



Proposed Change to the Fair Labor Standards Act Increasing the Exempt Status Wage Threshold

November 2015 • Lockton® Companies

If approved, proposed rule changes released by the Department of Labor (DOL) will raise the salary threshold at which an employee is eligible to be classified as exempt from \$23,660 to \$50,440.¹ This means an employee who is currently exempt and earning a fixed salary of \$970 or less per week would be disqualified from the exempt status and therefore entitled to overtime pay.

Three-Part Test Determines Exemption Status

The DOL manages the Fair Labor Standards Act (FLSA), which outlines the regulations that allow employers to decide if an employee can be classified exempt (paid a fixed salary with no overtime pay) or non-exempt (paid an hourly wage and eligible for overtime pay). So how does an employer know whether an employee should be eligible for overtime pay? The DOL provides employers with a three-part test that helps determine exemption status.

Part 1: Salary Basis

This test ensures the employee is regularly paid a predetermined amount each pay period (salaried). The amount cannot decrease due to the quantity or quality of the employee's work.

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Part 2: Salary Threshold Qualifier

This test ensures the employee is paid at least \$455 per week, or \$23,660 per year. To be exempt, an employee must earn at least this much on a salaried basis.

Part 3: Primary Job Duties

The DOL created five broad job categories that could qualify for exempt status:

- ❖ Executive (management roles with two or more direct reports)
- ❖ Administrative (for example, tax accountant or senior auditor)
- ❖ Professional (for example, electrical engineer or lawyer)
- ❖ Outside sales (at least 80 percent of time is spent selling while away from the office)
- ❖ Certain computer/technology jobs (for example, computer programmer or business systems analyst)

All employers are subject to an audit by the DOL to ensure their employees and their jobs satisfy these three tests. If the DOL determines an employer has violated the regulations by misclassifying an employee as exempt, the employer may be fined as much as \$1,100 per violation and subject to up to three years of back overtime wages, payable to all misclassified employees (both current and former).² The DOL has the option to pursue criminal prosecution for willful repeat violators.

Why Change the Rules?

On March 13, 2014, the DOL received a presidential memorandum urging it to “update, modernize, and simplify” the current FLSA rules.

The DOL proposed increasing the salary threshold from \$455 to \$970 per week, or \$50,440 annually. Additionally, the proposed threshold will be indexed annually using the US Consumer Price Index or the 40th percentile of earnings for all full-time salaried workers (yet to be determined.) Consequently, with the updated law, each year the salary threshold requirement will be updated automatically. This is not the current practice under existing law.

No changes have been proposed for the salary basis or job duties tests.

Who Will Be Affected?

According to the DOL, nearly 5 million white collar workers would be affected by the proposed rule change.³ Any employer who currently classifies an employee as exempt AND the employee earns less than the weekly threshold of \$970 per week may soon be required to start paying the employee overtime and change the employee’s status to nonexempt. Some examples of roles that are likely to be affected include:

- ❖ Food service managers/supervisors
- ❖ Retail sales managers/supervisors
- ❖ Non-profit managers/supervisors
- ❖ Customer service representatives
- ❖ Legal support workers
- ❖ Office and administrative support workers
- ❖ Social workers
- ❖ Counselors

When Will the Updated Rules Take Effect?

Although no formal timetable exists for release of the updated rules, final rules are expected sometime in late 2015 or early 2016.

