



Everything Employers Need to Know About the **FINAL OVERTIME RULE**



For the first time in 15 years, the minimum salary that must be paid to exempt employees is increasing. If you have employees who don't get overtime, you'll need to understand this rule. Note, all employees are entitled to overtime unless the employer can show that the employees meet one of the many exemptions. This final rule affects those classified under the "white collar" exemptions.

Although the salary went up, some incentive payments may be counted now (a new provision). Keep in mind, some states have higher salary requirements and may not allow the incentive pay to count toward the salary. Read on for details!

1. Basic provisions of the final overtime rule

On September 24, 2019, the U.S. Department of Labor (DOL) announced a final rule impacting exemptions from overtime. The rule updates the earnings thresholds necessary for "white collar" exempt employees (i.e., executive, administrative, professional) from the Fair Labor Standards Act's (FLSA) minimum wage and overtime pay requirements.

The final rule is effective on January 1, 2020. Basic provisions of the final rule include:

- Raising the total annual compensation requirement for "highly compensated employees" from \$100,000 per year to \$107,432 per year;
- Allowing employers to use nondiscretionary bonuses and incentive payments (including commissions) paid at least annually to satisfy up to 10% of the standard salary level, in recognition of evolving pay practices; and
- Revising the special salary levels for workers in U.S. territories and the motion picture industry.

The "standard salary level" is raising from \$455 per week to **\$684 per week** (equivalent to \$35,568 per year for a full-year worker)

2. Criteria for a "white-collar" exempt employees

The most commonly known exemptions are the "white collar" categories. Employees must meet specific criteria to be exempt from overtime pay and minimum wage.

The salary level has increased as noted previous. The salary basis primarily means paying a fixed salary every week, with deductions permitted only for narrowly specified reasons. Finally, the duties test for each exemption outlines the job duties and responsibilities that must be met for the employee to qualify as exempt. All three things must be met in order for an employee to be considered exempt.

The five broad categories of white collar exemptions are Executive, Administrative, Professional (learned or creative), Computer Employees, and Outside Sales. The specific duties are defined by regulation, but some red flags are outlined here:

EXECUTIVE EXEMPTION

To qualify for the executive employee exemption, all of the following tests must be met:

- The employee must be compensated on a salary basis (as defined in the regulations) at a rate not less than \$684 per week;
- The employee's primary duty must be managing the enterprise, or managing a customarily recognized department or subdivision of the enterprise;
- The employee must customarily and regularly direct the work of at least two other full-time employees or their equivalent; and
- The employee must have the authority to hire or fire other employees, or the employee's suggestions and recommendations as to the hiring, firing, advancement, promotion or any other change of status of other employees must be given particular weight.

Employees who challenge their classification as executives often argue that they do not possess the required level of authority. As indicated, the employee must supervise two or more employees and have a primary duty of "management." That term is defined to include duties such as training employees, setting rates of pay or hours of work, assigning and directing work, conducting performance evaluations, handling complaints, imposing discipline, and so on.

CRITERIA EMPLOYEE MUST MEET:

- salary level test
- salary basis test
- duties test

ADMINISTRATIVE EXEMPTION

To qualify for the administrative employee exemption, all of the following tests must be met:

- The employee must be compensated on a salary or fee basis (as defined in the regulations) at a rate not less than \$684 per week;
- The employee's primary duty must be the performance of office or non-manual work directly related to the management or general business operations of the employer or the employer's customers; and
- The employee's primary duty includes the exercise of discretion and independent judgment with respect to matters of significance.

This exemption is often wrongly applied based on job titles (such as "administrative assistant"), or to employees who do not exercise the degree of authority and independence required.

In general, the employee should compare and evaluate possible courses of conduct and make a decision after considering the options. For example, an employee who can enter into significant contracts with vendors (such as ordering several dozen new computers) may have the necessary authority. However, an employee who orders mundane office supplies (such as notepads and writing instruments) does not have such authority.

PROFESSIONAL EXEMPTION (LEARNED OR CREATIVE)

The professional exemption is broken down into two categories – learned professionals and creative professionals.

To qualify for the *learned* professional employee exemption, all the following tests must be met:

- The employee must be compensated on a salary or fee basis (as defined in the regulations) at a rate not less than \$684 per week;
- The employee's primary duty must be the performance of work requiring advanced knowledge, defined as work which is predominantly intellectual in character and which includes work requiring the consistent exercise of discretion and judgment;
- The advanced knowledge must be in a field of science or learning; and
- The advanced knowledge must be customarily acquired by a prolonged course of specialized intellectual instruction.

