Your Guide to the DOL’s New Overtime Rules

Namely

HR for Humans

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The Fair Labor Standards Act (FLSA) requires workers to be paid overtime if they work more than 40 hours a week. However, since the law's passage in 1938, certain employees have been exempted from this requirement. Wages are part of that equation—and soon, the minimum salary to exempt an employee from overtime could double.

Though the Department of Labor sought to enact the rules on December 1, 2016, a federal injunction has delayed their effective date for the time being. The news gives employers some reprieve—but HR must be prepared for what comes next.

Exempt vs. Non-Exempt: A Refresher

When determining overtime eligibility, HR managers need to consider wages and job duties.

The Duties Test

The FLSA exempts executives, computer professionals, commissioned salesmen, and administrative employees if their primary duty is related to the "management or general business operations of the employer or the employer's customers."

An exhaustive list of exemptions under the duties test can be found on the Department of Labor's website.

The Wages Test

Under a new DOL proposal, workers earning $47,476 or less per year must be eligible for overtime, regardless of job duties.

If an employee earns $134,004 or more a year and primarily performs nonmanual work, he or she can be deemed exempt. Bonuses can satisfy up to 10% of the salary level for exemption if paid quarterly.

Take heed: Just increasing an individual's salary is not enough to avoid having to pay them overtime. When determining overtime eligibility, the duties and wage tests have to be considered in tandem.

For example, an administrative assistant would not be considered exempt just because he or she makes over $47,476 per year—the duties test must still be adhered to. Conversely, an executive or manager earning less than the minimum salary for exemption would have to be compensated for time worked over 40 hours a week.

So What's Changing?

On May 18, the Department of Labor unveiled new rules significantly altering the wages test for the first time since 2004. The proposal increases the minimum salary from **$23,660 to $47,476**.

The new threshold represents the 40th percentile of earnings for full-time salaried workers in the census region with the lowest average wages. The rule establishes that this number will refresh every three years.

Needless to say, going from $23,600 to $47,476 is a big jump. The change could lead to the reclassification of millions of workers—possibly a quarter of all exempt employees.

$47,476
NEW THRESHOLD

$23,660
OLD THRESHOLD

Preparing for the Final Rule

Reclassifying employees is by no means a simple process, even for smaller employers. Though a court injunction has put the changes' future into question, employers should proceed conservatively.

1

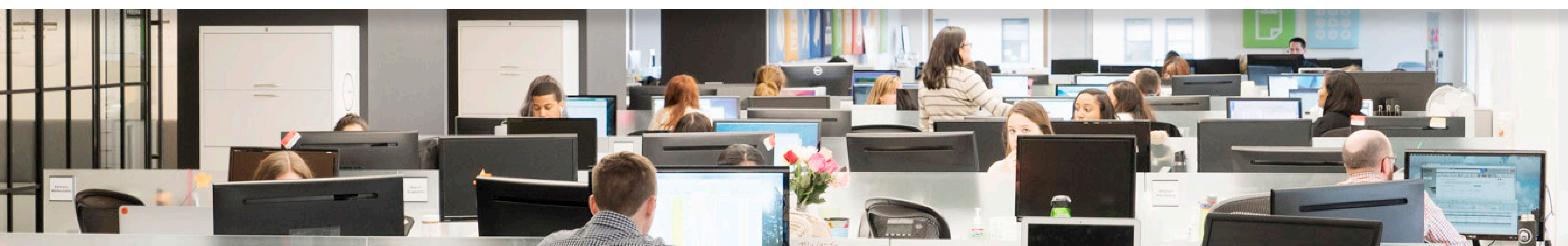
Identify Potential Changes

Get a lay of the land—pull an employee report including job titles and compensation data. In particular, see which employees are earning under or around $55,000. **That's the sweet spot for positions that are most often misclassified**—like assistant managers, sales support roles, and customer service representatives. It's critical to consider those salaries and each employee's weekly hours worked in light of the new $47,476 limit. Also keep in mind that the rule also provides for an automatic increase to the threshold every three years.

Once you have pared down your report, examine each employee's responsibilities to determine if they really should be exempt from overtime under the Department of Labor's duties test. Remember, exempt status is not purely a matter of salary or title—if an individual's responsibilities alone warrant overtime, their salary is a moot point. These individuals need to be earning overtime pay.

Unsure about an employee's classification? While the safest course of action would be to consult legal counsel, remember one steadfast rule: making an employee non-exempt is never unlawful. The same cannot be said for the reverse—making an employee exempt.

Once you have identified who should be exempt from overtime, it's time to crunch some numbers.



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Calculate the Costs

So, you've identified the employees that should be overtime exempt—but their salaries fall close to the $47,476 minimum. You can either increase their salaries or reclassify them. Determining the most economical approach for your organization is the next logical step.