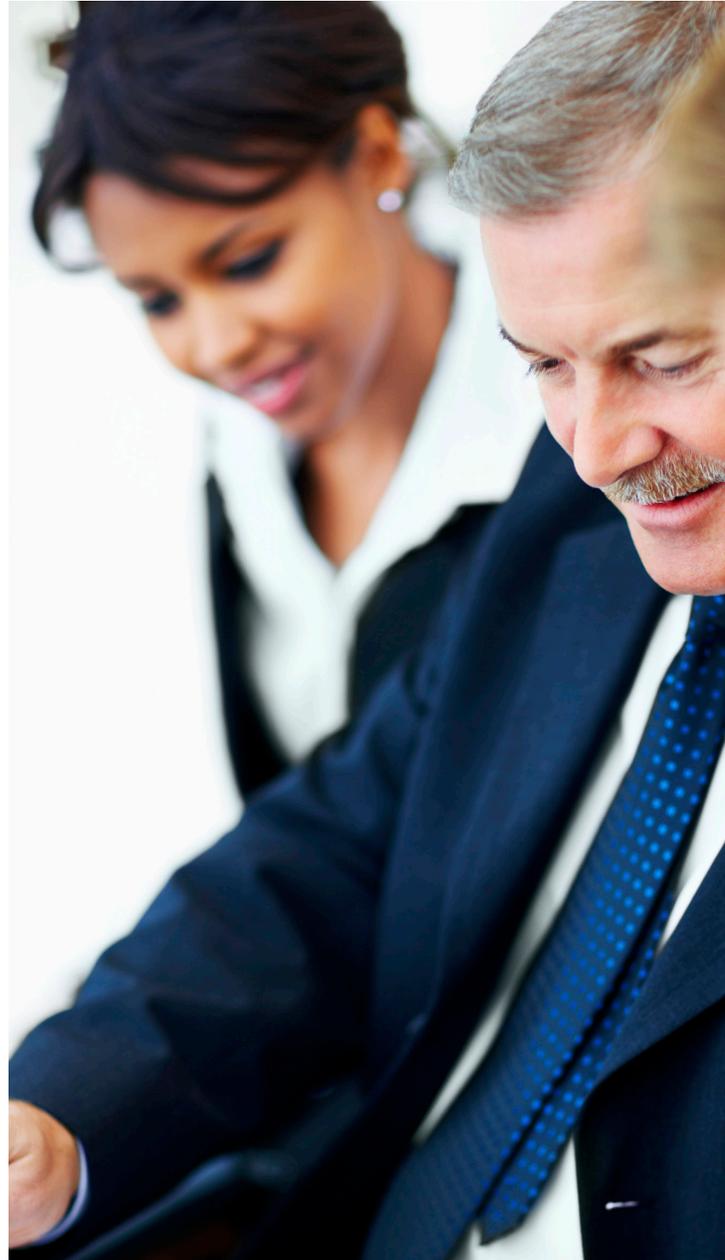
The DOL collected comments from employers through September 4, 2015. These comments are being evaluated by the DOL and may or may not affect the final rules.

How Employers Can Prepare

First, employers should ensure exempt employees are appropriately classified under the current law, using the \$455 threshold (\$23,660 annually). If you need assistance properly classifying your employees, the Lockton Compensation Practice provides FLSA evaluations and recommendations for our clients.

Next, employers should immediately identify any employees who would be affected by the proposed rule changes (those currently in an exempt status and earning a salary of less than \$970 per week) and begin tracking the hours worked by these identified employees. Lockton's Compensation Practice provides this analysis to our clients for a nominal fee.

Finally, employers should consider all options and prepare a strategy in the event these rules are adopted. The Lockton Compensation Practice performs financial modeling and can develop a strategy to help you mitigate the cost of the proposed rules changes.



References

¹ United States Department of Labor. *Notice of Proposed Rulemaking: Defining and Delimiting the Exemptions for Executive, Administrative, Professional, Outside Sales and Computer Employees*. Document 80 FR 38515. Washington: Federal Register, 2015. Federalregister.gov. Web. 24 September 2015.

² *Wages and Hours Worked: Minimum Wage and Overtime Pay*. Department of Labor. Department of Labor, September 2009. Web. 24 September 2015.

³ *Notice of Proposed Rulemaking: Overtime*. Department of Labor. Department of Labor, 6 July 2015. Web. 24 September 2015.

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