

DEPARTMENT OF LABOR: NEW OVERTIME RULE

EFFECTIVE DECEMBER 1, 2016

NAR LEGAL AFFAIRS DEPARTMENT
July 2016

The Department of Labor recently issued its [final rule](#) amending the Fair Labor Standards Act (“FLSA”) regulations related to the FLSA’s exemptions from minimum wage and overtime pay requirements (“Final Rule”). Effective December 1, 2016 (“Effective Date”), employers must meet increased minimum salary thresholds in order to claim either the: 1) executive, administrative and professional exemption (“EAP Exemption”); or 2) highly compensated employee (“HCE”) exemption (“HCE Exemption”).

KEY PROVISIONS:

Here are the Final Rule’s key provisions:

1) INCREASED MINIMUM SALARY LEVELS:

As of the Effective Date, the Final Rule requires the following minimum salary levels be met in order to claim the FLSA’s exemptions from minimum wage and overtime pay requirements:

EXEMPTION	MINIMUM SALARY LEVEL
EAP Exemption	\$913/week (\$47,476/annually)
HCE Exemption	\$134,004/annually

The Final Rule does not impact an employer’s ability to continue to pay a computer employee an *hourly* salary of \$27.63 under the [Computer Professional Exemption](#). However, if an employer pays a computer employee on a *salary* basis, the new minimum salary level of \$913 a week would apply. In addition, and for purposes of clarification, the new minimum salary level of \$913 a week applies to the [Learned Professional and Creative Professional Exemptions](#).

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These new minimum salary levels represent a significant increase to the FLSA exemptions' requirements, which prior to the Final Rule, were set at \$455 a week (\$23,660 annually) for the EAP Exemption and \$100,000 annually for the HCE Exemption.

2) AUTOMATIC UPDATES TO MINIMUM SALARY LEVELS:

The Final Rule provides that the minimum salary levels shall be automatically updated every three years, beginning on January 1, 2020. The Department of Labor will provide 150 days' prior notice of the new minimum salary thresholds.

3) NONDISCRETIONARY BONUSES, PAYMENTS AND COMMISSIONS:

The Final Rule allows employers to use nondiscretionary payments, bonuses and commissions (collectively, "Nondiscretionary Payments"), to satisfy the minimum salary level requirements. Here is a breakdown of how employers can use Nondiscretionary Payments to satisfy the minimum salary levels:

EXEMPTION	NONDISCRETIONARY PAYMENTS
<u>EAP Exemption</u>	<ul style="list-style-type: none">• May satisfy up to 10% of the minimum salary level.• Must be made at least quarterly.
<u>HCE Exemption</u>	<ul style="list-style-type: none">• May satisfy any portion of the minimum salary level.• No frequency requirement.

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It is important to understand that Nondiscretionary Payments are forms of compensation that are promised to employees, and are not payments made in the employer's sole discretion. For example, commissions and bonuses paid to induce employees to work more efficiently or to stay with the company may be Nondiscretionary Payments. A holiday bonus, which is paid in an employer's sole discretion, would be considered a discretionary payment.

While there is no cap on the amount of Nondiscretionary Payments that can be made to satisfy the HCE exemption's minimum salary level, an employer must always pay a HCE no less than \$913 dollars a week. Provided the employer meets this weekly requirement, the employer can choose to make up the remainder of the HCE's minimum salary level through Nondiscretionary Payments. While the Nondiscretionary Payments made to a HCE can be made in any frequency, the employer must meet the minimum salary level no later than the first pay period of the following calendar year.

ADDITIONAL CONSIDERATIONS:

The minimum salary level test is only one of the factors in determining whether an employee is properly classified as exempt under the FLSA. In addition to the minimum salary level test, the employee must meet the: 1) salary basis test, which means that the employee is paid a fixed, predetermined salary that is not subject to reduction based on the quality or quantity of the employee's work ("Salary Basis Test"); and 2) duties test outlined in the [EAP Exemption](#) and the [HCE exemption](#) ("Duties Test"). The Final Rule did not make any changes to either the Salary Basis Test or the Duties Test.

NEXT STEPS:

In anticipation of the Final Rule's Effective Date, employers should begin taking stock of its employees who are currently classified under either the EAP Exemption or the HCE Exemption. Provided these employees meet the Salary Basis Test and the Duties Test for such exemptions, an employer may continue to classify these employees as exempt as long as such employee meets the Final Rule's new minimum salary level test.

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If any of these employees' salaries fall below the new thresholds, employers have the option of either raising such employee's salary to meet the increased minimum salary levels, or an employer may choose to reclassify the employee to a non-exempt status. Remember, claiming an exemption under the FLSA is optional.

If an employee is reclassified to a non-exempt status, an employer is then obligated to comply with the FLSA's minimum wage and overtime payment requirements with respect to such employee. Under federal law, an employer's overtime obligations kick in for all hours an employee works over 40 hours in any given work week. In addition to the FLSA, state law may have stricter requirements when it comes to overtime pay obligations. Be sure to also consider your obligations under applicable state laws.

Under the FLSA, an employer must pay the employee at a rate of one and a half times the employee's regular rate of pay for any hours worked in excess of 40 hours. And to be clear, the overtime requirement, and corresponding hours worked, is calculated on a weekly basis.

Where employers choose to convert employees from exempt to non-exempt status, but are concerned about potential overtime payment obligations, there are a number of ways employers can reduce the amount of overtime paid to an employee. Consider using one or more of the following strategies to manage overtime obligations:

- 1) Hire additional part-time workers or contractors. Paying straight time to these workers may be less expensive than paying overtime to an employee.
- 2) Shift workloads. Assess the workloads of employees and determine if an employee on your staff with a relatively light workload may have the capacity to take on certain tasks of newly non-exempt employees, thereby freeing up the newly non-exempt employee's workday. In addition, consider shifting certain tasks to exempt employees, who are not subject to the FLSA's overtime requirements.

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- 3) Eliminate tasks. Assess whether certain required activities add sufficient value. For example, if there is a weekly staff meeting, consider whether the non-exempt staff's attendance is necessary or if there is another way to communicate any relevant information in a more time-effective manner. Also consider eliminating paid lunch breaks, which can easily convert working hours to 40 hours or less a week, thereby adding a cushion should employees occasionally work a longer day.
- 4) Manage scheduling. Manage a non-exempt employee's schedule by making scheduling adjustments to account for hours an employee may work at evening or weekend events during a given work week. Remember, any time an employee spends answering work emails or otherwise doing work-related tasks, regardless of where the employee is located, counts towards the 40-hour work week threshold.

PENALTIES:

Failure to comply with the FLSA comes at a steep price. The FLSA subjects employers to civil monetary penalties of up to \$1,100 per violation for willful or repeated violations of the FLSA, and allows an aggrieved employee to bring a private claim for: 1) back pay; 2) an equal amount in liquidated damages; and 3) reasonable attorneys' fees.

CONCLUSION:

The costly consequences of noncompliance with the FLSA make it essential that employers ensure that their employees are properly classified as exempt. In light of the Final Rule, employers should use the next several months to assess how to properly classify employees as of the Effective Date.