U.S. DEPARTMENT OF LABOR’S NEW OVERTIME RULE

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Agenda for Today

• Review of The Fair Labor Standards Act
• Review of the “White Collar” Exemptions
• Review the New Department of Labor Rule
• Tips for How to Deal with the Changes
The FLSA establishes minimum wage, overtime pay, recordkeeping, and youth employment standards covering employees in the private sector and in Federal, State, and local governments.

- Covered non-exempt workers are entitled to a federal minimum wage of not less than $7.25 per hour currently.
- Overtime pay at a rate not less than one and one-half times the regular rate of pay is required after 40 hours of work in a workweek.
Who is covered by the FLSA?
Are employees of small businesses covered?

• The FLSA does **not** specifically provide an exemption for small businesses.

• Generally, employees of **enterprises** that have an annual gross volume of sales made or business done of **$500,000** or more are covered by the FLSA.

• In addition, employees of **certain entities** are covered by the FLSA regardless of the amount of gross volume of sales or business done.
  – These entities include: hospitals; businesses providing medical or nursing care for residents; schools (whether operated for profit or not for profit); and public agencies.

• Even if an employer is not covered on an enterprise-wide basis, employees may be **individually** covered by the FLSA if their work regularly involves them in commerce between States (**"interstate commerce"**). The FLSA covers individual workers who are “engaged in commerce **or** in the production of goods for commerce.”
• The FLSA is enforced by the U.S. Department of Labor’s Wage and Hour Division.

• The FLSA covers more than 135 million workers at more than 7.3 million establishments nationwide.
Who is entitled to the minimum wage and overtime pay under the FLSA?

• Most employees covered by the FLSA must be paid the **minimum wage** (currently $7.25/hour) and **premium overtime pay** at least one and one-half times their regular rate of pay for any hours they work beyond 40 in a workweek.

• The FLSA does, however, **exempt** certain kinds of covered employees from the minimum wage and overtime requirements, including **bona fide executive**, **administrative**, and **professional employees** who qualify for the so-called “**white collar**” exemptions.
White Collar Exemptions

- Executive
- Administrative
- Professional

*also*

- Outside Sales
- Computer Employees
- Highly Compensated Employees
Three Tests for Exemption:
– Salary Basis Test
– Job Duties Test
– Salary Level Test

• Job titles do **not** determine exempt status.
• The fact that an employee is paid a salary, standing along, does **not** guarantee exempt status.
Three Tests for Exemption:

– Salary Basis Test
– Job Duties Test
– Salary Level Test
Salary Basis Test

• Employee must be paid on a *salary basis*
  – The employee regularly receives a *predetermined amount* of compensation each pay period on a weekly, or less frequent, basis.
  – The predetermined amount cannot be reduced because of variations in the *quality* or *quantity* of the employee’s work.
  – Subject to limited exceptions, an exempt employee must receive the *full salary* for any week in which the employee performs *any work*, regardless of the number of days or hours worked.
White Collar Exemption Criteria

Three Tests for Exemption:

– Salary Basis Test
– Job Duties Test
– Salary Level Test
Executive Exemption - DUTIES

- The employee’s primary duty must be managing the enterprise, or managing a customarily recognized department or subdivision of the enterprise;
- The employee must customarily and regularly direct the work of at least two or more other full-time employees or their equivalent; and
- The employee must have the authority to hire or fire other employees, or the employee’s suggestions and recommendations as to the hiring, firing, advancement, promotion or any other change of status of other employees must be given particular weight.
Administrative Exemptions - DUTIES

- The employee’s primary duty must be the performance of office or non-manual work directly related to the management or general business operations of the employer or the employer’s customers; and
- The employee’s primary duty includes the exercise of discretion and independent judgment with respect to matters of significance.