To qualify for the *creative* professional employee exemption, all the following tests must be met:

- The employee must be compensated on a salary or fee basis (as defined in the regulations) at a rate not less than \$684 per week;

LEARNED
PROFESSIONALS
e.g. physician assistants,
certified public accountants

CREATIVE
PROFESSIONALS
e.g. actors, musicians,
composers

- The employee’s primary duty must be the performance of work requiring invention, imagination, originality, or talent in a recognized field of artistic or creative endeavor.

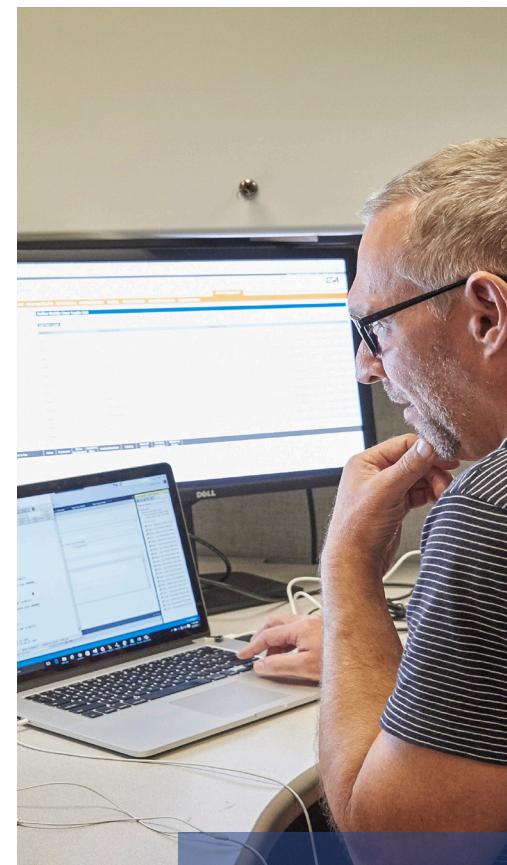
Challenges involving the learned professional exemption commonly arise from failure to meet the educational requirements. Learned professionals must have a certain amount of authority and discretion, but must also meet certain educational requirements (like having a four-year degree). If the education requirement hasn’t been met, the employee cannot be exempt — even if the duties performed would otherwise qualify. Challenges involving the creative professional exemption are uncommon, but may involve the extent of the invention, imagination, originality, or talent exercised by the employee. Whether the exemption applies must be determined on a case-by-case basis.

It’s important to note that although they may fall under the “professional” exemption, teachers (full or part-time), doctors, and lawyers need not be paid the minimum salary leave in order to be classified as exempt.

COMPUTER EMPLOYEE EXEMPTION

To qualify for the computer employee exemption, the following tests must be met:

- The employee must be compensated either on a salary or fee basis (as defined in the regulations) at a rate not less than \$684 per week or, if compensated on an hourly basis, at a rate not less than \$27.63 an hour;
- The employee must be employed as a computer systems analyst, computer programmer, software engineer, or other similarly skilled worker in the computer field performing the duties described below;
- The employee’s primary duty must consist of:
 - The application of systems analysis techniques and procedures, including consulting with users, to determine hardware, software, or system functional specifications;
 - The design, development, documentation, analysis, creation, testing, or modification of computer systems or programs, including prototypes, based on and related to user or system design specifications;
 - The design, documentation, testing, creation, or modification of computer programs related to machine operating systems; or
 - A combination of the aforementioned duties, the performance of which requires the same level of skills.



This classification is unusual because the employees could be paid a salary or a minimum hourly rate specified in the regulation, but qualified workers are exempt from overtime either way. Challenges to the computer employee exemption commonly involve whether the employee designs and creates systems, or merely installs or upgrades existing systems. For example, a “help desk” employee who works in an IT department might respond to calls of system crashes, remove viruses, install upgrades, and troubleshoot applications. However, these duties do not involve the design or creation of new systems, so the employee would not meet this exemption.

OUTSIDE SALES EXEMPTION

To qualify for the outside sales employee exemption, all the following tests must be met:

- The employee’s primary duty must be making sales (as defined in the FLSA), or obtaining orders or contracts for services or for the use of facilities for which a consideration will be paid by the client or customer; and
- The employee must be customarily and regularly engaged away from the employer’s place or places of business.

These employees are not subject to the salary level or salary basis tests, so they were not affected by the rule change. Challenges of wrongful classification may involve whether the employee is actually “making sales” or whether the employee works away from the place of business for a sufficient percentage of time.

The salary requirements of \$684 per week **do not apply** to the outside sales exemption.

3. HOW THE FINAL RULE AFFECTS HIGHLY COMPENSATED EMPLOYEES (HCE)

The FLSA has an exemption for certain highly compensated employees (HCE) who earn above a higher total annual compensation level — which increased from \$100,00 to \$107,432 under the final rule. These employees must also satisfy a duties test.

The final rule did not change how employers may use bonuses to meet the salary level component of the HCE test, but does require highly compensated employees to be paid at least \$684 per week on a salary or fee basis.

