September 30, 2019

New FLSA Rule Raises Minimum Salary Thresholds for Exemption from Overtime Pay

Background

The U.S. Department of Labor (the "DOL") has just released, after much anticipation, final updates to the regulations that define which white-collar workers are exempt from the overtime provisions of the Fair Labor Standards Act (the "FLSA").

This final rule (the "2019 Final Rule") supersedes a similar final rule that the DOL published on May 23, 2016, under the administration of President Obama (the "2016 Final Rule"). The 2016 Final Rule most notably would have doubled the minimum salary level required for the executive, administrative, and professional "white collar" exemptions to $913 a week ($47,476 per year) with automatic increases every three years. The 2016 Final Rule was blocked on November 22, 2016 and invalidated on August 31, 2017 by a federal court in Texas. The validity of the 2016 Final Rule remains on appeal before the federal Fifth Circuit Court of Appeals.

On July 26, 2017, the DOL, under the administration of President Trump, issued a request for information to begin crafting a new rule to supersede the 2016 Final Rule. The DOL published a Notice of Proposed Rulemaking in March of 2019, taking into account the 2017 decision invalidating the 2016 Final Rule, and the comment period for the proposed rule—which yielded over 116,000 responses—closed in May of 2019.

Provisions of the New FLSA Rule

The 2019 Final Rule implements the following changes, which will become effective on January 1, 2020:

The 2019 Final Rule increases the new minimum salary level required for the executive, administrative, and professional "white collar" exemptions from $455 a week / $23,660 per year to $684 per week / $35,568 per year (compared to $913 a week / $47,476 per year under the 2016 Final Rule).

Up to 10% of the salary level for these "white collar" exemptions may be met with nondiscretionary bonuses, incentive payments, and/or commissions if the employer pays them at least annually (compared to quarterly under the 2016 Final Rule).

The 2019 Final Rule increases the minimum compensation level required to meet the separate "highly-compensated employee" exemption from $100,000 to $107,432 per year (compared to $134,004 under the 2016 Final Rule). Of that amount, at least $684 per week / $35,568 per year must be paid on a salary or fee basis.

Unlike under the 2016 Final Rule, these salary/compensation levels will not automatically increase every three years under the 2019 Final Rule.

The 2019 Final Rule increases the minimum salary that must be paid to employees in computer-related occupations to $684 per week, but leaves the existing alternative hourly rate of $27.63 intact.

The 2019 Final Rule does not affect the outside sales or inside retail sales exemptions, which do not include a salary threshold, nor does it affect the current duties tests for the "white collar" exemptions. The 2019 Final Rule is available here.

What These Changes Mean for You

As a result of these changes, an estimated 1.3 million workers (compared to an estimated 4.2 million workers under the 2016 Final Rule) will lose their current FLSA-exempt status on January 1, 2020, unless their salaries are increased. The hardest hit industries are likely to be education, retail, health services, and leisure/hospitality, particularly in rural areas or other markets with relatively low prevailing wages. Before the 2019 Final Rule goes into effect, every employer should assess which of its employees may be affected, and determine how to respond. One approach would be to raise the salaries/compensation of these employees to meet the new salary/compensation thresholds. Following this path may impose not only direct costs, but also indirect costs by creating pressure to raise salaries for other employees higher up on the organizational chart, or causing disgruntlement for those employees if the salary differential is compressed. Another approach would be to reclassify these employees as non-exempt and pay them overtime in accordance with the FLSA. To control costs associated with this approach, employers can consider limiting hours of non-exempt employees to 40 per week (if this can be accomplished consistently with operational needs), or reducing the employees' salaries in light of their expected future overtime earnings.

Alternatively, employers can consider adopting either a "fluctuating workweek" or a "*Belo* plan" for employees with irregular work hours. A "fluctuating workweek" is an arrangement, between an employer and employee(s) whose hours fluctuate from week to week, under which the employee's stated salary compensates the employee, on a straight-time basis, for all hours worked in the week; as a result, the employee(s) need to be paid only an "additional half time" (rather than time and one-half) for hours worked in excess of 40. A "*Belo* plan" is a written agreement between an employer and employee by which the employee is paid each week an amount consisting of a regular hourly rate (which is greater than the applicable minimum wage) for 40 hours per week and an amount that is one-and-one-half times that regular rate for a specified number of overtime hours (not exceeding 60 per week, and above which the employee must be paid additional compensation). A *Belo* plan is an option if the employee's duties necessitate irregular work hours (both above and below 40 in a work week) that neither the employer nor the employee can either control or anticipate with any degree of certainty, and the total wages per pay period would vary widely week to week if computed on an hourly basis. You should consult with an attorney before adopting a fluctuating workweek, or a *Belo* plan, or taking other measures to reduce overtime costs.

For advice or assistance in dealing with these important changes, or the various approaches to them, please contact any member of the Ropes & Gray labor & employment group.