

LEGAL UPDATES

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## Service

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# Labor Department Proposes Changes to Overtime Exemption Rules

On June 30, 2015, the United States Department of Labor (DOL) announced a long-awaited proposal to amend rules governing overtime exemptions for employees in executive, administrative and professional positions. If adopted, the proposed changes would dramatically expand the number of white collar workers eligible for overtime compensation under the Fair Labor Standards Act (FLSA).

The current salary threshold for overtime exemption, set in 2004, is \$455 per week (\$23,660 per year). The DOL seeks to redefine the threshold as the 40th percentile of earnings for full-time salaried workers and allow the threshold to update automatically, without formal rule changes.

Under the 40th percentile threshold, white collar workers currently making \$970 per week, or \$50,440 per year, would qualify for overtime compensation. A separate threshold for exempting highly compensated salaried employees would be set at the 90th percentile of annual earnings, increasing that threshold from \$100,000 to \$122,148. The DOL estimates that changing the salary threshold would qualify about 5 million additional workers for overtime wages within the first year of implementation.

## The White Collar Exemption Test

DOL regulations call for a three-part test in determining application of the white collar exemption. In its current form, that test requires satisfaction of the following for the exemption to apply: (1) payment of a fixed salary that is not reducible based on quality or quantity of work (the “salary basis test”); (2) the amount of salary paid meets or exceeds a threshold amount (the “salary level test”); and (3) the employee’s duties involve executive, administrative or professional duties (the “duties test”). Certain employees (i.e. doctors, teachers

and lawyers) are not subject to the salary level test. The proposed amendments address the second prong of this test.

### **The DOL's Reasoning**

The overtime exemption threshold has been updated seven times since the FLSA was passed in 1938. The DOL notes that automatically updating the salary level would “prevent the level from becoming outdated with the often lengthy passage of time between rulemakings.” And setting the salary level at the 40th percentile “minimizes the risk that employees legally entitled to overtime will be subject to misclassification” based on minimum tests related to their primary job duties.

### **What This Means to You**

The proposed change to the white collar exemption would dramatically increase the number of workers who are eligible for overtime pay and result in significant cost increases for employers. The DOL estimates the average annualized direct employer costs (i.e., regulatory familiarization, adjustments and managerial) would total \$239.6 million to \$255.3 million per year. The average annualized transfer of income from employers to employees is estimated at \$1.18 billion to \$1.27 billion.

If the proposal is enacted, employers will need to revise their overtime policies and practices and ensure they are in compliance with the DOL's mechanism to automatically update the salary and compensation thresholds.

After the DOL's proposed amendment is published in the Federal Register, the public will have 60 days to submit written comments. The DOL is particularly interested in comments on the percentile line of demarcation used to set the annual salary threshold.

The Notice of Proposed Rulemaking, Fact Sheet and other resources are available on the DOL website.

*Sara Fevurly, a summer associate at the firm, assisted in the preparation of this alert.*