To get started, you need to gauge how many hours per week these employees typically work. Ask managers to report to you the average weekly hours worked for the employee in question. With that amount, you can then calculate approximately how much the individual would earn in overtime pay per year by following the equations below:

Employee Salary ÷ 52 Weeks in a Year = **Weekly Wages**

Weekly Wages ÷ 40 Hours = **Hourly Wages**

Hourly Wages x 1.5 (Time and a Half) x Avg. Overtime Hours Per Week = **Weekly Overtime Wages**

Weekly Overtime Wages x Weeks Worked in a Year = **Annual Overtime Earnings**

Example:

Jim earns a $45,000 salary and works 50 weeks a year. As a graphic designer and a creative professional, Jim can be exempted under the duties test—but his salary falls under the new DOL minimum. A review of Jim's hours showed that he, on average, works about 47 hours a week, or 7 hours overtime. To determine the different costs of either giving Jim a raise or reclassifying him as non-exempt, we can use our equations:

Cost of Overtime

$45,000 ÷ 52 Weeks in a Year = $865.38 Weekly Wages
$865.38 ÷ 40 Hours = $21.63 Hourly Wages
$21.63 x 1.5 (Time and a Half) x 7 Hours Overtime = $227.11 Weekly Overtime
$227.11 x 50 Weeks Worked = **$11,355.50 Annual Overtime**

Based on our calculations, switching Jim's status to non-exempt would cost the company about $11,000 a year. Now, we should calculate the cost of giving Jim a raise above the threshold instead. The new minimum for exemption is $47,476—so let's propose increasing his salary to $50,000 to give ourselves some breathing room. The math here is simple:

Cost of a Raise

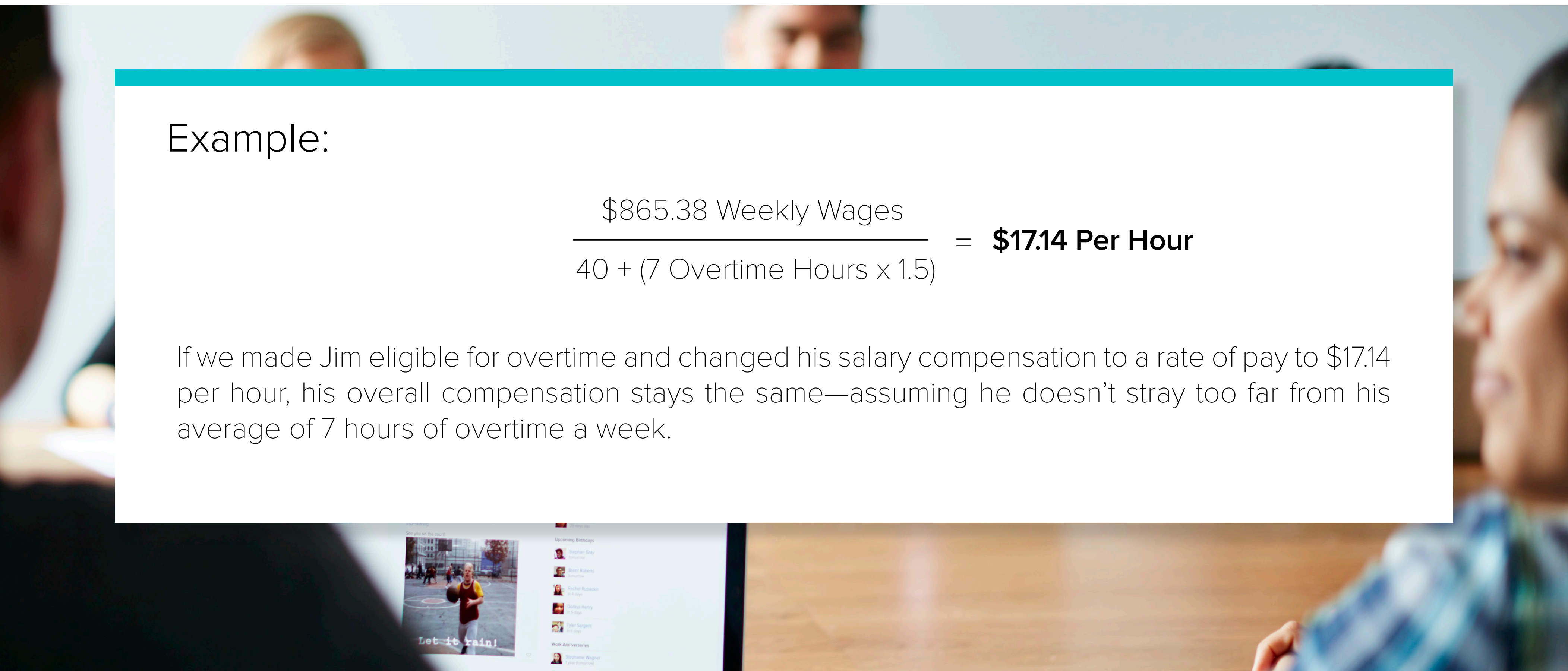
$50,000 - $45,000 = **$5,000**
$11,355.50 Annual Overtime > $5,000 Salary Increase

In this example, increasing Jim's salary above the threshold costs about $6,000 less than making him non-exempt.

$$\frac{\text{Weekly Wages}}{40 + (\text{Overtime Hours} \times 1.5)} = \textbf{New Hourly Wages}$$

Using the above formula is a "cost neutral" approach employers can take to altering compensation that entails making an employee nonexempt and reducing their base pay to an hourly rate that compensates for anticipated overtime.

