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Expanding Overtime Protections to Millions, U.S. Department of Labor Releases FLSA Proposed Rules

The federal Fair Labor Standards Act (“FLSA”) establishes minimum wage and overtime rules for employees, guaranteeing overtime pay at a rate of not less than one and one-half an employee’s regular rate of pay for hours worked in excess of 40 in a workweek. While these protections extend to most workers, the FLSA provides a number of exemptions, known as “white collar exemptions,” for executive, administrative, professional, outside sales and computer employees. Currently, to be classified as exempt, an employee must (i) be paid on a salary basis at least \$455 per week (\$23,660 a year); and (ii) meet certain minimum tests related to his or her primary job duties.

Earlier today, the U.S. Department of Labor (“DOL”) issued new proposed regulations to the FLSA. These proposed regulations have been in the works since President Obama issued an Executive Order in March 2014 in which he directed the DOL to update and modernize the existing “outdated” FLSA exemptions so that the law would address the changing nature of the workplace and only exclude higher paid employees from overtime. The proposed rules drastically increase the number of workers that would qualify for overtime pay, forcing employers to make a serious, proactive effort to review current employee classifications.

New Salary Level Test

Through this rulemaking, the DOL has proposed that the minimum salary threshold for exempt status be raised from \$455 per week to \$970 per week, or \$50,440 per year. This new proposed level is equal to the 40th percentile of weekly earnings for full-time salaried workers (based on projected data for the first quarter of 2016), as the DOL has determined that the 40th percentile of weekly earnings would “serve as a better proxy for distinguishing between overtime-eligible and exempt white collar workers.”

Thus, an employee making less than \$50,440 per year as of 2016 can no longer qualify for any “white collar” exemption. This change is particularly impactful for mid and lower-level manager and assistant manager positions where salaries are often near the cut-off point of the salary level test, particularly in industries such as retail, hospitality, and health care. If the rule is finalized as proposed, many low-level managers and assistant managers may automatically be disqualified from exempt status unless their salaries are raised to meet the new salary minimum, significantly increasing employers’ labor costs. The resulting

increase in costs, however, would likely occur even if these employees' salaries are not raised to meet the new minimum because they would become non-exempt and be entitled to overtime wages if they work more than 40 hours in a workweek. Based on information available to the DOL when it drafted the proposed rule, it estimates that approximately 4.6 million currently exempt workers will, without intervening action by their employers, become entitled to minimum wage and overtime protection in Year 1. The proposed regulations would also automatically update the salary threshold annually, either using a fixed percentile of wages or the Consumer Price Index.

New Highly Compensated Employee Test

In addition to changing the minimum salary for exempt employees, the proposed rule also raises the minimum salary needed to meet the highly compensated employee ("HCE") exemption. The rule proposes that the annual compensation level of a worker be equal to the 90th percentile of earnings for full-time salaried employees for the HCE exemption to apply. Based on data used for the rulemaking (the DOL used data from 2013 for the calculation it provided in its proposal), this annual salary amount would be \$122,148, but this amount would be even higher using earnings for full-time salaried workers in 2016.

No Change to Duties Test

Notably, the proposed regulations do not include changes to the duties tests applicable to the white collar exemptions, although the DOL stated that it is considering whether changes to those tests are necessary to ensure that they fully reflect the purpose of the exemption. It has asked for public comment on possible changes to the duties tests pursuant to the rulemaking process.

Public Comment Process

The rulemaking process requires the DOL to formally propose a rule changing the current exemptions, provide the public an opportunity to comment on the proposal, and then issue the final rule. Now that the regulations have officially been proposed, there is a 60-day comment period following the date of publication in the Federal Register during which the business community will have an opportunity to express concerns about the proposal prior to the final rule going into effect. Comments received will become a matter of public record and will be posted to the DOL's website. As a result of the significant impact this proposed rule will have on employers throughout the country, providing comments is an important way for employers to make certain their voices are heard and considered as the DOL moves to finalize a regulation that will continue to affect how employers classify their workforce and handle rising labor costs well into the future.

Next Steps for Employers

Even if the proposed regulations are modified based upon the public comments, they still will create narrower exemption classifications, entitling a greater number of employees to overtime and resulting in significant costs to employers both for increased overtime

payments and the expense of restructuring classifications/employee positions. To prepare for these changes and potentially save on later expense, as well as gain a greater understanding as to how the new rules impact your business, all employers should evaluate the exempt classifications of their current workforce and prepare to reclassify certain employee positions. Employers should pay special attention to those positions that are close to the salary threshold, including “assistant manager” and “supervisor” positions. Given the nuances of these regulations, guidance from legal counsel would be especially useful for an employee classification review. Employers also should review their policies regarding overtime and their hourly tracking systems as a result of the increased number of employees who will be entitled to overtime when the rule goes into effect. The pertinent considerations include determining which employees are impacted, how to address employee status (whether by reclassification or increasing salaries), and which policies and procedures (such as restructuring pay calculations) will need to be updated.

We will continue to provide further updates as new information becomes available on the proposed rule.

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