

# FYI<sup>®</sup> Alert

## For Your Information<sup>®</sup>

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## DOL Unveils Final Overtime Rule

In June 2015, the DOL proposed the expansion of overtime eligibility to millions of workers by more than doubling the minimum salary threshold for the so-called “white-collar” exemptions. Today, the DOL unveiled its widely anticipated overtime rule that will have profound implications for millions of employees and employers alike. Employers from coast to coast should assess the financial, operational and organizational impact of the final rule on their workplaces, and shape effective employee communications and compliance strategies.

### Background

The Fair Labor Standards Act (FLSA) establishes federal minimum pay standards for public and private sector employers. Employees covered by the FLSA must be paid at least the federal minimum wage and, in most cases, overtime at time and one-half of the employee’s regular rate of pay for all hours worked over 40 in any workweek. Regulations enforced by the DOL’s Wage and Hour Division provide exemptions from federal minimum wage and overtime requirements for salaried “executive, administrative, and professional” (EAP) employees (so-called “white-collar” employees) who satisfy minimum earnings and job duties tests.

To qualify for a white-collar exemption, employees generally must satisfy three tests. First, they must be paid on a salary basis that is not subject to reduction based on quality or quantity of their work (“salary basis test”). Second, their salary must meet a minimum salary level (“salary level test”). Third, the employee’s primary job duty must satisfy criteria set forth in DOL regulations (“duties test”).

More than two years ago, President Obama directed the DOL to modernize and streamline the rules governing which employees are entitled to receive overtime pay. (See our [March 14, 2014 FYI Alert](#).) Last year, the DOL [proposed](#) rules that would substantially narrow eligibility for the FLSA’s white-collar exemptions by raising the required salary level. The proposal raised the minimum annual salary threshold for the EAP exemption from \$23,660 to \$50,440, and increased the salary level for the highly compensated employee (HCE) exemption from \$100,000 to \$122,148. Those changes were expected to render nearly 5 million currently exempt white-collar workers overtime-eligible. (See our [June 30, 2015 FYI Alert](#).)



## The Final Rule

Today, the DOL unveiled its long-awaited [final rule](#) on “Defining and Delimiting the Exemptions for Executive, Administrative, Professional, Outside Sales and Computer Employees.” To maintain one of these exemptions, an employee’s compensation and primary job duties will have to satisfy the new regulatory requirements.

As expected, the final rule dramatically expands employee overtime eligibility by increasing the minimum salary threshold for a white-collar exemption that has been in place since 2004. A [Fact Sheet](#) issued by the White House states that the new rule is expected to extend minimum wage and overtime protections under the FLSA to 4.2 million currently exempt white-collar workers and to most salaried workers earning less than \$47,476. It also includes a state-by-state breakdown of affected workers.

### Salary Threshold Doubles

The DOL’s final rule more than doubles the minimum salary threshold under which most white-collar salaried workers are eligible to receive overtime pay — from the current \$455 a week (\$23,660 annually) to \$913 per week (\$47,476 annually) in 2016, slightly less than the DOL initially proposed. Those salary levels reflect the 40th percentile of earnings for full-time salaried workers in the lowest-wage census region (currently the South).



The rule similarly increases the total annual compensation level required to exempt HCEs from the current \$100,000 to \$134,004 (the 90th percentile of weekly wages of all full-time salaried employees nationally). To qualify for an HCE exemption, an employee must also receive a minimum salary of at least \$913 per week on a salary or fee basis and pass a minimal duties test.

**Automatic Increases.** In a significant shift, the salary and compensation thresholds will not be subject to annual indexing. Rather, they will automatically update every three years starting on January 1, 2020 to maintain the thresholds at the 40th percentile of full-time salaried workers in the lowest-wage region of the country or 90<sup>th</sup> percentile of annual earnings of full-time salaried workers nationally, respectively. Based on current wage growth projections, the salary threshold is expected to increase to more than \$51,000 with the first update on January 1, 2020. The special salary level test for employees in American Samoa and the base rate test specific to motion picture industry employees will also automatically update.

**Inclusion of Nondiscretionary Bonuses and Incentive Payments.** The final rule allows employers to use certain nondiscretionary bonuses and incentive payments (including commissions) to satisfy up to 10 percent of the new minimum salary level. Employers may credit nondiscretionary bonuses and incentive payments paid at least quarterly toward the new threshold and may also make a “catch-up” payment. Where an employer pays larger bonuses, the amount that may be attributed to the standard salary level is capped at 10 percent of the new minimum salary threshold.

HCEs must receive a salary or fee of at least \$913 each pay period (excluding nondiscretionary bonuses and incentive payments), but the final rule allows employers to continue to count nondiscretionary bonuses and incentive payments (including commissions) toward the total annual compensation requirement.

### Duties Tests Unchanged

While the DOL considered revising the current duties tests, the final rule leaves both the standard duties test and the HCE duties test unchanged. Thus, in determining exempt status, the existing job duty requirements will

continue to apply in tandem with the new minimum salary and compensation levels. (See our [April 3, 2014 FYI In-Depth](#) for information on the duties tests.)

### Effective Date

The new rule is slated to take effect on December 1, 2016. However, expected legal challenges and congressional efforts to block the rule may delay implementation. (See our [May 16, 2016 Legislate](#).)

## Planning for Change: Next Steps

Now that employers know what the final overtime rules require, they can determine what steps they need to take to bring pay practices into compliance. Employers should consider:

- Identifying currently exempt positions that are likely to be impacted by the new threshold
- Reviewing current overtime hours worked by currently exempt employees or positions
- Modeling different scenarios to determine the potential impact of the new rule
- Developing pay plans for exempt employees who will be reclassified as nonexempt
- Identifying any effects of changes on employee benefits
- Developing an appropriate communications strategy
- Training managers and supervisors on the new overtime rules

## In Closing

For nearly a year, employers have anxiously awaited the DOL's final word on overtime pay. The rule released today will significantly alter long-standing pay practices for employers nationwide — expanding overtime eligibility to more than 4 million workers. Employers who have not already done so will want to reexamine the classification of currently exempt employees and begin to develop pay plans for those who will no longer be exempt.

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