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## Client Alert: Not Again! DOL Proposes to Increase Salary Threshold Levels for Overtime Exemptions for the Third Time in Eight Years

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On August 30, 2023, the U.S. Department of Labor (DOL) announced its Notice of Proposed Rulemaking (NPRM) concerning updates to the Fair Labor Standards Act's (FLSA) overtime regulations, specifically the executive, administrative, professional, and highly-compensated employees (HCE) exemptions. In a move that could impact an estimated 3.4 million workers, the DOL's current proposal seeks, most notably, to increase the weekly salary level threshold from \$684 (\$35,568 per year) to \$1,089 (\$55,068 per year).

#### FLSA Overview

The FLSA requires that most employees be paid at least the federal minimum wage for all hours worked and receive time and a half the employee's "regular rate of pay" – that is, all remuneration, including, without limitation, incentive compensation, non-discretionary bonuses, and commissions an employee receives in a given workweek, subject to eight statutory exclusions – for all hours worked over 40 in a given workweek. Despite this general rule, the statute provides certain exemptions, commonly known as the "white collar" exemptions, for those employed as bona fide executive, administrative, or professional employees. Unlike non-exempt employees, exempt employees, including those that satisfy the white collar exemptions, are not entitled to overtime compensation for hours worked over 40.

To qualify for one of the white-collar exemptions, employees must satisfy certain criteria. Specifically, employees must (i) be paid on a salary basis, which means that their predetermined salary is not subject to reductions due to variations in the quality or quantity of their work; (ii) be paid at a rate not less than the weekly salary level threshold, which is currently \$684; and (iii) perform certain primary duties specific to each exemption. Employees who do not satisfy all of the exemption criteria will be entitled to overtime compensation.

The DOL's most recent NPRM marks the agency's third attempt to increase the weekly salary level threshold in the past eight years. As some employers may recall, in 2015, the DOL under the Obama Administration published a rule to raise the threshold from \$455 per week to \$913 per week. Although the rule was struck down by a federal court before it could go into effect, the reprieve was only temporary as the DOL under the Trump Administration published a new rule in 2019. The 2019 rule, which became effective on January 1, 2020 and is currently in effect, raised the salary level threshold from \$455 per week to \$684 per week, increased the HCE total annual compensation level from \$100,000 to \$107,432, and permitted employers to use non-discretionary bonuses and incentive payments, including commissions, to satisfy up to 10 percent of the salary level threshold.

## Proposed Changes

As set forth in the NPRM, the DOL proposes to make several changes to the FLSA's white-collar exemption regulations. The most impactful proposed change concerns the standard salary level threshold. As noted above, the NPRM proposes to set the threshold at the 35<sup>th</sup> percentile of weekly earnings of full-time salaried workers in the lowest-wage Census region (currently the South). Based on 2022 data, this would increase the salary level threshold from \$684 per week to **\$1,089 per week** (\$55,068 per year for a full-time worker).

Similarly, the NPRM proposes to set the HCE total annual compensation level equal to the 85<sup>th</sup> percentile of earnings for full-time salaried workers nationwide. Based on current data, this would increase the HCE total annual compensation level from \$107,432 per year (with a guaranteed weekly salary of at least \$684 per week) to **\$143,988 per year** (with a guaranteed weekly salary of at least \$1,089).

In addition, the NPRM proposes to increase the standard salary level threshold for inhabited U.S. territories by applying the standard salary level of \$1,089 per week to all territories except for American Samoa. Because American Samoa's minimum wage falls below the federal minimum wage of \$7.25, the salary level threshold will be equal to 84 percent of the standard salary level (\$890 per week) and will not increase to the standard salary level until 90 days after the minimum wage equals the federal minimum wage. The NPRM also proposes to increase the special salary level for the motion picture industry from \$1,043 per week to \$1,617 per week.

Lastly, the NPRM proposes to automatically update these earnings thresholds **every three years** with current wage data. The updates will be adjusted so that the standard salary level remains at the 35<sup>th</sup> percentile of weekly earnings of full-time non-hourly workers in the lowest-wage Census region and the HCE total annual compensation level remains at the annualized weekly earnings of the 85<sup>th</sup> percentile of full-time non-hourly workers nationwide.

Notably, the NPRM does not propose any changes to the duties tests of the white-collar exemptions. Similarly, the DOL will continue to permit employers to use non-discretionary bonuses, incentive payments, and commissions to satisfy up to 10 percent of the salary level for the exemptions.

Although the DOL's NRPM may be an unwelcome disruption for many employers, it is important to keep in mind that this is merely a proposal. Before it can become effective, the NPRM is subject to a 60-day notice and comment period that will not commence until the DOL publishes the proposed rule on the Federal Register. Following the notice and comment period, the DOL will consider the comments and publish the final rule, which would likely to go into effect in 2024. If history is any indication, however, the new rule will likely be challenged in the courts. Nevertheless, it is critical that employers take appropriate steps **now** to determine how they will manage the new overtime regulations if or when a final rule goes into effect.

## Prepare for Compliance

Because the NPRM merely proposes changes to the FLSA's white-collar exemption regulations, employers should not make any changes to exempt employees' classifications or increase salaries until such time as the DOL publishes a final rule. However, to ensure FLSA compliance, we recommend that employers reevaluate their current exempt workforce and be prepared to make changes by following the guidelines below.

## **1. Analyze Your Workforce**

An initial first step in preparing for the potential implementation of changes to the salary level threshold is to determine how many, if any, exempt employees are paid a salary that currently exceeds \$684 per week (\$35,568 annually) but is less than the proposed \$1,089 weekly salary level threshold (\$56,628 annually).

