alert
Labor and Employment Practice
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The New Overtime Regulations: How Will They Affect *Your* Workplace? (Part 1)

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SUMMARY
On May 18, 2016, the Department of Labor (DOL) unveiled the final version of its highly anticipated overtime regulations. In its first increase since 2004, the standard minimum salary level for exemption from overtime under the Fair Labor Standards Act (FLSA) has been increased by just over 100 percent, from $455 per week ($23,660 annually) to $913 per week ($47,436 annually). The salary level for highly compensated employees (HCEs) has also been increased, from $100,000 to $134,004 annually. The changes take effect December 1, 2016.

To help you navigate the waters, we have prepared a multi-part series discussing changes under the regulations and how they will affect employers and workers. In this first segment, we provide a general overview of the specific regulatory changes relevant to the standard salary level and the salary level for highly compensated employees.

The Revised Salary Levels

Employers have been dreading the new regulations since March 2014 when President Obama issued a directive to the DOL to "modernize and streamline" existing overtime rules to make more workers eligible for overtime. Almost 16 months later, in July 2015, the DOL published proposed regulations seeking to increase the minimum salary threshold for exempt workers to $970 per week ($50,440 annually) and to increase the salary level exemption for HCEs to $122,148 annually. Although the final regulations ***decreased*** the proposed standard salary level by $57 per week ($3,004 annually), they ***increased*** the HCE level by $11,856 annually.

When the salary level increases were proposed, the DOL estimated that more than 4.6 million workers who were currently exempt would no longer meet the minimum salary threshold and would become eligible for overtime unless their salaries were increased to the new minimum salary levels. With the slight decrease between the proposed and final standard salary levels, the 4.6 million estimate has been revised downward, to approximately 4.2 million workers.

Indexing, Increases and Potential Decreases

The new standard salary level is indexed to the 40th percentile of weekly earnings for full-time salaried workers in the lowest wage Census Region in the United States, currently the South Census Region. The new HCE total annual compensation level is indexed to the 90th percentile of earnings of full-time salaried workers nationwide. After the new initial levels go into effect on December 1, 2016,

they will be updated every three years and revised levels will be published at least 150 days before they go into effect, with the first update taking effect on January 1, 2020. This means that employees could receive raises every three years; however, the new regulations are silent as to what happens if the wage level for the lowest wage Census Region decreases, and depending on the economy, standard salary levels may remain static or even decrease.

The Revised Salary Basis Now Permits Use of Nondiscretionary Bonuses, Incentive Payments and Commissions

The regulations also amend the **salary basis** test to permit employers to use nondiscretionary bonuses and incentive payments, including commissions, to satisfy up to 10 percent of the new **standard salary level** ($913/week). For example, nondiscretionary incentive bonuses tied to productivity and profitability may be counted. Regardless of the value of any bonuses paid, the amount attributable to the standard salary level is capped at 10 percent of the required salary amount.

Catch-Up Payments for the Standard Salary Level

To be able to credit nondiscretionary bonuses and incentive payments toward a portion of the standard salary level, employers will be required to make such payments on a quarterly or more frequent basis. A **"catch-up" payment** may also be made at the end of a quarter if an employee does not earn enough in nondiscretionary bonuses and incentive payments (including commissions) to retain their exempt status. The employer has one pay period to make up for the shortfall, that is, up to 10 percent of the standard salary level for the preceding 13-week period. Any such catch-up payment will count only toward the prior quarter's salary amount and not toward the salary amount in the quarter in which it is paid. If the employer chooses not to make the catch-up payment, the employee will be entitled to overtime pay for any overtime hours worked during the quarter. This suggests that employers should consider implementing time-keeping procedures for all employees, including employees who are currently exempt.

Nondiscretionary Bonuses, Incentive Payments and Commissions May Not be Used to Meet Total Annual Compensation Requirement for HCEs

The 10 percent amendment does not apply to HCEs even though they are also subject to the **standard salary level** of $913/week. Employers are already permitted to fulfill almost two-thirds of the HCE **total annual compensation** requirement (rising from $100,000 to $134,004/year) with commissions, nondiscretionary bonuses and other forms of nondiscretionary deferred compensation earned during a 52-week period (not including credit for board or lodging, payments for medical or life insurance, or contributions to retirement plans or other fringe benefits). Based on this, the DOL determined not to permit employers to use nondiscretionary bonuses and incentive payments to also satisfy the **standard salary level**.

Catch-Up Payments for HCEs Left Unchanged

What remains unchanged is that employers may also make **"catch-up" payments for HCEs** who do not meet the minimum total annual compensation by the last pay period of the relevant 52-week period. Such payments must be sufficient to achieve the required level and may be made during the last pay period of that year or within one month after the end of the 52-week period. Any such final payment made after the end of the 52-week period may count only toward the prior year's total annual compensation and not toward the total annual compensation in the year it was paid. If the employer fails to make such a payment, the employee does not qualify as a highly compensated employee; however, the employee may still qualify under another of the white collar exemptions. Even so, this suggests that employers should consider implementing time-keeping procedures for all exempt employees.

What Happens Next?

These changes will have the greatest impact on industries with substantial numbers of low-paid managers (eg., production, retail, restaurants, service) as well as on educational institutions and non-profits; however, virtually all employers in all industries

will be affected. Further, and despite the DOL's optimism at increasing wages and the number of workers eligible for overtime, workers will also suffer numerous adverse consequences.

In the meantime, follow us for the next several weeks as we delve into the revised regulations and a multitude of potential issues and outcomes. Our series of Alerts will discuss what employers should be doing NOW to ensure compliance by December 1, 2016; anticipated impacts of the new rules on both employers and workers and how to handle them; and a focus on issues for specific industries, including educational institutions, restaurants, non-profits, retail, service and production industries.

Also watch for our Roundtable Series coming to a city near you – we will sit down with clients and friends to discuss how the new overtime regulations will affect their workplaces and provide them with practical solutions.

This Alert was written by Catherine E. Walters, a member of the firm's Labor and Employment Practice. Catherine can be reached at 717.257.7569 or cwalters@saul.com. This publication has been prepared by the Labor and Employment Practice for information purposes only.

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