
ALERT – DEPARTMENT OF LABOR REVISES REQUIREMENTS FOR EXEMPTIONS FROM MINIMUM WAGE AND OVERTIME PAY REQUIREMENTS

1. SUMMARY

The United States Department of Labor (“DOL”) has now issued its final revisions to the Fair Labor Standards Act (“FLSA”) regulations regarding the executive, administrative, and professional employee exemptions to the FLSA’s minimum wage and overtime pay requirements. The DOL formally rescinded the 2016 revisions, which a federal judge struck down. The main changes are the increase in the minimum salary for exempt employees to \$684 per week (\$35,568 per year), an increase from the 2004 minimum of \$455 per week (the 2016 increase to \$913 per week has been invalidated). The minimum salary to qualify for exemption under the Highly Compensated Employee standard increased from \$100,000 to \$107,432. Employers may count nondiscretionary bonuses, incentives, and/or commissions towards up to 10% of the minimum salary level, as long as the amounts are paid at least annually.

The new rules become effective January 1, 2020. As of that date, employees making between \$455 - \$684 per week will no longer be exempt from overtime pay and minimum wage regulations.

Please note that many states, including California, have their own regulations regarding overtime pay and heightened minimum wage requirements.

2. BACKGROUND

In order to comprehend the rationale underlying the revisions, it is necessary to understand this issue from the Government’s perspective. Congress passed the Fair Labor Standards Act in 1938 (during the height of the

Depression). The Act was designed to guarantee a minimum wage to all workers, and overtime pay to all employees who worked over forty (40) hours per week. From the Government’s point of view, overtime pay is the *rule*, subject only to limited exceptions. This means that employers who do not pay overtime bear the burden of demonstrating that their employees fall into one of the enumerated exceptions.

The initial version of the Act exempted from overtime pay workers employed in “a bona fide executive, administrative, or professional capacity . . . or in the capacity of outside salesman.” Implementing regulations that took effect in 1940 imposed three (3) tests that the employment had to satisfy in order to be exempt from minimum wage and overtime laws:

1. the employee must be paid a predetermined and fixed salary that is not subject to reduction because of variations in the quality or quantity of work performed (the “salary basis test”);
2. the amount of salary paid must meet a minimum specified amount (the “salary level test”); and
3. the employee’s job duties must primarily involve executive, administrative, or professional duties as defined by the regulations (the “duties test”).

The rationale underlying these exemptions was that the type of work exempt employees performed was difficult to standardize to any time frame and could not be easily spread to other

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workers after forty (40) hours in a week, making enforcement of the overtime provisions difficult and generally precluding the potential job expansion intended by the FLSA's time-and-a-half (1½) overtime premium. It was also believed that the exempted workers typically earned salaries well above the minimum wage and were presumed to enjoy other privileges to compensate them for their long hours of work, setting them apart from the nonexempt workers entitled to overtime pay.

3. THE CURRENT RULES RE EXEMPTIONS TO OVERTIME LAWS

Since its enactment, Congress has expanded the Act's exemptions to include retail and service enterprises (1961), teachers and academic administrative personnel (1966), computer systems analysts, programmers, software engineers, and similarly skilled professional workers (1972). The minimum salary level for executive, administrative, and/or professional employees has been raised several times, most recently in 2004. Under the 2004 version of the Act, employees may qualify for the executive, administrative, or professional exemptions only if they make at least \$455/week. The salary requirement does not apply to outside salespersons, doctors, lawyers, or teachers.

The 2004 version of the Act creates an "Executive" exception for employees whose primary duties involve managing an enterprise or a subdivision of an enterprise; customarily and regularly directing the work of two (2) or more employees; and either hiring/firing or making hiring/firing recommendations. The "Administrative" exemption applies to employees whose duties include office or non-manual work directly related to the management or general business operations of an employer or of the employer's customers, and must involve the exercise of discretion and independent judgment on matters of significance. The "Professional"

exemption applies to workers whose work (1) requires knowledge of an advanced type in a field of science or learning customarily acquired by prolonged, specialized, intellectual instruction or study; or (2) is original and creative in a recognized field of artistic endeavor; or (3) involves teaching in a school system or educational institution; or (4) involves computer systems analysis, programming, software engineering, or other similarly skilled work in the computer field. In addition, the work must require the consistent exercise of discretion, judgment, or invention, imagination, or talent in a recognized field of artistic endeavor.

