

New DOL Overtime Rules: Compliance and Litigation Prevention Tips

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Does your business have exempt employees who earn less than \$47,476 a year? If so, they will likely not be exempt for long. Beginning December 1, 2016, most workers who earn less than \$47,476 a year (just over double the current threshold amount of \$23,660) must be paid overtime unless they otherwise qualify as exempt from the Fair Labor Standards Act (FLSA). And, that threshold amount will now automatically increase every three years beginning in 2020. Misclassification of employees as exempt and the resulting failure to pay overtime serve as the basis for one of the fastest growing areas of litigation in the country. In this update, we provide the details related to the new regulations and practical suggestions for compliance and litigation avoidance.

On May 18, 2016, the U.S. Department of Labor (DOL) announced the publication of a new final rule that substantially revises existing overtime regulations to narrow the scope of overtime “exemptions,” requiring the reclassification of a large number of employees. The final rule is broadly similar to the notice of proposed rulemaking the DOL announced last year, although the DOL has made some changes to its original proposal. The DOL estimates that the new rules will require the reclassification of at least four million workers within the first year after implementation. The new rule goes into effect on December 1, 2016.

The Fair Labor Standards Act requires that most employees in the United States be paid at least the federal minimum wage for all hours worked and overtime pay at time and one-half the regular rate of pay for all hours worked over 40 hours in a workweek. However, Section 13(a)(1) of the FLSA provides an exemption from both minimum wage and overtime pay for employees employed as bona fide executive, administrative, professional and outside sales employees. Section 13(a)(1) and Section 13(a)(17) also exempt certain computer employees. A more relaxed version of these exemptions currently applies to certain “highly-compensated” individuals (those paid total annual compensation of at least \$100,000).

To be treated as exempt, most employees must satisfy both a “duties” test and a “salary basis” test: (1) the employee must have a “primary” job duty that qualifies for an exemption and (2) be paid on a salary basis at not less than specified minimum amounts summarized below. The final rule affects only the second prong, the “salary basis” test. The DOL considered making revisions to the “duties” test, but chose not to do so.

Salary Requirement Increase

Currently, the salary basis test requires (with certain exceptions) that exempt employees receive at least \$455 in guaranteed salary per week. This amount translates to an annual salary of \$23,660. The final rule increases the weekly salary requirement equal to the 40th percentile of earnings for full-time salaried workers, in the lowest-wage census region, which currently is the South. This amounts to \$913 per week or \$47,476 annually for a full-year worker.

The DOL is also changing the minimum salary necessary for a worker to qualify for the relaxed test applicable to “highly-compensated” workers. The new rule raises the total annual compensation requirement for highly compensated employees to \$134,004. This is the annual equivalent of the 90th percentile of full-time salaried workers nationally.

Certain Incentive Payments Can Now Count Toward the Minimum Salary

Under existing law, employers could count only an employee’s actual salary toward the standard salary level test. An employer could *not* count other forms of compensation, such as bonuses or commissions. The final rule changes this. Under the final rule, up to 10 percent of the salary amount can be satisfied by the payment of nondiscretionary bonuses, incentives and commissions, that are paid quarterly or more frequently.

This new rule does not impact highly compensated employees, as to whom employers could (and still can) count the employee’s *total* compensation toward the minimum salary threshold.

Automatic Salary Test Increase

The overtime regulations had not been updated since 2004. For the first time, the final rule provides for *automatic*

increases to the minimum salary requirements. Every three years, beginning January 1, 2020, the standard threshold will be raised to the 40th percentile of full-time salaried workers in the lowest-wage census region, which the DOL estimates to be \$51,168 in 2020. The automatic update will apply to highly-compensated employees as well. Every three years, the highly-compensated employee threshold will increase to the 90th percentile of full-time salaried workers nationally, which the DOL estimates will be \$147,524 in 2020. The DOL will post new salary levels 150 days in advance of their effective date, with the first such posting on August 1, 2019.

Practical Implications

The changes to the minimum salary requirement will result in extending overtime protections to millions of workers who were historically exempt. Employers must carefully review classifications for their workforce to determine what changes must or should be made in response to the final rule.

Most obviously, employers must determine whether any employees currently treated as exempt will fall below the new salary threshold. Employers should take particular care to evaluate the total compensation package for such employees, to determine whether employees currently receive other forms of incentive pay that can be counted toward the minimum salary threshold. Employers should also determine whether they can and should alter the form of incentive pay so that it can be used for this purpose, e.g., making discretionary bonuses non-discretionary or paying annual non-discretionary bonuses on a quarterly, rather than annual, basis.

But employers should also take advantage of the longer-than-expected implementation period provided by the DOL to review the classification of their workforce more deeply—and should consider doing so as part of a privileged review done by or under the direction of counsel. Although the final rule affects only the quantitative salary basis test and not the qualitative duties test, employers should not treat compliance with the new rule as a mere math exercise. The final rule has cast a bright spotlight on the issue of which workers are and can be treated as exempt. This is likely to prompt increased misclassification lawsuits brought by employees who meet the new salary threshold but perform a mix of exempt and nonexempt tasks that raise questions under the existing duties tests. Employers should consult with their wage-and-hour counsel to determine the best way to review positions that are currently treated as exempt to determine whether those positions are affected by the changes.

Read the [full text of the DOL's final rule](#). Read the DOL's [additional guidance on the final rule](#).

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