- Work “directly related to management or general business operations” includes, but is not limited to, work in functional areas such as tax; finance; accounting; budgeting; auditing; insurance; quality control; purchasing; procurement; advertising; marketing; research; safety and health; personnel management; human resources; employee benefits; labor relations; public relations; government relations; computer network, Internet and database administration; legal and regulatory compliance; and similar activities.
White Collar Exemptions: PROFESSIONAL

Professional Exemption - DUTIES

• **Learned Professional:**
  – The employee’s primary duty must be the performance of work requiring **advanced knowledge**, defined as work which is predominantly intellectual in character and which includes work requiring the consistent exercise of discretion and judgment;
  – The advanced knowledge must be in a **field of science or learning**; and
  – The advanced knowledge must be customarily acquired by a **prolonged course of specialized intellectual instruction**.

  or

• **Creative Professional:**
  – The employee’s primary duty must be the performance of **work requiring invention, imagination, originality or talent** in a recognized field of artistic or creative endeavor.
    • The requirements are generally met by actors, musicians, composers, soloists, certain painters, writers, cartoonists, essayists, novelists

• **Also**: teachers and employees practicing law or medicine
“Primary duty” means the principal, main, major or most important duty that the employee performs. Determination of an employee’s primary duty must be based on all the facts in a particular case, with the major emphasis on the character of the employee’s job as a whole.
White Collar Exemption Criteria

Three Tests for Exemption:
- Salary Basis Test
- Job Duties Test
- Salary Level Test
Currently & until December 1, 2016:
To qualify for exemption, employees generally must be paid at not less than $455 per week or $23,660 per year on a salary basis.

29 C.F.R. §541.600
Change Ahead!

• Revision to salary level rules
• Will more than double the salary level required for most “white collar” exemptions
• New rules are effective on December 1, 2016
• Last change was in 2004
NEW Salary Level Test

Effective December 1, 2016:

• To qualify for exemption, employees generally must be paid at not less than $913 per week or $47,476 per year on a salary basis.

  – From $455 to $913
  – From $23,660 to $47,476
Simplification

The simplest way to simplify the rules

– No changes to salary basis test
– No changes to the duties tests
  • No change to “primary duty” definition
– Changes only the salary level test
Bonuses and Incentives

• Bonuses and Incentive Payments
  – Change from current law
  – Employers can use nondiscretionary bonuses and incentive payments (including commissions) to satisfy up to 10% of the required salary level
    • Payments must be paid at least quarterly
Bonuses and Incentives

• Only non-discretionary bonuses count
  – Compensation to induce employees to work more efficiently or to remain with the company
  – Incentive bonuses tied to productivity or profitability, *e.g.*,  
    • a bonus based on a specified percentage of the profits generated by a business in the prior quarter
    • Bonuses for meeting set production goals, retention bonuses, and commissions based on a fixed formula

• Discretionary bonuses don’t count
  – Those at the employer’s sole discretion and not in accordance with any preannounced standards, *e.g.*,  
    • Unannounced bonus
    • Spontaneous reward for a specific act

• Annual bonuses don’t count
  – Bonuses must be paid at least quarterly
What if an employee doesn’t earn enough in nondiscretionary bonuses and incentives in a given quarter to remain exempt?

A “catch-up” payment is permitted at the end of the quarter.
• Applying the catch-up provision
  – Employer must pay the exempt employee a salary of at least 90% of the minimum salary level for each work week (90% of $913 = $821.70)
  – At the end of the quarter, if the salary plus all non-discretionary bonuses, incentive payments, commissions do not equal at least $11,869 (=25% of $47,476), employer must make up the shortfall in the very first pay period of next quarter
  – If the employer chooses not to make the catch-up payment, the employee would be entitled to overtime pay for any overtime hours worked during the quarter.
Automatic Updating

• Automatic Updating
  – Salary levels for exemptions will be updated every three years
    • Proposed regulations would have changed them annually
  – DOL will publish updated rates at least 150 days before effective date
  – First automatic revision effective January 1, 2020
Highly Compensated Employees

Employees with total annual compensation of at least $134,004 (currently $100,000) are exempt from FLSA minimum wage and overtime requirements, if they:

– Perform office or non-manual work; and
– Customarily and regularly perform any one or more of the exempt duties or responsibilities of an executive, administrative, or professional employee (a “relaxed” duties test)

• Also, the employee must receive at least $913 per week on a salary basis. Non-discretionary bonuses and incentive payments (including commissions) may be used to satisfy the remainder of the $134,004 total annual compensation requirement.

