor Standards Act (FLSA), according to a federal appeals court. The ruling has widespread implications for any employer with salaried employees and any employer considering revising their employee compensation programs.

In the employer-friendly decision, the appeals court held that deducting PTO earned by salaried employees to make up shortcomings in weekly productivity expectations does not violate federal wage laws. The decision arose in the context of a collective action brought by a full-time registered nurse employed by a home health company. At the heart of the case was the company's compensation program. That program considered its full-time nurses to be

salaried employees exempt from overtime laws but still required those employees to reach a certain number of weekly “productivity points.” When an employee worked a full workweek but did not meet the required productivity points, the company automatically deducted earned PTO to make up the difference.

The plaintiff claimed that, by deducting PTO earned by salaried employees who did not meet productivity point requirements, the employer unlawfully deducted from the employee’s compensation in violation of the FLSA. But, after analyzing the FLSA and associated regulations, the appeals court disagreed. The court concluded the company’s practice of deducting PTO from its salaried employees who fell short in weekly productivity points — and its point system in general — did not violate the FLSA because “the key question when determining the legal classification of an employee,” whether hourly or salaried, “is whether an employer made an *actual* deduction from an employee’s base pay,” according to the ruling. Because the deduction was of PTO and not from the employee’s base pay, the court reasoned that the company did not engage in an “actual practice” of salary deductions and, therefore, did not change the employees’ status from salaried to hourly.

The concept of base pay was critical to the court’s analysis. The plaintiff argued that because PTO was earned on a scheduled basis and could be converted to cash at some point, such as at separation, it should be treated as salary. In rejecting this argument, the court explained that while PTO is part of overall compensation, salary only includes the predetermined amount an employee receives at the end of a pay period. So long as an employer does not dock or decrease an employee’s salary, it does not violate the FLSA’s salary basis test, and the employer need not pay the employee an hourly rate or overtime.

This case allows employers some latitude in considering their employee compensation and performance metrics, as well as leeway in developing a compensation structure that fits its business needs. As the largest employer expense, payroll is a critical business consideration and implicates multiple complicated statutes and regulations. Having a knowledgeable partner to navigate this process and answer questions is essential. Our attorneys in [Saxton & Stump’s Labor & Employment Group](#) can assist you in developing or revising your compensation processes. Please contact [Richard L. Hackman](#), [Harlan W. Glasser](#) or [Stephen Fleury](#) based in our Pennsylvania offices or [Beth Palmer](#), [Alice Paylor](#) or [Rene Stuhr Dukes](#) based in our South Carolina office.

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