The remainder of the total annual compensation may include commissions, nondiscretionary bonuses, and other compensation. Because employers may fulfill a majority of the HCE total annual compensation requirement with commissions, nondiscretionary bonuses, and other forms of deferred compensation, employers may not also use nondiscretionary bonuses and incentive payments to satisfy the weekly standard salary amount.

4. HOW BONUSES AND INCENTIVES COME INTO PLAY

This is new! Employers are allowed to use nondiscretionary bonuses and incentive payments to satisfy up to 10 percent of the standard salary level for white collar exempt employees. This can include a bonus tied to productivity or profits generated by a business in the previous year. If an employer uses a bonus payment to meet the minimum salary threshold, the payment must be made on an annual basis or more frequently.

If an employee does not earn enough in nondiscretionary bonus or incentive payments in a given year (52-week period) to retain his or her exempt status, employers may make a “catch-up” payment within one pay period of the end of the 52-week period. This payment may be up to 10 percent of the total standard salary level for the preceding 52-week period. Any such catch-up payment will count only toward the prior year’s salary amount and not toward the salary amount in the year in which it is paid.

For example, the manager of a retail store might be given a quarterly bonus based on the store’s profits. Those bonus payments may count toward up to 10 percent of the required salary. If the store isn’t profitable and the manager’s salary would not reach the required level, the employer could make a “catch-up” payment at the end of the year.



5. MEETING THE DUTIES TEST

While some things changed under this final rule, other things stayed the same. The rules did not make any changes to the duties tests. Essentially, you’ll evaluate whether an employee qualifies as exempt using the same standards that have already been in place. Exempt employees must still meet the duties test and the salary test and be paid at the new salary level to be exempt.

6. PART-TIME OR SEASONAL EMPLOYEES ARE INCLUDED

Yes. Part-time or seasonal employees must also earn \$684 per week if they are classified as exempt. If they do not earn at least \$684, they may not be exempt. The minimum required salary is not based on a 40-hour week, and it cannot be prorated for part-time employment.

Whether you have an employee working 20 hours per week or 40 hours per week, if the employee is classified as exempt, that employee must earn \$684 per week.

A part-time or seasonal exempt employee doesn’t have to make \$35,568 annually as long as he or she gets paid \$684 per week. For example, the employee could work two weeks per month and make \$684 each week.

7. STATE LAWS MAY HAVE HIGHER THRESHOLDS

State laws are not preempted. You may need to follow a higher state salary test. The FLSA provides minimum wage and hour standards, and does not prevent a state from establishing its own protective standards. If a state is more generous than the provisions of the FLSA, the higher standard applies in that state.

For instance, some states tie their salary level to the state minimum wage, so if the state increases its minimum wage, the required salary level will also increase.

8. MANAGING EXPECTATIONS AND CHALLENGES

If employees need to be classified from exempt to nonexempt, handling employee responses can be a challenge. It can be disheartening for an employee to go from an exempt job classification to nonexempt.

While some employees might welcome the chance to earn overtime if they are reclassified as nonexempt, others may see being reclassified as a negative. Often, having exempt status is considered more prestigious – a “salaried” employee may be viewed as a professional and, when assigned a task or project, is less micromanaged in how it gets done, or how much time is needed to complete it. Being reclassified, for example, may mean having to ask permission to work overtime in order to control overtime costs. This can result in employees seeing their jobs as less flexible – and flexibility is a perk many employees value.

To help with this, make sure you are clear in how you communicate the change. Presenting it with a modicum of compassion might also help, as could focusing on the benefits of earning overtime.

If you’re reclassifying one group of employees to nonexempt, think about moving similar groups to nonexempt to be consistent among employees.

Points you may want to cover when reclassifying employees to nonexempt:

It’s not a demotion. Reclassification is a matter of compliance and has nothing to do with job performance.

It’s not a pay cut. Employees’ new hourly rates were likely calculated so they take home the same amount each week that they did when they were salaried.

It may be a pay raise. Eligibility for overtime guarantees employees will be paid for all working time. If they work more than 40 hours a week, they’ll have to be paid one and one-half times their hourly rate for any overtime hours.



If it's not a pay raise, it may mean more time off. Reclassification can improve work-life balance because instead of feeling pressure to stay late at the office every night, employees can justify heading home when their eight hours are up.

Flexibility has not necessarily been eliminated. Workers will have to log their 40 hours, but they may have flexibility as to when they begin and end their workday, or how that 40 hours is broken up over the course of the workweek. If this is the case in your workplace, stress this with those who are being reclassified.

It's easy. Time tracking may be new to employees who used to be exempt, but it doesn't have to be difficult. For a smoother transition, thoroughly train affected employees and their managers on time-keeping procedures. Review policies on overtime, explaining when and from whom they must get permission to work more than 40 hours a week.

