How Will the New Overtime Rule Impact Your Business This Comp Season? 10 Tips for Employers

Insights
10.03.24

As the final quarter of 2024 begins, many employers are turning to the year-end review process. While you're planning for raises, bonuses, and other employee incentives this comp season, you'll need to account for the new exempt salary threshold that is scheduled to take effect January 1. Indeed, the U.S. Department of Labor's (DOL's) next big hike will raise the salary threshold for the white-collar exemptions to nearly $59k – and the minimum salary for the "highly compensated employee" (HCE) exemption will increase to a whopping $151,164. While legal challenges to the DOL's rule are ongoing, you can't count on a court stepping in before the next effective date. So, now is the time to ensure your practices comply with the most recent requirements and to get ready for the next phase. Here are your top 10 steps to consider as you develop your compensation plan for 2025.

1. Keep Compliance Top of Mind

You'll want to start by reviewing the major changes at the federal level that were recently finalized. Under the Fair Labor Standards Act (FLSA), employees generally must be paid an overtime premium of 1.5 times their regular rate of pay for all hours worked beyond 40 in a workweek — unless they fall under an exemption.

One of the criteria for the FLSA's executive, administrative, and professional exemptions (the so-called "white-collar" exemptions) is earning a weekly salary above a certain level. As of July 1, that level is $844 a week ($43,888 annualized). For the next phase, which takes effect on January 1, the salary threshold will rise to $1,128 (or $58,656 a year).

In addition to raising the salary threshold, the rule makes the following key changes:

- The salary threshold will be **automatically updated**every three years starting on July 1, 2027.
- The threshold for the**"highly compensated employee" (HCE) exemption** rose to $132,964 on July 1, and will rise again to $151,164 on January 1. The HCE threshold will also be updated every three years.

2. Identify Employees Below the Threshold

Do you currently have white-collar exempt employees who earn less than $58,656 a year (or $132,964 for HCE)? You will have to decide whether to raise their salary to meet the new threshold or convert them to non-exempt status. If you decide to convert them, there are many considerations, and you should work with legal counsel to decide on the best course of action. Additionally, you may want to start tracking their actual hours worked now to help you understand the potential impact of converting to non-exempt status, as those individuals will need to be paid overtime.

3. Consider These Key Compensation Issues

If you decide to reclassify your employees to non-exempt status, there are many considerations you'll have to work through, including the following:

- **How Much to Pay.** Will you divide the employee's weekly salary by 40 hours to determine their hourly rate, or will you factor in the employee's estimated overtime and adjust accordingly?
- **Regular Rate Calculations.** Overtime premiums are based on the employee's "regular rate of pay." Employers are sometimes surprised to learn the regular rate is not simply an employee's hourly rate of pay or their take-home pay. The regular rate is based on "all remuneration" earned from employment with the exception of eight specific exclusions contained in section 7(e) of the FLSA.
- **Incentive and Bonus Pay.** The regular rate includes all types of compensation – including things like non-discretionary bonuses, commissions, payments for undesirable shifts or duties, and some non-cash payments depending on the circumstances. Keep in mind that most bonuses are not discretionary and must be included in the regular rate. It is common for employers to pay out bonuses based on a formula announced ahead of time and designed to incentivize certain behavior. Such bonuses are not discretionary. You can read more about the regular rate here.
- **How to Track Non-Exempt Employees' Work Time.** Employers are required to make and keep records of non-exempt employees' working time. Before converting employees to non-exempt status, it may require some planning, reconfiguration of workflow, and implementation of new processes or technology to ensure that you are accurately recording their work time. It is best practice to think about these questions in advance and explore multiple potential recordkeeping processes to determine which options meet your needs and are cost-effective.
- **How Benefits Will Be Affected**. Do you have different vacation, sick leave, and other policies for exempt and non-exempt employees? You will have to consider how to transition reclassified employees to new programs and train workers and their supervisors on new procedures.

Before converting an employee to non-exempt status, you may also want to see if they qualify for another exemption – such as the outside sales exemption – that does not require a minimum salary threshold.

