

Change is Coming Soon: The New FLSA Regulations

If you have been paying attention to the business news recently, you will probably be aware that there are updated regulations from the US Department of Labor relating to employers' overtime obligations that are about to take effect on December 1. These new regulations will require employers to either raise the salaries of some white collar employees who are now exempt from the overtime requirements of the Fair Labor Standards Act or to reclassify these employees as non-exempt and pay them time and a half for any hours worked in excess of 40 in any work week. The impact of the new rules will be significant: because the salary threshold has not been changed since 2004, the new threshold nearly doubles the amount a white collar worker must receive in order to remain exempt. This issue of *The Resource* will provide an overview of the new regulations and provide tips and strategies for dealing with the changes to the white collar exemptions.

The Fair Labor Standards Act

The Fair Labor Standards Act (FLSA) is the federal law that mandates the payment of a federal minimum wage and overtime pay to workers who do not fall within a specific FLSA exemption. The FLSA was signed into law by Franklin D. Roosevelt in 1938 as a part of the "New Deal" to help our nation recover from the Great Depression. As originally conceived, the law had three primary goals: to assist lower wage workers by establishing a fair minimum wage; to provide consistent wage and hour standards in order to promote fair competition among the states; and to encourage employers to hire additional workers and create jobs through the establishment of overtime pay. When first enacted, the FLSA called for a minimum wage of twenty-five cents per hour and required overtime pay for non-exempt workers after 44 hours of work in a workweek. The federal minimum wage was raised on average every 3-4 years; the last increase was in 2009, to \$7.25 per hour.

Because workers employed as bosses, managers, administrators and professionals were thought to be in charge of the workplace and better able to influence their compensation, from the outset, these so called "white collar employees" were considered to be "exempt" from the FLSA protections of minimum wage and overtime. The first regulations laid out two tests, both of which must be met in order for a worker to be covered by the white collar exemption: a "Salary Test" whereby the employee must receive a fixed minimum salary of at least thirty dollars per week, and a "Duties Test" requiring that the employee exercise real managerial or executive authority in the workplace.

The Call for Change

Over the next seven decades, the Duties Tests were refined and modified from time to time, including a major overhaul in 2004, which simplified the tests for executive, administrative and professional employees and created a relaxed Duties Test for employees receiving over \$100,000 per year in compensation. However, while the initial Salary Test threshold of \$30 per week in 1938 was 2.73 times the current minimum wage, the law did not include any mechanism for adjusting the salary threshold for the white collar exemption based on inflation or consumer pricing. Therefore, the white collar salary threshold was rarely increased--only eight times in seventy-eight years--and never indexed to inflation or the cost of living. As a result, in 2016, an employee making a salary of \$455 per week (or \$24,300 per year) could qualify as an exempt white collar worker, ineligible for overtime, even though his earnings were below the federal poverty level for a family of four.

On March 13, 2014, President Obama issued a memorandum asking the US Department of Labor (DOL) to “modernize and streamline” the existing overtime regulations to update existing protections consistent with the intent of the FLSA; to address the changing nature of the workplace, and to simplify the regulations to make them easier for both workers and businesses to understand and apply.

On July 6, 2015, the DOL issued a Notice of Proposed Rulemaking (NPRM) that would increase the white collar exemption threshold by tying it to data from the Federal Bureau of Labor Statistics and invited interested parties to submit written comments on the proposed rule by September 4, 2015. The Department received over 270,000 comments in response to the NPRM from a variety of interested stakeholders. The feedback the Department received helped shape the Final Rule.

The Final Rule

The Final Rule updating the federal overtime regulations was announced on May 18, 2016, with an effective date of December 1, 2016. Under the Final Rule, the salary threshold for executive, administrative and professional employees is set at the 40th percentile of earnings for full time workers in the lowest wage Census Region (currently the South), or \$913 per week (\$47,476 per year). The new Final Rule also establishes a mechanism for automatic updates of the salary level every three years, with the first to occur on January 1, 2020.

