

## **Employers Will Be Working Overtime to Implement Final Rule**

The highly anticipated revisions to the federal Fair Labor Standards Act (“FLSA”) overtime regulations for white collar workers were published by the U.S. Department of Labor (“DOL”) on May 18, 2016 (the “Final Rule”). While the Final Rule may be subject to challenge, either in Congress or in the courts, for now employers should assume that the Final Rule will go into effect on December 1, 2016. Employers should therefore start reviewing their workplace practices and compensation structure, and, if changes are required, be ready to put a plan in action.

### *A brief recap of the FLSA*

The FLSA establishes rules governing minimum wage and overtime pay, and covers most U.S. employers and employees.<sup>1</sup> The law presumes that every eligible employee working for a covered employer is entitled to overtime pay at the rate of 1 ½ times the employee’s regular rate for all time worked over 40 hours per week, *unless* the employee is “exempt” from the overtime requirement. The most commonly relied upon exemptions are the executive, administrative and professional exemptions, which are typically referred to as the “white collar” exemptions.

For a position to be exempt under one of the white collar exemptions, it must satisfy a two-prong test. First, the employee’s job duties must meet the applicable test for one or more exemptions. Second, except in limited circumstances, employees must be paid a fixed minimum base salary for every week they perform any work. Currently, the minimum salary threshold is set at \$455 per week (\$23,660 annually).

The FLSA also exempts “highly compensated” employees earning total annual compensation of \$100,000 or more, who customarily and regularly perform at least one of the exempt duties of a white collar exempt worker.

### *Highlights of the Final Rule*

The Final Rule increased the salary basis threshold more than two-fold, to \$913 per week (\$47,476 annually). Commissions, and *nondiscretionary* bonuses and other incentive compensation may account for up to 10% of the minimum salary threshold, if those amounts are paid at least on a quarterly basis. Employers may pay employees who fell short of the salary threshold a “catchup” payment within one week of the end of the applicable quarter.

The Final Rule also raised the total annual compensation requirement for highly compensated employees to \$134,004, of which at least \$913 per week must be paid on a salary basis (nondiscretionary compensation may not be factored into this weekly salary threshold for such workers).

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<sup>1</sup> Some non-profit organizations and smaller businesses will not be covered entities under the FLSA, although individual employees may still be covered. Additionally, state minimum wage laws likely also apply even if the FLSA does not. Please contact us for details.

Importantly, the Final Rule established a mechanism to update these compensation levels automatically every three years, starting January 1, 2020.

### *What employers should do now*

The dramatic increase in the base salary threshold for the white collar exemptions will leave many employers scrambling to figure out how to comply with the Final Rule without significantly affecting their bottom line or employee relations. Employers should immediately begin auditing their workforce and workplace practices to understand which exempt employees will be impacted by the rule because they make less than the new salary threshold, the nature of the work performed by those employees, and how many hours per week each of those employees works, making sure to include all compensable work. Performing this analysis is critical in assessing the financial and other impacts of the various options.

### *Some options – and some pitfalls*

While there are several options available for handling exempt employees currently earning less than the new salary threshold, the DOL has outlined the most obvious ones. These are discussed below.

#### A. Preserving the exempt status and raising the base salary to the new threshold

While this might be seen as a good “quick fix” for workers who are currently earning a base salary close to the new threshold, increasing employees’ salary without reviewing the employees’ duties and responsibilities could potentially backfire. As stated above, an individual’s exempt status also depends on whether his or her actual job duties meet the applicable duties test – which did not change with the Final Rule. Therefore, an employee earning \$47,476 after December 1 who believes his or her position does not meet the applicable duties test could *still* bring a claim – and recover even greater damages if ultimately found to be owed overtime.

Companies must also consider the extent to which raising certain workers’ base salary might require salary adjustments for other workers for employee relations purposes. Additionally, because the base salary threshold will be subject to automatic cost of living increases every three years starting on January 1, 2020, the one-time salary bump could have a long-term impact on the size of a company’s payroll.

#### B. Converting employees to non-exempt status and start paying overtime

Before converting employees to non-exempt status, employers will need to assess how the change in status may impact other areas, including eligibility for benefits. In the case of Massachusetts employees, conversion to non-exempt status could also impact the enforceability of non-compete agreements, in light of recent legislative efforts to ban such agreements for non-exempt workers. Reclassifying employees as non-exempt could also have a morale impact on employees who view themselves as “professionals” and might see being “on the clock” as a demotion.

Converting employees to non-exempt status does not necessarily require employers to convert the individual from salaried to hourly (and there are a few ways that employers can modify employees' existing compensation structure to comply with the Final Rule). However, regardless of the method of payment, non-exempt employees will need to track and report their hours to ensure and document that all time worked has been appropriately paid. Although the DOL has stated that it will not require any particular form of timekeeping records, the obligation to keep such records falls on the employer, who will want a reliable tracking system in case a dispute arises in the future.

The amount of time employees spend working outside regular business hours – including the extent to which employees monitor and answer emails after regular business hours – will need to be taken into consideration. There are scenarios where the employee's compensation structure can be adjusted to allow for a certain level of overtime to be paid, without increasing the employee's total compensation. However, non-exempt employees will need to be instructed not to work more than the agreed-upon hours without prior approval from a manager.

A proper communication plan will need to be developed to notify managers and employees of the nature and reason for the changes. Reclassified workers and their managers will need to be properly trained on the new timekeeping procedures. Periodic check-ins are advisable to ensure compliance with the new system.

#### C. Converting employees and limiting hours to no more than 40 hours per week

The Final Rule may prompt certain companies to re-evaluate staffing levels and redistribute workload to ensure that non-exempt employees work no more than 40 hours per week. The Final Rule might prompt employers to outsource certain functions, hire part-time employees (who will not be eligible for most employer-provided benefits) or utilize temporary employees. Massachusetts employers should consult with counsel before hiring independent contractors, in light of the high threshold applicable in the state for classifying such workers as non-employees.

#### *A silver lining*

The white collar exemptions – particularly, the administrative exemption – have often been misinterpreted. Companies who become aware that an employee has been misclassified as exempt often face a difficult choice between reclassifying an employee – and risk triggering litigation – or not reclassifying the employee and risk facing increased damages if the employee sues. The Final Rule will provide a good opportunity for employers to reclassify employees who may be misclassified as exempt, without raising a red flag. If in doubt, reclassifying an employee as non-exempt may buy peace of mind.

#### **Conclusion**

While the DOL expects the Final Rule to boost wages for workers by \$12 billion over the next 10 years, it remains to be seen if workers will truly see a change in their take home pay. We expect most employers will strive to find creative solutions to minimize the long-term financial impact of the Final Rule. Unless all salaries are increased above the new threshold or employees' hours restricted to no more than 40 hours a week – neither of which will be realistic

for most entities – critical decisions will need to be made about employees’ compensation rate and structure, workload and work schedule.

The employment lawyers at Casner & Edwards, LLP are experienced in advising clients on wage and hour compliance and devising business solutions for structuring the workforce. For assistance and further information about what Casner & Edwards, LLP can do for you, please contact Stephanie Smith at [smith@casneredwards.com](mailto:smith@casneredwards.com); Stan Cygelman at [Cygelman@casneredwards.com](mailto:Cygelman@casneredwards.com); Steve Perry at [perry@casneredwards.com](mailto:perry@casneredwards.com) or Anita Lichtblau at [Lichtblau@casneredwards.com](mailto:Lichtblau@casneredwards.com)

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