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Labor & EMPLOYMENT

How to prepare for DOL's new FLSA overtime rules

On Dec. 1, 2016, just more than a month from now, new regulations updating the requirements for the “white collar” and “highly compensated employee” (“HCE”) exemptions under the Fair Labor Standards Act will take effect.

Although there are a number of benefits to classifying employees as exempt under the FLSA, an employer's misapplication of the exemptions may result in significant financial liability. Therefore, it is important for employers to carefully review employee classifications and consider their current options.

Final Rule

The Department of Labor's final rule makes four significant changes to the white collar and HCE exemptions under the FLSA. Specifically, under the Final Rule:

The “salary level” test for the white collar exemptions (executive, administrative and professional employees) will be increased from \$455 per work-week, to \$913 per work-week;

The HCE “compensation threshold” will be increased from \$100,000 per year, to \$134,000 per year;

Employers will be able to count nondiscretionary bonuses and incentive payments, including commissions, in satisfying up to 10% of the “salary level” test for white collar exemptions; and

Both the white collar “salary level” test and the HCE “compensation threshold” will be automatically increased every three years.

Salary level test

In general, in order to qualify for the FLSA's white collar exemptions, the employee must, among other things, meet the salary basis and salary level requirements. Currently, the minimum salary



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level required to meet one of the FLSA's white collar exemptions is \$455 per work-week (\$23,660 annually). (In New York, it is currently \$675 per work-week (\$35,100 annually)). As of Dec. 1, 2016, however, the federal minimum salary level will more than double, increasing to \$913 per work-week (\$47,476 annually). The Department of Labor has indicated that the new minimum salary level is set at the 40th percentile for weekly earnings of full-time salaried workers in the lowest-wage U.S. Census region, which is currently the South.

HCE compensation threshold

The Department of Labor has also amended the HCE exemption. Under the HCE exemption an employer may classify an employee as exempt, so long as he or she: (1) meets the white collar “salary basis” and “salary level” tests; (2) meets the HCE “compensation threshold”; and (3) meets a relaxed duties test. Currently, the HCE “compensation threshold” is \$100,000 per year. As of December 1, 2016, however, the HCE “compensation threshold” will increase to \$134,000 per year. The Department of Labor has

indicated that the new HCE “compensation threshold” is set at the 90th percentile of weekly earnings of full-time salaried workers nationally.

Nondiscretionary bonuses and incentive payments

In connection with the increase to the “salary level” test, the final rule authorizes employers to count nondiscretionary bonuses and incentive payments, including commissions, in meeting the minimum salary requirements. The final rule marks the first time this process is available for the white collar exemptions’ “salary level” test. Under the final rule, these nondiscretionary bonuses and incentive payments may only be counted to satisfy up to 10 percent of the minimum salary level (i.e., a maximum of \$91.30 per work-week, or \$4,747.60 annually). More importantly, nondiscretionary bonuses or incentive payments must be paid at least every quarter. If an employer elects to count these bonuses or payments in meeting the minimum salary requirements and its employee has not received the required minimum salary at the end of the quarter, the employer is permitted to make a “catch-up” payment. In order to be considered timely, this catch-up payment must be made within one pay period following the quarter. The Department of Labor has indicated that if the employee fails to receive the required minimum salary in a given quarter and no timely catch-up payment is made, that employee is entitled to overtime pay for any overtime hours worked during that quarter. Therefore, if an employer elects to utilize nondiscretionary bonuses and incentive payments to meet the minimum salary requirements for employees, it

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should develop and adopt a procedure to ensure the minimum quarterly salary level is reached for each affected employee.

Updating mechanism

The final rule also creates an updating mechanism to continually establish new salary levels and compensation thresholds for both the white collar and HCE exemptions. This updating mechanism allows the Department of Labor to automatically update the “salary level” test and HCE “compensation threshold” every three years. Under this updating scheme, the Department of Labor will post the new salary level and compensation threshold at least 150 days prior to their effective date, maintaining the above-mentioned percentiles with respect to full-time salaried employees (i.e., 40th percentile in lowest-wage Census Region for “salary level” test and 90th percentile nationally for “compensation threshold” for HCE). According to the Department of Labor, updating the salary and compensation levels is the best method to ensure that the exemption tests continue to provide an effective means of distinguishing between overtime-eligible white collar employees and those who may be *bonafide* executive, administrative, and professional employees.