The Final Rule allows up to 10% of the white collar minimum salary to be fulfilled with incentive pay, such as bonuses, commissions, catch-up payments and other non-discretionary incentive pay. In order to count toward the minimum salary figure, the incentive pay must be paid at least quarterly, and, if there is a gap between the threshold and the actual pay, the employer must make it up with catch-up payments.

Under the 2004 regulations, employees paid \$100K annually were exempt if they customarily and regularly perform at least one exempt duty. The new Final Rule changed this “Highly Compensated Employee” threshold salary to the 90th percentile annualized salary for full-time salaried workers nationally, or \$134,004 annually.

The Final Rule did not change the Salary Basis Test, which will still requires that exempt white collar workers receive the same salary each week in which they perform any work without deductions for

quantity or quality of work. The Final Rule also made no changes to the Duty Tests: exempt employees must still meet the primary duties tests for the executive, professional or administrative exemptions.

Compliance with the New Rules

As was the case prior to the new Final Rule, in order to be exempt from the minimum wage and overtime provisions under the so-called “white collar” exemptions of the FLSA, an employee: (1) must be paid on a salary basis (except for highly skilled computer employees who may be paid on an hourly basis); (2) must be paid a salary that meets the current threshold as established by Federal Regulation; and (3) must perform certain designated duties consistent with an executive, administrative or professional position. The new Final Rule impacts only the salary threshold and how it is calculated and updated. Many employers will need to make no changes to how their employees are classified and compensated as a result of the new Final Rule. Only employees who are classified as exempt and who are earning less than the new salary threshold of \$913 will be affected. We anticipate that the employers that will be most impacted are those in retail, hospitality and food service industries.

In order to ensure compliance with the Final Rule, employers should first identify all employees who are classified as exempt from overtime and review how those employee are compensated. If any exempt employee is paid a salary that is less than the new threshold of \$913 per week, taking into account up to 10% in any permitted non-discretionary incentive pay, adjustments will be required on or before the December 1 effective date of the new Final Rule.

Options for compliance with regard to these affected employees include: (1) making no change to their compensation, re-classifying them as non-exempt and paying them overtime for hours worked in excess of 40 in any work week; (2) raising their salaries to meet the new threshold; or (3) adjusting their salaries so as to re-allocate pay between the regular rate for non-overtime hours and the overtime rate. Employers may also want to consider adjusting employees’ schedules, re-allocating job duties or hiring additional workers to minimize the payment of overtime to newly non-exempt workers. Employers will also need to ensure that any newly non-exempt employees’ hours are tracked and recorded to comply with the recordkeeping requirements of the FLSA.

Frequently Asked Question about the New Final Rule

Q. May some employees in a job classification that meets the duties test be exempt and others non-exempt based on salary?

A. Yes. The exemption is applied on an employee by employee basis, not based on job classification.

Q. Are employers required to pay employees on a weekly basis to meet the new standard?

A. No. Pay can be bi-weekly, semi-monthly or monthly, but overtime is determined on a week to week basis. Each work week stands alone.

Q. What are examples of non-discretionary incentive pay that can be used to satisfy the salary threshold?

A. Payments promised to the employee in advance and paid at least quarterly, such as commissions, bonuses paid on a fixed formula and incentive pay for set goals.

Q. Can a Christmas bonus be part of an employee's salary to meet the new threshold?

A. Generally, no. An unannounced holiday bonus is a discretionary bonus that cannot be used to satisfy the new salary threshold.

Q. Can a private employer provide time off at a rate of time and a half to satisfy overtime requirements?

A. No. Only public agencies such as state governments may provide comp time in lieu of overtime payments.

Q. Where can I find additional information about the FLSA and the new overtime rules?

A. A summary of the new rule, additional Q & A, fact sheets, the language of the rule itself and much more is available at: www.dol.gov/whd/overtime/final2016.

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L. Diane Tindall
dtindall@wyrick.com

Kyle R. Still
kstill@wyrick.com

Daniel J. Palmieri
dpalmieri@wyrick.com

Jenna C. Borders
jborders@wyrick.com

T. Cullen Stafford
cstafford@wyrick.com

Employee Benefits and Executive Compensation

H. Gray Hutchison
ghutchison@wyrick.com

Richard A. Rogers
rrogers@wyrick.com

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