

Final Rule for Overtime & Exempt Status

In 2014, President Obama signed a Presidential Memorandum directing the Department of Labor (DOL) to update the regulations defining which white collar workers are protected by the Fair Labor Standards Act (FLSA) minimum wage and overtime standards. The memorandum instructed the DOL to look for ways to modernize and simplify the regulations while ensuring that the FLSA's intended overtime protections are fully implemented.

On May 18, 2016, the DOL released the Overtime Final Rule. The Department concluded that the standard salary level of \$455 weekly (\$23,660 annually for a full-year employee) set in 2004 was too low. The real value of the salary level has fallen significantly since it was set 12 years ago. Today, the annualized equivalent of the standard salary level is below the 2015 poverty threshold for a family of four.

Key Provisions of the Final Rule

The Final Rule focuses primarily on updating the salary and compensation levels needed for workers to be exempt. Specifically, the Final Rule:

1. Sets the standard salary level at \$913 per week or \$47,476 annually for a full-year worker;
2. Sets the total annual compensation requirement for highly compensated employees (HCE) subject to a minimal duties test to \$134,004; and
3. Establishes a mechanism for automatically updating the salary and compensation levels every three years to maintain the levels at the above percentiles and to ensure that they continue to provide useful and effective tests for exemption.

Additionally, the Final Rule amends the salary basis test to allow employers to use nondiscretionary bonuses and incentive payments (including commissions) to satisfy up to 10 percent of the new standard salary level.

Important Note: Standard Duties Test

The Department is not making any changes to the standard duties test. The Department heard concerns from many employers, both in pre-rulemaking outreach and in comments on the proposal, that changes to the standard duties test would be disruptive to employers.

Effective Date

The effective date of the Final Rule is December 1, 2016. The initial increases to the standard salary level (from \$455 to \$913 per week) and HCE total annual compensation

requirement (from \$100,000 to \$134,004 per year) will be effective on that date. Future automatic updates to those thresholds will occur every three years, beginning on January 1, 2020.

Current Regulation Comparison with Final Rule

	Current Regulations <small>(2004 until effective date of Final Rule, 2016)</small>	Final Rule
Salary Level	\$455 weekly	\$913 weekly - 40th percentile of full-time salaried workers in the lowest-wage Census region <small>(currently the South)</small>
HCE Total Annual Compensation Level	\$100,000 annually	\$134,004 - 90th percentile of full-time salaried workers nationally
Automatic Adjusting	None	Every 3 years, maintaining the standard salary level at the 40th percentile of full-time salaried workers in the lowest-wage Census region, and the HCE total annual compensation level at the 90th percentile of full-time salaried workers nationally.
Bonuses	No provision to count nondiscretionary bonuses and commissions toward the standard salary level.	Up to 10% of standard salary level can come from non-discretionary bonuses, incentive payments, and commissions, paid at least quarterly.
Standard Duties Test	See WHD Fact Sheet #17A* for a description of Executive, Administrative, Professional (EAP) duties.	No changes to the standard duties test.

* https://www.dol.gov/whd/overtime/fs17a_overview.htm

New Overtime Rule Q&A

What determines if an employee falls within one of the white collar exemptions?

To qualify for exemption, a white collar employee generally must:

1. be salaried, meaning that they are paid a predetermined and fixed salary that is not subject

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- to reduction because of variations in the quality or quantity of work performed (the “salary basis test”);
- 2. be paid more than a specified weekly salary level, which is \$913 per week (the equivalent of \$47,476 annually for a full-year worker) under this Final Rule (the “salary level test”); and
- 3. primarily perform executive, administrative, or professional duties, as defined in the Department’s regulations (the “duties test”).

Certain employees are not subject to either the salary basis or salary level tests (for example, doctors, teachers, and lawyers). The Department’s regulations also provide an exemption for certain highly compensated employees (“HCE”) who earn above a higher total annual compensation level (\$134,004 under this Final Rule) and satisfy a minimal duties test.

How can employers implement the updated salary level requirement established in this Final Rule?

Employers have a range of options for responding to the updated standard salary level. For each affected employee newly entitled to overtime pay, employers may:

- ▲ increase the salary of an employee who meets the duties test to at least the new salary level to retain his or her exempt status;
- ▲ pay an overtime premium of one and a half times the employee’s regular rate of pay for any overtime hours worked;
- ▲ reduce or eliminate overtime hours;
- ▲ reduce the amount of pay allocated to base salary (provided that the employee still earns at least the applicable hourly minimum wage) and add pay to account for overtime for hours worked over 40 in the workweek, to hold total weekly pay constant; or
- ▲ use some combination of these responses.

The circumstances of each affected employee will likely impact how employers respond to this Final Rule. For example, employers may be more likely to give raises to employees who regularly work overtime and earn slightly below the new standard salary level, in order to maintain their overtime-exempt status so that the employer does not have to pay the overtime premium. For employees who rarely or almost never work overtime hours, employers may simply choose to pay the overtime premium whenever necessary. The Department accounted for these (and other) possible employer responses in estimating the likely costs, benefits, and transfers of the Final Rule.

Nothing in the rule requires employers to change employees’ pay to hourly from salaried, even if the employees’ classification changes from exempt to overtime eligible.

May employers use bonuses to satisfy part of the new standard salary level test?

Yes. The Department is changing the regulations to allow nondiscretionary bonuses and incentive payments (including commissions) to satisfy up to 10 percent of the standard salary test requirement. Such bonuses include, for example, nondiscretionary incentive bonuses tied to productivity or profitability (e.g. a bonus based on the specified percentage of the profits generated by a business in the prior quarter). The Department recognizes that some businesses pay significantly larger bonuses; where larger bonuses are paid, however, the amount attributable toward the Executive, Administrative, Professional (EAP) standard salary level is capped at 10 percent of the required salary amount.

For employers to credit nondiscretionary bonuses and incentive payments (including commissions) toward a portion of the standard salary level test, such payments must be paid on a quarterly or more frequent basis.

