ROPES & GRAY

ALERT

Labor & Employment

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New FLSA Rule Raises Minimum Salary Thresholds for Exemption from Overtime

Background

In 2014, President Obama signed a Presidential Memorandum directing the U.S. Department of Labor (the "DOL") to update the regulations that define which white collar workers are exempt from the overtime provisions of the Fair Labor Standards Act (the "FLSA"). The DOL published the Notice of Proposed Rulemaking in July 2015, and the comment period for the proposed rule—which yielded 270,000 responses—closed in September 2015. On May 18, 2016, after much anticipation, the DOL published the final rule (the "Final Rule").

Provisions of the New FLSA Rule

The Final Rule implements the following changes, which will become effective on December 1, 2016:

- The Final Rule increases the new minimum salary level required for the executive, administrative, and professional "white collar" exemptions from $455 a week ($23,660 per year) to $913 per week ($47,476 per year).
- Up to 10% of the salary level for these "white collar" exemptions can be met with nondiscretionary bonuses, incentive payments, and/or commissions if the employer pays them at least quarterly.
- The Final Rule increases the minimum compensation level required to meet the separate "highly-compensated employee" exemption from $100,000 to $134,004 per year. Of that amount, at least $913 per week must be paid on a salary basis.
- These salary/compensation levels will automatically increase every three years. For the executive, administrative, and professional exemptions, the salary will be adjusted to the 40th percentile of full-time non-hourly workers in the region of the country with the lowest average wages. For the highly compensated employee exemption, the salary will be adjusted to the 90th percentile of full-time non-hourly workers nationally.
- The Final Rule increases the minimum salary that must be paid to employees in computer-related occupations to $913 per week, but leaves the existing alternative hourly rate of $27.63 intact.

The Final Rule does not affect the outside sales or inside retail sales exemptions, which do not include a salary threshold, nor does it affect the current duties tests for the "white collar" exemptions. The Final Rule is available here.

What These Changes Mean for You

As a result of these changes, millions of workers will lose their current FLSA-exempt status on December 1, 2016. The hardest hit industries are likely to be education, retail, health services, leisure/hospitality, and business and professional services. Before the Final Rule goes into effect, employers should assess which employees will be affected, and how the employer will want to respond. One approach would be to raise the salaries/compensation of these employees to meet the new salary/compensation thresholds. Following this path may impose not only direct costs, but also indirect costs by creating pressure to raise salaries for other employees higher up on the organizational chart, or causing disgruntlement for those employees if the salary differential is compressed. Another approach would be to reclassify these employees as nonexempt and pay them overtime in accordance with the FLSA. To control costs associated with this approach, employers can consider limiting hours of nonexempt employees to 40 per week (if this can be accomplished consistent with operational needs), or reduce the employees' hourly rate in light of their expected future overtime earnings.

Alternatively, employers can consider adopting either a "fluctuating workweek" or a "*Belo* plan" for employees with irregular work hours. A "fluctuating workweek" is an arrangement, between an employer and employee(s) whose hours fluctuate from week to week, that the employee's stated salary compensates the employee, on a straight-time basis, for all hours worked in the week; as a result, the employee(s) need to be paid only an "additional half time" for hours worked in excess of 40. A "*Belo* plan" is a written agreement between an employer and employee by which the employee is paid a set regular rate above the minimum wage that includes expected overtime pay, up to a maximum number of hours worked (not exceeding 60 per week, and above which the employee must be paid additional compensation). A *Belo* plan is an option if the employee's duties necessitate irregular work hours and the total wages per pay period would vary widely week to week if computed on an hourly basis. You should consult with an attorney before adopting a fluctuating workweek, a *Belo* plan, or taking other measures to reduce overtime costs.

For advice or assistance in dealing with these important changes, or the various approaches to them, please contact any member of the Ropes & Gray labor & employment group.