9. STAYING COMPLIANT WITH LABOR POSTERS

We looked over the final rule and determined that it won't bring a mandatory posting change, for a few reasons:

- While the FLSA poster mentions overtime, the information on the poster is very general. It mentions when overtime must be paid and states that certain occupations and establishments are exempt.
- The FLSA poster does not delve into the details of the overtime exemption, and it's these details that the rule is changing.
- The details of the rule outline various costs associated with putting it into place, and the cost of a poster update is not mentioned.

While the poster won't be updating due to this new rule, it's still important to make sure you have this poster visible to your employees.

10. CONSEQUENCES FOR NOT COMPLYING WITH THE NEW OVERTIME RULE

FLSA violations are no laughing matter. If back wages are owed, the employer will be asked to pay the back wages and will be subject to a fine.

Employers who willfully or repeatedly violate the minimum wage or overtime pay requirements are subject to a civil money penalty of up to \$2,014 for each such violation. Willful violations of the FLSA may result in criminal prosecution and the violator fined up to \$10,000. A second conviction may result in imprisonment.



CONCLUSION

While some employers may think the DOL final overtime rule is coming at lightning speed, others may have taken preparatory steps back in 2016 when a different version of the rule was ready to take effect.

If you did the leg work back then, great. Although you still should review company policies and procedures to be sure you're in compliance, chances are it won't be too burdensome. If you haven't had time to prepare, it's not too late. However, time is of the essence.

As the sports saying goes, "the best defense is a good offense." To avoid having to defend your actions when it comes to employee classifications and overtime pay, following these steps and having a good action plan can go a long way toward ensuring you have a solid offense for the New Year.

FREQUENTLY ASKED QUESTIONS

Q: Is the new salary level a gross or net amount?

A: These are gross amounts. (For example, required taxes, FICA, and employee United Way contributions, don't matter.)

Q: Must employers reclassify an employee to exempt if the employee meets the duties test and the salary test?

A: No. Employers could decide to pay all employees overtime. That is fine. Employees may always be classified as nonexempt, but not every employee may be exempt.

Q: Will restaurant managers be affected by this rule?

A: Yes, no business or industry will be excluded. In fact, restaurants, non-profits, and other service industries will likely face some of the tallest hurdles in complying with the new law, mainly due to a tight labor market and other business challenges.

Q: How did the DOL come up with the new salary level?

A: According to the DOL, the salary amount accounts for wage growth since the 2004 rulemaking by using the most current data available at the time the DOL drafted the final rule, and applying to current data the same method and long-standing calculations used to set that level in 2004 — i.e., by looking at the 20th percentile of earnings of full-time salaried workers in the lowest-wage census region (then and now the South), and/or in the retail sector nationwide.

Q: Who is NOT affected by this rule change?

A: Employees who are classified as nonexempt ("hourly") won't be affected. For instance, inside sales professionals generally are nonexempt. Some employees may be exempt from overtime, but are still entitled to minimum wage, such as farmworkers, certain employees of motor carriers, taxi drivers, and certain commissioned employees in retail or service establishments, to name a few.

To prepare for pending changes, employers should:

- Review job duties for exempt and nonexempt employees.
- Make sure employees are classified properly.
- Identify any white collar exempt employees paid less than the proposed salary.
- Review company policies on overtime practices.
- Consider shifting or eliminating job duties to curb overtime and help control costs.
- Look at overall headcount for retention and attrition plans.

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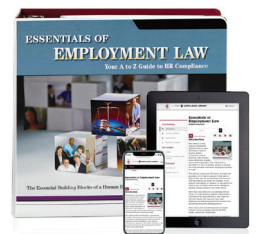
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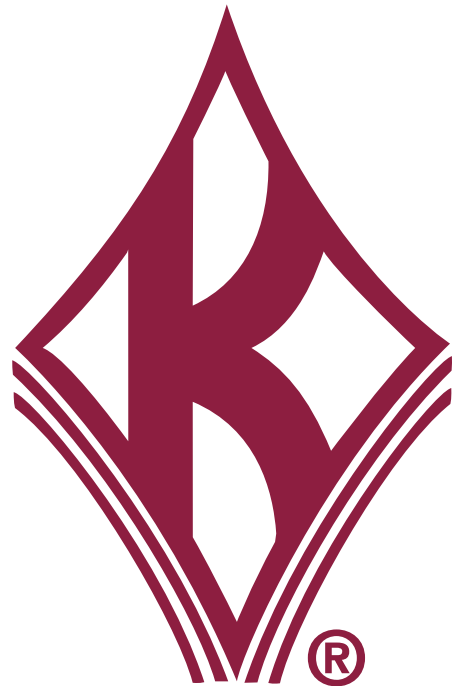
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