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DOL Finalizes New Overtime Rules

By Jessica Summers

Take Away: *The DOL has issued new rules that, effective January 1, 2020, will substantially increase the minimum salary that employers must pay employees for them to qualify for the white collar and the highly compensated exemptions to the federal overtime pay requirements. While these new rules may require some employers to make adjustments – the increases are significantly smaller than those that were enacted, but never went into effect, under the Obama Administration. The new rules also do not make any changes to the duties tests associated with the exemptions.*

The rules surrounding which employees can qualify as exempt from the overtime requirements of the federal Fair Labor Standards Act (FLSA) have been in a state of flux for over five years. President Obama and his Administration first began working on changes to the rules in March of 2014. The Department of Labor (DOL) under the Obama Administration finalized new rules in May of 2016 only to have a federal court issue a nationwide injunction in November of 2016 blocking the rules from going into effect just a week before they were scheduled to do so. The ruling was appealed but was not resolved before President Trump took office. Unsurprisingly, under the new Administration, the DOL changed its course. The DOL ceased any defense of the Obama Administration's overtime rules, instead choosing to simply defend the DOL's authority to promulgate such rules and start the rulemaking process anew, culminating with the DOL's issuance of new proposed rules in March of 2019. **After this long tortured history, on September 24, 2019, the DOL issued new final rules which are scheduled to go into effect on January 1, 2020 and are expected to do so without any significant challenges.**

So what is in the new rule? The key changes are as follows:

- **On January 1, 2020, the salary threshold for the white collar exemption will increase by approximately 50% from the current $455 per week (or $23,660 annually) to $684 per week (or $35,568 annually).**

  This increase is considerably less than the $913 per week (or $47,476 annually) that was part of the Obama-era rules.

  The DOL calculated the new salary threshold based on the 20th percentile of weekly earnings for full-time salaried workers in the lowest paid Census Region (currently the South) as calculated by the Bureau of Labor Statistics (BLS). Thus, although the $684 per week was calculated based on the average salaries in the South, the thresholds will apply to the whole country. This is the same methodology that the Obama-era rules used, however, those rules used the 40th percentile rather than the 20th which resulted in the markedly higher threshold.
- **On January 1, 2020, the salary threshold for the highly compensated exemption will increase from $100,000 annually to $107,432 annually.**

  This increase is significantly lower than that proposed by the DOL in March. Under the proposed rule, the threshold would have been increased to $147,414 (the 90th percentile of weekly earnings nationally). Based on the comments that it received, for the final rule the DOL decided to lower the threshold to the 80th percentile of weekly earnings nationally, thus arriving at the $107,432 annual rate.
- **The salary thresholds for the white collar and highly compensated exemptions will not be subject to automatic increases.**

  The Obama-era rules marked the first time that the regulations included a system for automatically increasing the salary thresholds in the future. In the new final rule the DOL has abandoned this concept and instead simply committed to more regularly updating the salary thresholds through the notice and comment process.
- **Under the new rule, employers will be permitted to count non-discretionary bonuses and incentive compensation (including commission) towards up to 10% of the white collar salary threshold as long as the payments are made at least annually.**

Under the preexisting rules, employers were not permitted to include any types of bonuses or incentive compensation in calculating whether an employee's compensation meets the white collar salary threshold.

The Obama-era rules introduced the notion of allowing employers to satisfy a portion of the white collar salary threshold through non-discretionary bonuses or incentive compensation. The only difference between the Obama-era rules and the new final rules is that, while the Obama-era rules required that these payments be made at least quarterly to qualify, the new rules only require payment of the bonuses or incentive compensation on an annual basis.

In short, under the new rules employers can satisfy up to 10% of the new white collar salary threshold (i.e. $3,556.80 per year) through the at least annual payment of non-discretionary bonuses or incentive compensation. To account for the fact that an employer may not be able to calculate in advance what an employee's non-discretionary bonus or incentive compensation will be, the new rule also allows employers to make catch-up payments to bring employees up to the salary threshold as long as the catch-up payments are made by the last pay period of the year or within one month of the end of the year. Such a catch up payment will be credited towards the prior year and will not count towards the threshold for the year in which it is paid.

Prior to the new rules, employers were permitted to include certain types of bonus and incentive payments for the purposes of the highly compensated salary threshold. The new rules do not make any changes to how bonuses and incentive compensation are treated for the purposes of the highly compensated exemption.

- **The new rule will make no changes to the duties tests for the white collar or highly compensated exemptions.**
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  As with the Obama-era rules, the DOL did not propose or make any changes to the duties tests, which, together with the salary threshold, apply to qualify an employee for the white collar or highly compensated exemptions.

Therefore combining the preexisting rules with the new rules going forward:

- To be exempt under a white collar exemption, an employee's primary duties must be executive, administrative, professional, computing, or outside sales (as defined by regulation) and the employee must be paid a salary of at least $684 per week. Employees in computer-related positions can either be paid a salary of at least $684 per week or on an hourly basis at a rate of no less than $27.63 (unchanged by the final rule).
- To be exempt as a highly compensated employee, the employee must regularly and customarily perform one or more of the duties of an executive, administrative or professional employee (as defined by regulations) and the employee must earn at least $107,432, which includes at least $684 per week on a salary basis.

Employer Considerations: Because of the late hour at which the Obama-era rules were enjoined from going into effect, many employers already reviewed and made changes to their workforces in 2016 to comply with those rules. Provided that no changes (including new exempt hires with lower salaries) have been made since, any employer that brought itself into compliance with the Obama-era rules should find that it is also in compliance with the latest final rules.

All other employers should review and identify whether they have any employees who have qualified as exempt using the $23,660 (for white collar) or $100,000 (for highly compensated) thresholds but who do not earn enough to meet the new salary thresholds. The choice will then need to be made as to whether to reclassify these employees as non-exempt (in which case they will be eligible for overtime) or increase their compensation to meet the new thresholds. From a financial standpoint, this will largely require an employee-by-employee assessment of the amount of overtime that the employee needs to work versus the amount that the employee's salary would need to be increased to meet the new threshold. Employers can, of course, strictly limit the overtime that a newly non-exempt employee works in order to avoid increased payroll costs. However, this will need to be balanced with productivity concerns, particularly where the employee has traditionally worked significantly more than forty hours per week. For employers who do end up reclassifying employees as nonexempt, they will also have to start tracking hours in order to calculate when and how much overtime is due.

While the new rules do not make any changes to the duties test, in evaluating employee exemptions, employers are also well advised to confirm that all of their exempt employees also have adequate duties to qualify them for the exemption.

Join us October 8, 2019 at 12:00 p.m. for a webinar in which we will take a deeper dive into these new rules and recommendations for businesses on what steps they need to take before the rules go into effect on January 1, 2020.

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