

PLANNING FOR DOL'S OVERTIME RULES IN A TOUGH LABOR CLIMATE

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On March 7, 2019, the U.S. Department of Labor announced its proposed regulations on overtime that would render more than 1 million new workers eligible for overtime pay. Coupled with a historically tight labor market, this new rule has the potential to place even greater strain on employers already struggling to attract and retain new talent for their respective workforces.

The Fair Labor Standards Act requires most employers to pay most employees overtime premium pay at least 1.5 times their regular rate of pay for any hours worked over 40 in a week. Section 13(a)(1) of the FLSA, referred to as the white collar exemption, exempts bona fide executive, administrative, professional, outside sales and computer employees from the FLSA's minimum wage and overtime requirements.

The regulations implementing the exemption generally have required three things: (1) the employee must be paid a predetermined and fixed amount that is not subject to reduction because of variations in the quality or quantity of work performed (the salary-basis test); (2) the predetermined amount must meet a minimum specified threshold (the salary-level test) and (3) the employee's job duties must primarily involve executive, administrative or professional duties as defined by the regulations (the duties test). As a reminder, the duties test states:

For the executive exemption, an employee's primary duty must be to manage the enterprise or a department or subdivision of the enterprise and to customarily and regularly direct the work of at least two employees. The employee must have the authority to hire or fire, or his/her suggestions and recommendations as to the hiring or firing must be given particular weight.

For the administrative exemption, an employee's primary duty must be to perform office or nonmanual work directly related to the management or general business

operations of the employer or the employer's customers and must include the exercise of discretion and independent judgment with respect to matters of significance.

For a professional exemption, an employee's primary duty must be work requiring knowledge of an advanced type in a field of science or learning customarily acquired by prolonged, specialized, intellectual instruction and study, or in one of a few other specialized fields, such as professional teachers, creative artists and certain computer employees.

The proposed overtime rule will only affect the salary-level test. The FLSA applies on a workweek basis. Under current law, employees with a salary below \$455 per week (annualizing to \$23,660) must be paid overtime if they work more than 40 hours per workweek. The new proposed regulation would boost the standard salary level to \$679 per week (annualizing to \$35,308), a 50% increase. Of course, the old salary basis and the duties tests would still apply in the analysis to determine whether an employee is exempt from FLSA overtime requirements.

Additional details of the proposed DOL regulations include:

Special "base rate" threshold for employees in the motion picture industry of \$1,036 per week.

Higher salary level for the white collar exemption, to \$147,414. This figure is higher than the Obama administration's \$134,004.

Nondiscretionary bonuses and incentive payments (including commissions) may be used to satisfy up to 10% of the new salary-level requirement, so long as payment is made on an annual or more frequent basis. (Though it remains to be seen how this applies in light of the salary-basis test as it stands.)

No automatic increases in the salary threshold, but the DOL proposes that the salary level will be revisited every four years via the notice and comment rulemaking process.

Potential Effect of the Labor Shortage

To complicate matters further for employers, 7.5 million American jobs were unfilled in March 2019, according to the DOL. In this challenging labor climate, it is more important than ever that employers audit, implement and effectively communicate any changes in employee pay or classification to their workforces.

Further, the job market is demanding that employers not only comply with new DOL regulations, but also make decisions that do not hurt workforce morale or place their

companies at a competitive disadvantage with other businesses with respect to hiring and retaining employees.

First, how employers react to the new regulations will largely depend on the number of hours their exempt employees actually perform work. So, if a company has employees who consistently work more than 40 hours per week, it may be more cost-effective to raise their salaries above the proposed \$35,308 threshold. Of course, this assumes that an increase is sensible in the specific context. Employers often must weigh even seemingly insignificant increases against factors such as compensation-compression up the chain. And, again, the duties test must still be satisfied under the FLSA.

On the other hand, for employees who rarely, if ever, work more than 40 hours per week, reclassifying salary-exempt employees to nonexempt could be preferable. The employer must track all hours worked for a reclassified employee, and the employer should maintain such timekeeping records for a period of three years.

Given the potential influx of employees accustomed to working when and where they want, businesses should consider updating their handbooks to detail overtime policies for nonexempt employees and possibly limit employees' authorized overtime. Though employers would still have to pay for any unauthorized overtime worked, they may counsel and discipline employees for that unauthorized overtime.

Reclassifying workers as nonexempt has the potential to create morale and retention problems. Many employees equate their professional identities with being salary exempt, and reclassifying employees from exempt to nonexempt status could result in the loss of key benefits such as retirement plans. So, employers should be cognizant of the effect a reclassification may have on an employee's morale.

To maintain morale and an engaged workforce, employers should strongly consider leaving benefits intact for reclassified workers. Employers should assure employees that decisions about reclassification were made based on the totality of the circumstances for the company, in compliance with the new overtime rule, and have nothing to do with any employee's performance or standing with the company.

Companies also could use new hires or even temporary employees to ensure that newly nonexempt employees do not work overtime. Also, some newly reclassified workers' tasks might be reassigned to employees whose classification remains exempt.

Finally, it is key that employers are prepared to communicate any changes to affected employees in a sensitive manner. Let employees know that these changes are due to compliance with federal regulations and not a demotion or reduction in pay or benefits.

The proposed rule is just the first step in what will be a lengthy notice-and-comment process. Although the DOL anticipates the rule will be effective in January 2020, employers should not wait until the rule is finalized to begin auditing and reviewing their employee classifications. Staying ahead of these regulatory changes and proactively preparing for their potential impact on employees may provide an employer with advantages in recruiting and retaining talent in a labor market where there is little room for error.

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