White Collar Workers Get a Raise

By Tina Aiken

Last month, the United States Department of Labor ("DOL") released its final rule regarding changes to the overtime threshold for the Fair Labor Standards Act ("FLSA"). Most notably, the DOL doubled the minimum salary needed to qualify for certain exemptions, from the previous level of $455 a week (or $23,660 a year) to $913 a week (or $47,476 a year).

Background. Unless an employee meets an exemption to the FLSA, the employee must be paid at least the federal minimum wage for each hour worked, and one and one-half times the employee's regular rate of pay for any hours worked in excess of forty (40) per week. The most common FLSA exemptions are the executive, administrative and professional exemptions, often referred to collectively as "the white collar exemptions." In order for an employer to validly treat an employee as exempt, the employee must, with few exceptions, meet both a duties test (perform certain duties) and a salary-basis test (be paid a fixed minimum amount per week that is not subject to reduction based on the quality or quantity of work performed).

New Regulations. The DOL's new regulations increase the weekly salary that an employee must earn to fulfill the salary-basis test of the white collar exemptions to the 40th percentile of weekly earnings for full-time salaried workers in the lowest wage region of the United States (currently $913 per week). Unlike under current regulations, employers will be permitted to use nondiscretionary bonuses, incentive payments and commissions to satisfy up to 10 percent of the new salary requirement, provided these payments are made on a quarterly or more frequent basis. While significantly increasing the salary threshold, the DOL did not issue any changes to the duties test for white collar exemptions.

The new regulations also raise the pay requirements of the "highly-compensated" exemption. Currently, employees who earn total annual compensation (including salary, commissions and nondiscretionary bonuses) of at least $100,000, and whose base salary is at least the minimum for other exempt employees, are exempt if they customarily and regularly perform at least one of the duties or responsibilities enumerated in the "white collar" exemptions tests. The new regulations raise the pay requirement for this exemption to $134,004, which is the annual equivalent of the 90th percentile of earnings of full-time salaried workers nationwide.

The new regulations also provide, for the first time in the FLSA's history, that the salary-basis threshold will automatically increase every three years, beginning January 1, 2020. The inflation adjustments will be set at the 40th percentile for the lowest-wage Census region for the white collar salary threshold and the 90th percentile for salaried workers nationally for highly compensated employees. The DOL will publish the new rates 150 days before the effective date every three years.

The new regulations take effect December 1, 2016. This is the third increase in the salary basis since the FLSA's inception in 1938. The DOL last updated the white collar overtime regulations in 2004, when the threshold value increased from $250 per week to $455.

How will the new regulations affect employers? The DOL estimates that 4.2 million currently exempt workers who earn at least $455 per week but less than the new salary level of $913 per week will become newly entitled to overtime protection. Of those, an estimated 65,000 currently exempt workers who earn at least $100,000 but less than $134,004, and who meet the minimal highly compensated employee duties test but not the standard duties test, will also become eligible for minimum wage and overtime. The Department also estimates that 5.7 million salaried white collar workers and 3.2 million salaried blue collar workers who are currently entitled to overtime will have their overtime protection strengthened because their status as overtime-eligible will be clear based on the salary test alone without the need to examine their duties. This includes an estimated 732,000 salaried white collar workers who the Department estimates are currently misclassified as exempt who will now receive greater overtime protection.

The DOL projects that the new rule will result in transferring approximately $1.2 billion in increased overtime pay annually from employers to employees over the first ten years. The Department further estimates that employers will spend nearly $300 million in corresponding administrative costs to adjust to the new regulations. There is also the added cost of a likely increase in wage and hour lawsuits being filed.

What should employers do? The new regulations give employers plenty to do over the next six months, including a handful of options to consider:

- Increase employee salaries to the new salary level and continue to treat such employees as exempt (assuming the duties requirement is met);
- Reclassify employees as nonexempt and pay overtime for hours worked over 40;
- Reduce employee hours to reduce or eliminate overtime work; and/or
- Adjust the amount of an employee's earnings to reallocate it between regular wages and overtime so that the total amount paid to the employee remains largely the same.

In addition, employers should consider taking the following actions:

- Communicate about the new regulations to employees now to prepare them for the potential impact. Let employees who could be impacted know there is a chance they may be reclassified as nonexempt.
- Reclassified employees will need to understand that they are required to record all hours worked. Employers should consider additional training for reclassified employees and their managers regarding proper timekeeping practices and procedures.
- Communicate to newly classified nonexempt employees (and remind others) that overtime without authorization is prohibited.
- Finally, employers may consider using the change in the law as an opportunity to reclassify workers who have been misclassified.

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