4. Consider the Impact on Morale

Reclassifying employees to non-exempt could have a negative impact on morale, so you should consider preparing a communication plan that addresses sensitive issues. For instance, many employees associate prestige with being classified as an exempt-salaried employee, like the flexibility that comes with being salaried, and don't want to track and record their hours worked.

Remind employees that they are valued and let them know you are required to make changes in light of the federal government's new wage and hour rules. The DOL has made clear that the goal is to make more people eligible for overtime pay — which means more workers will likely need to be converted to non-exempt — and you can explain to employees that your decisions are meant to keep your business compliant with the latest regulations.

5. Plan to Provide Advance Notice of Changes

In addition to developing communications focused on employee relations and morale, you'll want to prove a written communication to each employee about the specific changes to their compensation and what new responsibilities come with the changes, such as timekeeping, meal and rest breaks, and other requirements.

Note that some states require advance notice of wage changes, so you should check your local requirements. Regardless of the state law, however, you should clearly communicate the new terms of employment before they take effect.

6. Review Your Policies on Company Equipment and Personal Devices

Do you have different policies for exempt and non-exempt employees when it comes to issuing company equipment and using personal devices? Exempt employees may have more leeway to use company laptops or their own personal devices — such as smartphones — to conduct business while traveling or outside of their regular office hours. Also, be mindful of expense reimbursement in situations where the employee is paid at or close to the salary threshold.

7. Develop a Training Plan for Managers and Newly Non-Exempt Employees

We highly recommend you provide detailed training to newly reclassified employees and their managers prior to the changes taking effect. The specifics may vary from business to business, but you'll want to cover scheduled hours, OT approval policies, timekeeping procedures, rules about meal and rest breaks and more.

8. Ensure Exempt Employees Meet the Duties Test

Besides the salary test, exempt employees also need to satisfy certain duties requirements.

Don't forget that the white-collar exemptions have more requirements than just the salary threshold. To qualify for these exemptions, employees must meet three criteria:

- Be paid on a salary basis;
- Be paid at least the designated minimum weekly salary; and
- Perform certain duties.

Notably, neither their job title nor job description alone determines whether an employee qualifies for a white-collar (or any other) exemption.

Now is a good time to review your exempt jobs for compliance will all criteria – not just the salary threshold. Click here to read more about the duties requirements for the white-collar and highly compensated employee exemptions.

9. Track Legal Challenges

Legal battles continue over the DOL's authority to raise the salary threshold. So far, however, the rule has been blocked only as it applies to the state of Texas as an employer while the district court hears the underlying legal challenge. But even though the ruling only impacts Texas state employees, the battle isn't over for other employers. It's possible the same judge or others could decide to extend that ruling nationwide and halt the OT rule from taking effect for all employers across the country.

In another case questioning the DOL's power to set any salary basis floor, the 5th U.S. Circuit Court of Appeals actually handed the agency a win. It noted that Congress gave the DOL explicit authority to define and delimit the terms of the OT exemption, and therefore the agency was not acting outside of bounds by setting a salary floor. While this is a major victory for the DOL, the pathway to the January 1 salary hike is still fraught with peril.

In the meantime, however, the July 1 increase is already in effect and private employers across the country will need to adjust their compensation practices to comply until and unless a court says otherwise.

10. Don't Forget About State Wage and Hour Laws

It is important to remember that other jurisdictions can have higher, stricter, or different wage and hour requirements. For example, some states have a higher salary threshold for the white-collar exemptions than the FLSA's new $844 per week (July 1, 2024) and $1,128 per week (January 1, 2025). Others might have different exemptions or exceptions, including some that do not have salary thresholds. Of course, some jurisdictions also have higher minimum wage rates and/or additional overtime-type requirements.

Finally, while the FLSA regulates little in the way of actual wage payments, deductions, and notification of pay terms, many states have detailed requirements and might even have different provisions for non-exempt versus exempt employees.

Conclusion

We will continue to monitor developments from the DOL's Wage and Hour Division, so make sure you are subscribed to Fisher Phillips' Insight System to get the most up-to-date information. For further information, contact your Fisher Phillips attorney, the authors of this Insight, or any attorney in our Wage and Hour Practice Group.

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