

## Complying With the Department of Labor's Proposed Overtime Regulations



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On March 7, the U.S. Department of Labor issued its long-anticipated proposed rule that would expand overtime eligibility under the Fair Labor Standards Act (FLSA) to include a significant number of additional workers. The proposal will be open to public comment for 60 days, with the final rule set to take effect around January 1, 2020.

Under current regulations, in effect since 2004, employees with a salary below \$455 per week, or \$23,660 annually, are nonexempt and must receive overtime pay for hours worked over 40 hours per week, regardless of whether their duties fall within one of the FLSA exemptions. The new rule would raise the salary threshold from \$455 to \$679

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per week, or \$35,308 per year, meaning that employees who earn less than those thresholds will be automatically nonexempt and eligible for overtime on the effective date. Employees earning salaries in excess of either threshold may still be nonexempt and eligible for overtime based on their job duties. The new numbers are a product of the same methodology used in 2004, which based the threshold on the 20th percentile of earnings of full-time salaried workers in the lowest-wage census region (the South), as well as the retail sector nationwide.

This is the second attempt by the Department of Labor in recent years to update the overtime rule. In May 2016, under the Obama administration, the agency proposed regulations to lift the salary threshold to \$913 per week, a significant and controversial increase that would have required employers to reclassify as many as four million workers. However, that rule never went into effect. In November 2016, shortly before the effective date of the rule, a federal court in Texas issued a nationwide injunction halting its implementation, and the Fifth Circuit Court of Appeals declined to review that decision until the Department of Labor issued revisions.

While the new rule would raise the salary threshold by about only half the amount contemplated by the Obama-era rule, the Department of Labor nevertheless anticipates that approximately one million additional employees will become eligible for overtime under the proposed changes. The new rule also does away with a provision of the prior rule that would have generated automatic increases in the salary threshold every three years, perhaps a concession to the flurry of negative public comments over that section of the enjoined rule. Instead, the new proposal provides that the Department of Labor will revisit the salary threshold question every four years through the rulemaking process, with future changes based in part on input from the public.

Somewhat surprising to many observers, the proposed rule would raise the annual salary requirement for “highly compensated employees” to \$147,414 per year, a substantial increase not only over the current level of \$100,000, but also over the \$134,004 proposed by the Obama administration. To meet this exemption, an employee must receive at minimum the new standard salary amount of \$679 per week on a salary or fee basis. However, the current text of the proposed rule would permit employers to factor in nondiscretionary bonuses, commissions and other incentive payments that are paid annually or more frequently to fulfill up to 10 percent of the standard salary level, provided the payments are made on an annual or more frequent basis. For employees who do not earn sufficient nondiscretionary bonuses or incentive payments in a given 52-week period

to meet the highly compensated salary threshold, the proposed rule allows employers to make a “catch-up” payment within one pay period of the end of the year to meet the exemption. This “catch-up” payment will count only toward the prior year’s salary and not toward the year in which it is paid. The Department of Labor has opened the door for public comments on whether the proposed 10 percent cap should be higher or lower.

Notably, the proposed rule does not change the current “duties test” used by the Department of Labor and the courts to determine whether employees perform duties that meet one of the exemptions in the regulations or whether they do not and should therefore be classified as nonexempt and entitled to overtime wages. Nor does the proposed rule create different salary levels for different regions of the country based on variations in the cost of living. Also, there are no proposed changes to the regulations affecting certain categories of employees, including police officers, firefighters, paramedics, nurses and certain nonmanagement skilled workers, like carpenters and electricians.

### **Implications**

Assuming the proposed rule survives scrutiny, employers can take steps to mitigate the financial impact of the changes and ensure compliance. As a general proposition, given that the status quo holds with respect to the “job duties” requirement, employers should confirm that their exempt positions meet the applicable duties test and, if warranted, adjust the salary level or reclassify the position if necessary to ensure compliance.

For example, employers may wish to reclassify salaried exempt employees earning at or above the current threshold as nonexempt. Under this method, employers would calculate an hourly rate that accounts for the number of regular and overtime hours and results in the same total pay for those employees. Or, for those employees earning near the newly proposed threshold, employers could raise their salaries up to the new threshold of \$35,308. For employees who regularly work significant overtime hours, this method may cut down on administrative headaches, particularly in situations where overtime hours fluctuate. For employers that find the aforementioned options untenable, simply prohibiting salaried employees from working overtime may be a solution if the loss in productivity is manageable.

Now is a good time for employers to conduct an audit of their workforces to assess the financial impact of the new regulations. In particular, employers should pay close attention to employees earning salaries at or near both the old and new thresholds,

including those employees earning salaries near the “highly compensated” threshold. Given the potentially significant penalties available under the FLSA, employers should consult legal counsel when analyzing employee classification issues to ensure compliance in advance of the effective date of the revised regulations.