

Alert:

Department of Labor Announces More Stringent Test for Exemption from Overtime Pay

September 2019

The federal Fair Labor Standards Act ("FLSA") requires that non-exempt or "overtime-eligible" employees be paid one and one-half times their regular rate of pay for every hour worked over 40 hours in a workweek. For example, if an employee's regular rate is \$12 per hour, that employee must be paid \$18 per hour ($\12×1.5) for each overtime hour worked over the course of a week. Failure to properly pay for overtime work can end up costing an employer millions of dollars in back wages, penalties, and attorney fees.

Some employees, however, are "exempt" from the requirement to be paid extra when they work overtime. There are dozens of exemptions under federal law, but the most commonly-used are those for Executive, Administrative, and Professional employees--commonly referred to by the acronym "EAP" or as "white collar employees."

First, some basics: To qualify for one of the EAP exemptions, an employee must be paid on a salary basis **and** must meet the "duties" test for the chosen exemption--i.e., Executive, Administrative, or Professional. Being paid on a salary basis means receiving a fixed paycheck from which no deductions are made based on the quality or quantity of work performed in the workweek. For example, if an exempt employee's salary is set at \$1,000 or \$1,500 per week, that is the pay the employee must receive every week in order to remain exempt. This means, among other things, that the employee doesn't lose pay for partial day absences. But note that, contrary to popular belief, there is no such thing as an employee who is exempt just because he or she is salaried. ("I'm salaried, so I don't get overtime," is just another way of saying, "My employer may be breaking the law, hopefully unknowingly.") Rather, when an exemption is claimed, the employer must match each employee's actual job duties to one of the exemption tests and also comply with the appropriate salary basis test. For the same reason, there also is no such thing as the "Very Important Employee" exemption.

Since 2004, the minimum salary threshold exemption from overtime pay under federal law has been \$455 per week (\$23,660 per year). (Some states have enacted higher minimum salaries.) That means that the lowest an employer could set the salary of an employee and still claim that the employee is exempt has been \$455 per week. Effective **January 1, 2020**, the minimum salary for exemption as a white collar, or EAP, employee will increase to \$684 per week, which is equivalent to \$35,568 per year for a full-year worker.

On its face, this change affects only workers with salaries between \$455 and \$684 per week. However, there are several reasons why **all employers should take notice**.

First, any time the FLSA gets media attention, which it will now that the U.S. Department of Labor ("DOL") has announced this new rule, employees who think they are not being paid correctly start asking questions. And, there are many aggressive plaintiffs' attorneys ready and waiting to help these disgruntled

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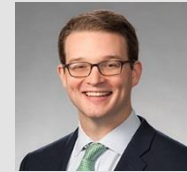


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employees. The FLSA is already the most litigated law in the federal court system, and it will not be surprising if the number of new cases increases. Therefore, every employer should be taking steps to find and correct compliance mistakes before employees and their lawyers do.

Second, the FLSA and its state counterparts are complicated laws, and many well-meaning employers are currently violating these laws unintentionally and unknowingly. One major difficulty for an out-of-compliance employer that wants to correct its practices is how to explain to employees why they are suddenly getting bigger checks. Using a change in the law as a reason to evaluate one's compliance may be the best "cover" an employer can have.

As such, there are a number of practical tips and steps employers should be considering between now and January 1, 2020.

- Don't rely on common sense to calculate your employees' pay. Instead, there is no substitute for knowing both the applicable federal law and the law of the state where your employees work. Get help as needed to understand applicable laws.
- Performing a wage-hour compliance audit now and every few years to detect problems, reduce expensive lawsuits, and help keep your company legally and financially healthy.
- Federal and state law may differ. Generally, the employee is entitled to the benefit of whichever law is more favorable to the worker.
- Overtime pay is generally one and one-half times the "regular rate," but it is not always obvious what the "regular rate" is. Commissions, bonuses, and certain other payments—even some fringe benefits—can change the regular rate retroactively. And, to complicate matters, DOL has issued proposed regulations which, if adopted, will change the "regular rate" calculation.
- Some employees may be exempt from overtime pay under federal law, state law, or both. Again, make sure you are complying with both sets of laws.
- The new regulations discussed above increase the minimum salary threshold for exemption but also relax somewhat the definition of salary, allowing employers to use nondiscretionary bonuses and incentive payments (including commissions) paid at least annually to satisfy up to 10% of the standard salary level. Make sure you understand your rights and obligations.

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