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UPDATE: DOL ISSUES FINAL RULES DOUBLING EXEMPTION THRESHOLD

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This is an update to our May 2, 2016 Alert, "Will Your Exempt Employees Be Reclassified as Non-Exempt and Entitled to Overtime Under the Proposed FLSA Overtime Regulations?"

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Earlier today, President Obama announced the United States Department of Labor's ("DOL") changes to the Fair Labor Standards Act ("FLSA") overtime regulations (the "Final Rule"). The Final Rule significantly modifies the minimum salary thresholds for employees to be considered exempt from overtime under the FLSA and will require employers to reclassify those employees who do not meet the new minimum salary threshold as non-exempt.

The Final Rule is expected to impact 184,792 employees in Pennsylvania and 131,854 employees in New Jersey. Dilworth Paxson LLP can provide both creative solutions and the necessary documents to ensure that legal requirements are met, while still reducing unnecessary overtime expenditures.

Final Rule

The FLSA provides for certain categories of employees to be exempt from overtime due to the nature of their job and/or the amount they are paid. Part 541 of the FLSA regulations governs the overtime exemptions for executive, administrative, and professional employees (the "White Collar Exemptions") under the FLSA. Each of these exemptions previously required that an employee be paid at least \$455 per week and perform certain job duties.

The first key change in the Final Rule changes the salary threshold for employees to be considered exempt from overtime under the White Collar Exemptions to the FLSA. The Final Rule sets the base salary level for the White Collar Exemptions at the 40th percentile of weekly earnings for full-time salaried workers. ***Under the Final Rule, the base salary to be considered exempt as of December 1, 2016 is \$913 per week (\$47,476 per year) as opposed to the prior standard of \$455/per week (\$23,000 per year).***

The second key change in the Final Rule is an increase in the base salary for a "highly compensated employee" ("HCE"). Presently, HCEs are exempt from the overtime pay requirement under the FLSA if they are paid a total annual compensation of at least \$100,000. Under the Final Rule this amount would also be adjusted annually, so that the HCE base salary would be at the 90th percentile of the weekly earnings of full-time salaried workers. ***Therefore, as of December 1, 2016, the base salary exemption for an HCE will increase from \$100,000 to \$134,004 per year.***

The third key change in the Final Rule is that the salary and compensation levels will be automatically updated every three (3) years. ***The base salary level for the White Collar Exemptions will be maintained at the 40th percentile of weekly earnings for full-time salaried workers. The HCE base salary will be maintained at the 90th percentile of the weekly earnings of full-time salaried workers.***

The fourth key change in the Final Rule is ***that employers can use nondiscretionary bonuses and incentive payments (including commissions), paid at least quarterly, to satisfy up to 10% of the new standard salary level.***

What You Can Do

The Final Rule means that more employees will be classified as non-exempt and will be entitled to overtime pay. Employers have a variety of options that they may take to comply with the new overtime rule: (1) employers can keep employee salaries the same and pay overtime to employees that are newly reclassified as non-exempt; (2) employers can keep employee salaries the same and limit non-exempt employees' hours to forty (40) hours per week (which may necessitate hiring additional employees); (3) employers can increase salaries to meet the increased minimum salary thresholds (which will eliminate the need to pay those employees overtime or hire additional employees); and (4) employers may decide to lower the base wage for employees who work overtime, such that the overall pay these employees receive remains the same.

Compliance Deadline

The effective date of the Final Rule is December 1, 2016. The increase to the standard salary level to \$913 per week and the HCE total annual compensation requirement to \$134,004 per year will be effective on that date. Employers need to prepare now for these regulations to take effect. Future automatic updates to those threshold occur every three (3) years, beginning on January 1, 2020.

More On What You Can Do

Though the Final Rule has not yet taken effect, best practices suggest that employers start taking action now to prepare for its implementation. A wage and hour audit would not only capture employees' classifications, but also actual hours worked by each employee. Taking this step now will help an employer minimize unnecessary costs and ensure a smooth transition to the new regulations. A failure to act quickly and to adequately review workforce compensation could open up an employer to liability for a failure to properly classify employees and pay them appropriately. By seeking legal advice, employers will be better able to understand the Final Rule and what steps can be taken to minimize additional costs and/or decreased productivity.

If the analysis and adjustments are not undertaken beforehand, the Final Rule could seriously impact an employer's payroll, as many salaried employees that were exempt previously must now be paid overtime. For example, consider an exempt employee earning \$25,000 per year who regularly works more than forty (40) hours in a given work week. That employee, under the Final Rule, would now be classified as non-exempt, and must be paid overtime for all hours worked over forty (40).

Due to the potential problems this may cause, employers should look for creative solutions for increased overtime costs. Such solutions could include flexible schedules for non-exempt employees, based on whether the need for overtime is determined by the need for certain hours to be covered, rather than longer hours being worked. Similarly, employers may consider shift work or staggering of employee hours to reduce overtime compensation. Another alternative employers may consider is hiring part-time employees and independent contractors. In addition to providing guidance on how the proposed FLSA regulations may affect your workplace, Dilworth counsel can assist you in performing a wage and hour audit that will take into consideration the Final Rule and the alternatives to reducing its impact on your business while maintaining compliance. Because the base salary for these exemptions under the FLSA is nearly doubling, it is very important for employers to know how many hours their salaried employees are working and what duties they are actually performing. A wage and hour audit would not just address salaries and hours, but would also focus on the classification of employees into certain FLSA categories. Particularly, a July 15, 2015 memo, from the Wage and Hour Division of the DOL, provides guidance on how the DOL is now more actively reviewing the misclassification of employees as independent contractors. A wage and hour audit will help to make sure that employee classifications are in compliance with the FLSA, and will assist in ensuring compliance with the proposed regulations when they take effect in final form.

- **Marjorie M. Obod** is a partner at Dilworth Paxson LLP and Chair of its Labor and Employment Group. **Katharine V. Hartman** and **Eric B. Meyer** are also partners at the Firm and all three attorneys have counseled and defended clients in all kinds of wage and hour disputes, ranging from individual claims to class and collective actions, in matters involving: misclassification of employees as exemptions under the "white collar" administrative executive and professional exemptions; misclassification of workers as independent contractors; failure to pay for alleged pre- and post- shift "off the clock" activities for non-exempt employees; improper calculation at the regular rate; improper tip credit and tip sharing and "service charge" practices; and other pay practice irregularities under state strategy and common laws. Eric Meyer's blog, *The Employer Handbook*, discusses the Final Rule here: <http://www.theemployerhandbook.com/2016/05/new-dol-overtime-rules-youve-got-hr-questions-answers.html>