29 C.F.R. § 541.601
• Change becomes effective on December 1
• **West Virginia** law requires advance notice of changes in pay rate
  – “When an employer changes an employee’s rate of pay . . . the employer shall furnish a written notice to the employee at least 1 full pay period prior to the effective date of the change.”
    • W. Va. C.S.R. § 42-5-4.2.
• Likewise, **Maryland** law requires at least 1 pay period in advance, notice of any change in a payday or wage.
  • Maryland Code § 3-504.
A Major Change

• Broad effect
  – 4.2 million exempt employees will automatically become non-exempt
  – 5.7 million additional workers now classified as exempt but in a gray area will be reclassified as non-exempt
  – All told, will affect more than 14% of the American workforce during fiscal year 2017
A Major Change

• Big Costs
  – Will cost employers about $1.2 billion a year in “transfer of income between employers and employees in the form of higher earnings”
  – Additionally, employers will spend about $295 million in “regulatory familiarization, adjustment costs, and managerial costs”
A Major Change

• Most affected industries
  – Professional and technical services
  – Health care
  – Finance
  – Retail
  – Insurance
  – Education
Preparing for Change

• Compliance Plan
  – Get started now!
  – This involves math, and math is hard.
Preparing for Change

• Compliance Plan
  – Figure out who will need to be reclassified
  – Train your managers and new non-exempts
  – Review your pay policies
  – Consider unintended consequences
Preparing for Change

1. **Figure out who will need to be reclassified**
   - Make a list of exempt jobs paid less than $47,476
   - What will you do with exempt employees close to the salary threshold?
     - Raise their salary to the new level?
     - Convert them to non-exempt and continue paying them a salary?
       » Will the salary be lower to account for overtime?
     - Convert them to non-exempt and pay them on an hourly basis?
Preparing for Change

• Do you have a sense of how much time they are actually working?
• Will you need to limit hours or hire additional workers?
• If you have an accurate sense of the amount of time necessary for the work, you can design a compensation structure that will closely replicate the salary of formerly exempt employees.
Preparing for Change

• EXAMPLE – Possible strategies for currently exempt accountant earning $42,000 annual salary and no bonus or commission.
  – Employee works 45 hours in a workweek
  – Works 52 weeks per year
  – Primary duty is exempt work
Preparing for Change

- **Option 1**: Increase the employee’s salary by $5,476 per year. Employee remains exempt.
- **Option 2**: Reclassify the employee as non-exempt at current salary. Overtime pay will add $7,875 in labor costs.
- **Option 3**: Reclassify the employee to non-exempt with hourly rate of $17. With the expected overtime, earnings should be about the same.
• Cost-Neutral Formula (for Option 3)
  – Weekly salary/(40 + (OT Hours x 1.5))
    ($42,000/52 weeks in a year)/
    (40 + (5 OT hours per week x 1.5))

= $807.69/47.5

= $17.00/hour

Can’t I just use comp time?

- The use of compensatory time ("comp time") instead of overtime pay is limited by the FLSA to a public agency that is a state, a political subdivision of a state, or an interstate governmental agency, under specific circumstances.

- Private employers cannot satisfy their overtime obligations by providing comp time and must pay overtime-eligible employees an overtime premium for hours over 40 in a workweek.
Preparing for Change

• This is a good time to revise job descriptions
  – Duties matter, not job titles
  – Draft the job description for exempt positions to show that the position is performing exempt work
Preparing for Change

• This also is a good time for a job duties review.
  – We all have employees in the gray area
  – Regulatory change provides a rare opportunity to make changes without shining a light on the reason
2. **Train your managers and new non-exempts**
   - Remember all the added requirements that come with non-exempt employees
   - You will need to train formerly exempt employees how to keep track of their time
   - You will need to train newly non-exempt managers who are used to answering emails at all hours that they can’t do that, or at least must account for their time
   - You will need to educate newly non-exempt on wage and hour policies that might apply to them in a less flexible manner
3. **Review Pay Policies**
   - Consider how your pay and benefits policies will apply to your newly non-exempt employees.
     - Benefits eligibility
     - Mobile devices
     - Travel time
     - Off-the-clock work
4. **Prepare for Unintended Consequences**
   - Employee status perception
   - Productive exempts who may be non-productive non-exempts
Questions & Answers

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