Let's incorporate this new formula into our prior example:



Example:

$$\frac{\$865.38 \text{ Weekly Wages}}{40 + (7 \text{ Overtime Hours} \times 1.5)} = \textbf{\$17.14 Per Hour}$$

If we made Jim eligible for overtime and changed his salary compensation to a rate of pay to $17.14 per hour, his overall compensation stays the same—assuming he doesn't stray too far from his average of 7 hours of overtime a week.

Regarding Changes in Compensation

Just because one compensation option is more economical doesn't necessarily mean it's best for the employee. As with any changes regarding an employee's salary, be sure to make them inline with your company's total rewards commitment and in the context of each employee's contributions to your company. Salary centers on how much a manager and a company value an employee's work and time, so communicating any changes effectively—even those made solely due to compliance with the new rules—is paramount.

Additionally, the cost neutral formula does pose risks—if your estimate of an individual's overtime hours is off, that could result in a lower overall compensation for the employee. While cost neutral, the challenges of the approach may outweigh the benefits to your organization.

3

Communicate Changes and Train Employees and Managers

So your company has done its homework and made its classification decisions—now it's time to get everyone on the same page. Reclassified employees are not the only ones that need to be situated, though. Managers, or anyone who supervises employees, have to understand overtime rules and what constitutes on-the-clock work in order to keep your organization compliant.

Employees

Breaking the news to employees can be difficult and even emotional. Employees losing their exempt status may initially react as though they have been "demoted" or have lost workplace flexibility. Help placate these fears by reminding your people that overtime eligibility is a compliance matter and not a mark of status, rank, or performance. Entitling the employee to overtime pay is a means of ensuring just reward for their valuable time and energy—and depending on the circumstances, could even result in a bump in overall compensation.

Some employees may have never worked in a non-exempt position before. You will have to train these individuals not only on how to log their hours (time and attendance HR software could be useful here) but also on your company's policies governing overtime. Instruct employees on whether they can check emails after hours, work from home, or travel for work. Neither of the three actions are forbidden by the FLSA, but in the interest of cost, your company or department's policies may have preexisting policies discouraging them.

If the DOL's new rules have resulted in the reclassification of many of your employees, it would be wise to put together a fact sheet they can reference. The document should include instructions on how to log time, what "hours worked" really means, frequently asked questions, and a summary of your company's overtime policies. Anticipate that reclassified employees will come with questions regardless. Now would be a good time to brush up on FLSA rules to keep them fresh in your mind.

Managers

Getting managers up to speed with the changes can be even more difficult. Some managers may have never managed non-exempt employees before. You will need to train supervisors on timekeeping procedures, wage and hour policies, and what constitutes compensable work. For example, an employee casually checking work emails after hours could be construed as "working," even if they were not directly asked to by their manager. A DOL fact sheet on compensable time can be accessed here.

Managers should remember that their own work habits can influence non-exempt employees. If you want to curb non-exempt employees from unnecessarily working after hours, limiting the number of after hours emails you send is a good place to start. Similarly, the manager must also be mindful of what he or she asks an employee to do past regular working hours—if an employee has to stay late for a meeting or assignment, consider offering them a chance to come into the office late the next day. The FLSA entitles employees to pay for hours worked over 40 per week, not hours worked past 5 p.m. or any other specific time of day. Workplace flexibility does not end with overtime.

It's important to keep in mind that managers are not automatically exempt from overtime. For these special cases where the individual does not "pass" the duties or wages test, you should plan to devote time to train them on how to manage both their time and the time of their employees.

Stay on Top of Future Changes

The new rule provides that the minimum threshold for exemption will be updated every three years. While you should always be mindful of your employee classifications, plan to spend extra time every three years auditing them.

As previously mentioned, the threshold will be tied to the 40th percentile of earnings of full-time salaried workers in the census region with the lowest average wages. That being said, current **DOL estimates point to the threshold being approximately $51,000 in 2020**. Be mindful of that increase when you raise wages this year.

Conclusion

The Department of Labor's changes to overtime rules, if enacted, could lead to the reclassification of millions. Employers must be prepared for what comes next.

Complying with the rule doesn't have to be hard. See how Namely can make it easy to manage employee status and reclassification.

Learn More

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