Potential Responses for Employers

Employers have two main options when dealing with employees currently classified as exempt who make less than \$47,476 per year. Specifically: (1) raise the employee’s salary to comply with the new “salary level” test and/or HCE “compensation threshold”; or (2) reclassify the employee as nonexempt.

If the employee is currently making a salary of less than \$47,476 per year, it may make sense to increase his or her salary above the threshold if: (1) the employee regularly works 40 or more hours per work-week; (2) the employer desires to mitigate the risk of unexpected overtime costs; and/or (3) a valued employee desires greater consistency in his or her pay level.

However, if an employer chooses to reclassify an exempt employee as nonexempt, there are a number of different

ways to implement this change. For example, the employer may:

- Pay the employee on an hourly basis. Record the employee’s hours worked and pay overtime (time and one-half) for any overtime hours worked. In determining the employee’s hourly rate, employers may take into account the overtime pay that the employee will be eligible for as a result of being reclassified.

- Pay the employee a salary meant to cover all hours worked up to 40 hours per work week. (e.g., \$500 for all hours worked up to 40 hours) Record the employee’s hours worked and pay overtime (time and a half) for any overtime hours worked.

In relation to above options, in an attempt to mitigate potential overtime liability resulting from reclassification, an employer may desire to establish a policy limiting employees to 40 hours of work per work-week, absent advanced approval from management. In the event an employee violates this rule, the employer must compensate the employee for all hours worked (including overtime). That said, the employer would take appropriate corrective action against the employee for his/her violation of company policy.

An additional, albeit significantly more complex option, is to:

Pay the employee on a fluctuating work-week basis. Under the FLSA, where there is a clear advanced mutual understanding between the employer and employee (preferably in writing), an employer may pay an employee a fixed salary (apart from overtime premiums) for the hours worked each work-week, whatever their number, rather than for working 40 hours or some other fixed weekly work period, provided that the amount of the salary is sufficient to provide compensation to the employee at a rate not less than the applicable minimum wage rate for every hour worked in those workweeks in which the number of hours the employee works is the greatest. Notably, the employee must receive extra compensation, in addition to his/her salary, for all overtime hours worked at a rate not less than one-half of the employee’s regular rate of pay. Since the salary in such a situation is intended to compensate the employee at straight time rates for whatever hours are worked

in the work-week, the regular rate of the employee will vary from week to week and is determined by dividing the number of hours worked in the workweek into the amount of the weekly salary to obtain the applicable hourly rate for that week. Payment of overtime hours at one-half such rate in addition to the salary satisfies the overtime pay requirement because such hours have already been compensated at the straight time regular rate, under the salary arrangement.

Guidance should be sought

Due to its complexity, employers should not attempt to implement a fluctuating work week methodology of pay without first receiving guidance from qualified labor and employment counsel.

Notably, there are other options available that could, in appropriate situations, result in no additional wages having to be paid or that could minimize the amount of overtime due.

That said, regardless of whether salary or compensation levels are at issue, Employers should use the implementation of the Department of Labor’s final rule as an opportunity to review all exempt positions and reclassify employees who were previously improperly classified, as necessary.

Finally, under New York’s Wage Theft Prevention Act (“WTPA”), employers are required to provide every new hire with written notice in English and in the language identified by each employee as his/her primary language, indicating, among other things: the employee’s rate of pay (including overtime rate of pay if applicable), how the employee will be paid (i.e. by the hour, shift, day, week, salary, commission or other), the regular payday, and certain information regarding the employer. Subject to limited exceptions, employers are obligated to provide an additional written notice anytime the related information changes. Each time the employer provides the notice the employer must obtain a signed and dated written acknowledgement from the employee, in English and in the primary language of the employee, of receipt of the notice. Notably employer’s must

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keep the signed acknowledgements on record for a minimum of six years. Violation of the WTPA's requirements can result in significant penalties (i.e., up to \$5,000 per violation per employee)

Therefore, to the extent any changes to pay, classification, or other WTPA required information will occur, the employ-

er should provide affected employees with formal advanced written notice that complies with the WTPA.

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