

# **THE NEW OVERTIME RULES OF THE FAIR LABOR STANDARDS ACT: How Will New Changes Affect Your Business – Chapter One**

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This is the first in a ten-part series of articles designed to help employers avoid mistakes that may result in regulatory problems under the federal Fair Labor Standards Act.

## **A. OVERVIEW OF THE 2016 REVISIONS:**

On May 18, 2016, the Department of Labor (“DOL”) announced updated rules to the Fair Labor Standards Act (“FLSA” or the “Act”) that will ultimately result in several million employees being eligible for overtime pay due to an increase in the current minimum salary requirement for the most commonly used overtime exemptions (executive, administrative and professional). The FLSA mandates that all employees not “exempt” from overtime pay be paid overtime for all hours “actually worked” in excess of 40 in any single workweek at a rate of 1 ½ times the “regular rate” of pay. Failure to pay overtime, as well as the failure to properly calculate overtime, is a violation of the Act and may be enforced either by the DOL or through private judicial proceedings.

The FLSA regulations governing the requirements for employees to qualify for the executive, administrative or professional exemptions has been updated for the first time since 2004, when the minimum salary required for those exemptions was set at \$455 per week (\$23,660 yearly).<sup>1</sup> The overtime exemptions are designed primarily to exclude blue-collar workers and those employees who perform principally manual or repetitive work regardless of the salary paid. Therefore, these exemptions must satisfy a “Salary plus Duties” test under the Act.

- The “salary test” requires a fixed minimum salary that is not subject to reduction based on the quality or quantity of work performed each week (this will be raised from \$455 to \$913 per week as of December 1, 2016); and
- The “duties test” requires that the employee’s job duties primarily involve the specific requirements for the specific exemption relied upon (the duties tests for overtime exemptions will remain unchanged).

Higher Minimum Salary – beginning on December 1, 2016, the minimum salary requirement for an employee to qualify for the executive, administrative or professional exemption under the FLSA will be raised from the current \$455 per week to \$913 per week (\$47,476 yearly). As of December 1<sup>st</sup> any employee who does not earn at least \$913 per week cannot be exempt from overtime under the most commonly relied upon exemptions, even if the duties test requirements are met. The duties requirements, which remain unchanged by the 2016 revisions, are listed below.

Automatic Updates – the revisions also establish a mechanism for automatically updating the salary and compensation levels required for overtime exemptions every three (3) years to maintain the current percentage salary standards (where \$913 represents the 40<sup>th</sup> percentile of earnings of full

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<sup>1</sup> Although the FLSA contains several provisions that describe employees who may be exempt from overtime pay if certain requirements are met, only the three most commonly used exemptions are discussed in this article.

time salaried workers in the lowest-wage Census Regions, and \$134,004 represents the 90<sup>th</sup> percentile of full-time salaried workers nationally). This means that another revision to adjust those numbers is anticipated on January 1, 2020 based on salary trends.

Non-discretionary Bonuses – on a positive note, employers may now use a non-discretionary bonus or incentive pay plan (including commissions) to satisfy up to 10% of the new salary minimum obligation. The bonus or incentive pay may be tied to productivity or profitability, but must be paid on a quarterly or more frequent basis. However, the new regulations allow for catch-up payments to satisfy short falls to the salary level. The DOL is likely to provide more guidance on this option before the new regulations take affect.

**B. OVERTIME EXEMPTIONS (ALL REQUIRE THE \$913/WK SALARY MINIMUM):**

The duties requirements, which remain unchanged by the 2016 revisions, are listed below:

**(1) Executive Employee Exemption – Must meet salary basis test plus:**

- Primary duty is managing the enterprise, or managing a recognized department or subdivision of the enterprise;
- Must customarily and regularly direct the work of at least two (2) or more other employees or their equivalent; and
- Must have the authority to hire or fire other employees, or have his or her suggestions and recommendations as to hiring, firing, advancement, promotion or other change of status of other employees be given particular weight.

Two (2) or more employees are 2 full-timers or equivalent (Ex: 1 full time & 2 part-timers). “Particular weight” means that the individual may give a recommendation such as to hiring, firing or promotion routinely, and that the recommendation has more importance even if there is no power to make the ultimate decision.

**(2) Administrative Exemption – Must meet salary basis test plus:**

- Primary duty is the performance of non-manual office work directly related to management or general business operations of the employer or its customers; and
- Primary duty includes exercise of discretion and independent judgment with respect to matters of significance.

The employee must actually assist with running company management or operations. Independent judgment means free from immediate supervision or control such that the employee can formulate, interpret and implement policy using his or her own judgment as opposed to needing approval.

**(3) Professional Exemption (learned or creative professional) – Salary basis test plus:**

**Learned Professional**

- 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;
- Advanced knowledge in the field of science or learning; and

- Advanced knowledge customarily acquired by a prolonged course of specialized intellectual instruction.

#### **Creative Professional**

- Primary duty must be the performance of work requiring invention, imagination, originality or talent in a recognized field of artistic or creative endeavor.

This exemption generally requires higher education with a degree or the use of originality, talent, creativity, inventiveness or artistic skills acquired over a long period of time in some recognized field. This does not apply simply because of the employee's years of on-the-job skill or experience.

#### **C. HIGHLY COMPENSATED EMPLOYEES:**

The 2004 revisions to the FLSA added the Highly Compensated Employee category exemption for those employees who earn \$100,000 or more annually (at least \$455 per week as salary), and who regularly perform at least one of the duties of an exempt executive, administrative or professional employee identified in the standard tests outlined above. Under the 2016 regulations, the minimum threshold will be raised to \$134,004 per year (with a minimum salary of \$913 per week).

#### **D. TIPS FOR COMPLIANCE:**

During the months leading up to the December 1<sup>st</sup> effective date for the new FLSA rules, employers should review the current status of all employees and determine the following:

1. Are employees properly classified as exempt given the increased "salary basis test" of \$913 per week?
2. If the employees meet the salary basis test, do they meet the "duties test" required to meet either the executive, administrative or professional exemptions?
3. Do you have any highly compensated employees who may be affected by the increased salary requirement of \$134,004 per year (at least \$913 per week)?
4. Might any other exemption apply (such as outside sales or computer employees)?
5. Identify all employees who will not meet the 2016 requirements for continued status as overtime exempt, and make changes to ensure that you are in compliance. This may be accomplished by structural changes in the company, and in some cases, employees being reclassified as non-exempt from overtime.

*Please note that the information contained in this article is not designed to address specific situations, and does not include rules or regulations that apply to all states. If you have questions concerning this topic, you should consult with legal counsel of your choice to obtain advice on various fact specific matters.*

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