For these affected workers, employers should first confirm that the individuals satisfy the relevant duties test(s) of their applicable exemption(s). In fact, employers who have not recently assessed the exempt status of their exempt workforce would be wise to use this time to conduct a wage and hour audit of their exempt classifications so that any necessary changes can be implemented – and communicated – on a grand scale.

Although the decision to reclassify affected workers who do not meet the requisite duties test(s) as non-exempt will be an easy one, employers will likely need to conduct a more in depth analysis to determine the best course of action for other affected workers whose salaries are currently beneath the proposed threshold. For these individuals, employers should assess the following:

- The number of overtime hours the affected employees currently work – and are likely to work in the future – on a weekly and annual basis;
- Whether the affected employees have the ability to work remotely by answering emails on their phones, taking calls or texts after hours, or working on a computer from home;
- Whether the affected employees are eligible for and receive additional compensation (i.e., incentive pay, non-discretionary bonuses, commissions, etc.) that would need to be included in an employee's regular rate of pay when determining overtime compensation; and
- The amount of overtime each affected employee is likely to receive on a weekly and annual basis based on their estimated overtime hours.

Because exempt employees do not always record their hours worked, employees should begin having their affected employees track their hours, including any time spent on remote activities after hours, on an interim basis. During this period, affected employees should be required to record their clock in and clock out times, both at the beginning and end of their shift as well as during their lunch break, assuming they take at least a thirty (30) minute uninterrupted lunch break. As a reminder, under the FLSA and its regulations, a bona fide lunch break must be at least 20 minutes (preferably 30 minutes) and be uninterrupted, meaning employees do not perform any work – and should not be asked to perform any work – while they are off the clock for their lunch break. Employers should ensure that all of their non-exempt employees, as well as their exempt employees affected by the NPRM, have a way to report a lunch break that is interrupted so that they are properly paid for that time.

For timekeeping purposes during this interim period, employers can utilize their current timekeeping software or time clock system or, if necessary, a simple time sheet. In fact, even an email reporting daily clock in and clock out times will suffice. To ensure that the reported time is representative of the employee's normal schedule, employers should closely monitor the affected employees' hours for at least several weeks, if not longer.

## **2. Determine How Best to Comply**

Armed with an understanding of their affected employees' hours worked, employers can assess the estimated economic costs of compliance and best determine how to handle the NPRM's proposed changes. Options include:

- Increasing an affected employee's salary to meet the new salary level threshold. This is likely the most viable option for individuals whose weekly salaries are already close to the proposed threshold of \$1,089 and/or who work so many hours that their weekly compensation, inclusive of overtime compensation, would exceed \$1,089 per week;
- Reclassifying certain affected employees as non-exempt. This option would be most appropriate for employees whose weekly salaries or hours worked are low enough that their total compensation, including overtime, for a given workweek does not meet the proposed salary level threshold of \$1,089. For these individuals, employers will need to determine their method of compensation. Specifically, employers should consider whether to (i) convert the employee to hourly; (ii) maintain the current weekly salary for all hours up to 40 in a workweek and pay overtime compensation on top of the salary; or, (iii) increase the weekly salary to reflect a portion of the employee's overtime compensation and reach an agreement with the employee that their weekly salary will be based on a specific number of hours per week in excess of 40 that reasonably reflects the employee's normal hours worked and pay additional overtime compensation on top of the salary. If utilizing this third option, employers will need to ensure that employees are properly paid overtime compensation at the appropriate rates for all hours worked over 40; or,
- Reclassifying certain affected employees as non-exempt and hiring additional employees as needed to ensure that non-exempt employees do not work over 40 hours in a given workweek.

### **3. Update Relevant Policies and Provide Training**

Employers who decide to reclassify certain employees as non-exempt should also use this time to update related policies (*e.g.*, policies concerning remote work or other off-the-clock work, uninterrupted lunch breaks, prohibitions on unauthorized overtime, etc.) and provide appropriate training to affected individuals. Regardless of whether employers elect to update policies during this time, newly reclassified employees will need to be trained on various timekeeping and scheduling issues to ensure that they are being paid properly for all hours worked in a workweek. To ensure a seamless transition for their newly reclassified employees, employers should ensure that these changes are communicated before implementing any changes. This will be critical not only for employee morale, but also to ensure compliance with state or local law if such notice requirements exist in the state(s) applicable to the employer.

### **4. Prepare a Communication Strategy**

Lastly, a critical component of these changes will be ensuring that employers have a clear and positive communication strategy to minimize the negative impact on employee morale. If choosing to reclassify certain employees, employers may receive backlash from employees who view the reclassification as a demotion or an unfavorable change in status. To combat these negative perceptions, employers should be prepared to answer questions concerning their decision to reclassify. Employers should also stress the importance of their employees and highlight both that these changes will not result in a pay decrease and that they are making these changes to ensure compliance with federal wage and hour law. By preparing a positive messaging strategy in advance of the implementation of any new regulations, employers will maximize their chances of maintaining a happy and productive workforce.

## **Conclusion**

Although the changes proposed in DOL's NPRM likely represent a significant challenge to employers, employers can ease the burden of this transition with thoughtful and advance planning. We will keep you apprised of any developments as they arise. If you have any questions regarding the new proposed overtime regulations, or any other general wage and hour compliance concerns, please contact Kate Decker at [kdecker@shumaker.com](mailto:kdecker@shumaker.com) or 419.321.1452 or any of Shumaker's other experienced Labor and Employment attorneys.