HR Insights

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Prorated Salaries

At some point, most employers will likely need to adjust a salaried employee's compensation in a process called proration. This may be necessary when an employee is newly hired or leaves the organization during the middle of a pay period. Prorated salaries can seem complex and difficult at first glance; however, understanding when an employer can prorate a salaried employee's salary and how to do so can provide peace of mind and help an organization avoid potential compliance issues.

This article provides a general overview of prorated salaries, including when to prorate a worker's salary and how to calculate it.

What Is a Prorated Salary?

A prorated salary is when an employer adjusts a salaried employee's compensation proportional to the number of days the employee worked during a specific pay period. This tends to occur when an employee is hired during the middle of a pay period, receives a pay raise or takes unpaid leave. For example, when an employee is hired during the middle of a pay period, their paycheck for that first pay period will reflect their full salary rate reduced in proportion to the days they worked.

When Can Employers Prorate Employee Salaries?

Employers may only prorate an exempt employee's salary. Nonexempt employees do not qualify for prorated salaries because they are hourly workers. Hourly employees do not receive predetermined wages since they're only paid for the hours they work. Additionally, they are eligible for overtime pay at least 1.5 times their regular rate of pay for any work performed over 40 hours in a workweek.

To qualify as an exempt employee under the Fair Labor Standards Act (FLSA), an employee must be paid at least $684 per pay period, or $35,568 annually. In addition, they must perform work that is not subject to the FLSA's overtime provisions. This generally means work that is administrative, professional or executive in nature, which is determined by the employee's job duties, not their job title.

The FLSA generally prohibits an employer from lowering an exempt employee's pay if they perform any work during a workweek. However, an employer may prorate a salaried employee's pay in the following situations:

- A salaried employee is hired or terminated in the middle of a pay period.
- An employee receives a pay increase in the middle of a pay period.
- A salaried employee takes unpaid leave during the middle of a pay period, which may include leave under the Family and Medical Leave Act in certain circumstances.
- A salaried employee receives unpaid disciplinary action.
- A salaried employee who is not entitled to paid time off (PTO) takes personal or vacation days (or an employee who is eligible for PTO elects to take unpaid PTO).
- A salaried employee is furloughed or their working hours are reduced.

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Determining a Prorated Salary

To prorate a salaried employee's salary, an employer must first determine the employee's hourly rate of pay according to their annual rate of pay. Since a salaried employee typically works eight hours per day, five days per week for 52 weeks each year, an employer can divide the employee's annual salary by 52 to determine the employee's weekly pay. For example, for an employee earning $40,000 per year and working 40 hours per week, their hourly rate of pay is $769.23 pre-tax. Employers can adjust this calculation based on how frequently they pay employees (e.g., divide by 12 to calculate an employee's hourly rate for a monthly pay period or divide by 26 for a biweekly pay period).

The employer then must calculate the percentage of work days during the specific pay period they need to pay the employee. To do this, the employer determines the total number of days in a pay period and the number of days the employee worked during the pay period. The employer then divides the number of days the employee worked by the total number of days in the pay period. This will provide the employer with the percentage of days the employee worked in the pay period. For example, if an employee who is paid weekly worked only three days in a week, to calculate the percentage of days they worked in the pay period, the employer divides three by five, which is 0.6, or 60%.

To calculate the total amount owed, the employer multiplies the employee's wages per pay period by the prorated percentage. In this example, the employee's prorated salary for the pay period would be $461.54, or $769.23 times 0.6.

When an employer must prorate an employee's salary due to a pay raise, they need to calculate the prorated amount for the employee's original and new salary, then add them together for the total prorated salary during the pay period the employee's pay raise became effective.

Takeaway

Prorating an employee's salary can seem challenging and confusing. However, by being aware of situations in which an employee's salary can be prorated and how to calculate it properly, not only can employers be confident that they're paying their exempt employees properly but also reduce potential violations of wage laws. Employers are encouraged to seek local legal counsel for specific guidance about prorated salaries.

Contact SCS Agency Inc today for more information on payroll and compensation best practices.