In addition to the foregoing, there is also an exemption for Highly Compensated Employees, which the current regulation defines as total annual compensation exceeding \$100,000. The exemption also requires that such employees have primary duties involving office work, or perform job duties that fall under at least one of the other "Professional" categories.

4. THE NEW REGULATIONS (EFFECTIVE 1.1.20)

The most significant change under the new regulations is the increase in the salary level requirement. As of January 1, in order to qualify for one of the Act's exemptions, an employee must make at least \$685/wk. (\$35,568 per year)¹. An employer may use nondiscretionary bonuses and incentive payments (including commissions) to satisfy up to ten percent (10%) of the salary test, provided that these payments are made on at least a quarterly basis. Alternatively, employers can meet the minimum salary requirement by making a "catch up" payment at the end of each quarter, up to

¹ There are special rules for workers employed in American Samoa, and for workers employed in the motion picture industry.

a maximum of ten percent (10%) (\$3,556) of the salary requirement.

The DOL made no changes to the “duties” tests for Executives, Administrators, and/or Professionals. The salary level for the Highly Compensated Executives increased to \$107,432.

The overtime pay requirements do **not** apply to the following entities:

- employees of companies with annual revenues (according to gross volume of sales made or business done) of less than \$500,000 *and* which are not involved in interstate commerce;
- military personnel;
- unpaid volunteers;
- self-employed individuals;
- clergy/religious workers; and
- non-profits *except* to the extent that they are engaged in ordinary commercial activities.

Unlike other federal regulations, there is no “small employer” exemption other than that set forth above.

As under the prior law, the salary test does not apply to outside salespersons, doctors, lawyers, teachers, or computer professional making \$27.63/hr. or more. The prior regulations with respect to retail employees on commission also did not change.

5. OPTIONS FOR EMPLOYERS

Employers have the following options in response to the Act’s revisions:

- reduce the hours of salaried employees whose salaries are below the new “salary level requirement” such that these

employees do not work more than forty (40) hours per week;

- increase the compensation of any salaried worker currently making less than \$35,568 annually;
- reclassify Executive, Administrative, and Professional employees making less than \$35,568 as non-exempt;
- increase the hours of part time employees so that full time employees need not work more than forty (40) hrs./wk.; or
- reduce the base compensation of employees such that overall level of compensation (after payment of overtime) remains the same.

It appears that affected employers may incur increased regulatory familiarization costs, increased record keeping costs, and increased managerial/oversight costs, in addition to potential increased employee compensation. Significantly, employers who have not previously tracked work hours, meal breaks, and rest breaks of salaried employees making less than \$36,000 will have to start doing so, and will have to have these figures audited regularly. In addition, employers will have to review their employee benefit plans and retirement plans to determine whether changes need to be made to the balance of employer/employee payment of premiums and matching contributions.

6. MURKY ISSUES

A. “Sales” Employees – the Supreme Court rejected a DOL regulation holding that the exemption for employees engaged in selling or servicing automobiles does not apply to service advisors, and remanded the case for further consideration without deciding the issue (*Encino Motorcars, LLC v. Navarro*, 579 U.S. ____ (2016)).

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Accordingly, there is still some uncertainty regarding the scope of the “sales” exemption.

B. “Flex Time” Employees – it is unclear how the new regulations will affect employees who had previously been given great latitude with respect to arriving at and leaving from the office. Most companies who require their employees to complete and submit their own time sheets report that this system results in significant inaccuracies.

C. “Telecommuting” Employees – employers who have previously allowed their salaried employees to telecommute will have to devise a method for accurately tracking the work hours of these employees.

D. Enforcing Restrictions on Overtime – it is unclear what employers can do to limit employees to a 40 hour work week where the employees previously had no hours restrictions.

E. Sources of additional revenue – the DOL has not provided suggestions regarding the sources of the additional revenue that employers will need to generate in order to pay overtime to formerly exempt employees.

Publish and publicize new procedures regarding overtime work, overtime pay, and tracking of hours.

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PRACTICAL TIPS

Start working **now** with your employment attorneys and HR personnel to identify employees affected by the new regulations and to decide how to adjust their hours and/or compensation going forward;

Implement appropriate accounting systems and procedures to track hours worked and meal breaks;

Review your benefits packages and determine whether any changes need to be made as of January 1, 2020; and

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