BURR ALERT

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SIX OPTIONS FOR COMPLYING WITH NEW DOL FLSA SALARY RULES

By Ron Flowers

It is rare for an employee's salary to double with one raise, yet, under the Department of Labor's (DOL's) proposed rule, employers will need to double some employees' salaries to continue to pay them salaries without overtime. By now, everyone has heard of the Department of Labor's proposed rule increasing the required weekly salary to $970 per week, or $50,440.00 annually, for employees to be exempt from the Fair Labor Standards Act's (FLSA's) overtime provisions under most of the "white collar" exemptions. The proposed rule was published in the Federal Register on July 6, 2015, and the 60-day comment period expired on September 4, 2015. Although more than 250,000 comments were submitted to the DOL, the final rule is anticipated to closely resemble the proposed rule. The Administration is expected to act fairly quickly finalizing the rule, so employers can expect the final rule to be published and the changes to be implemented in early to middle 2016.

Designed to adjust for inflation the original 1975 salary requirements, the proposed rule more than doubles the current salary requirement of $455.00 per week or $23,660.00 per year. The FLSA requires employers to pay employees who do not meet an exemption 1.5 times their regular rate for hours worked over 40 in a workweek. The proposed rule sets the new salary requirements for the executive, administrative, professional, and computer professional exemptions,[1] which cover most salaried employees exempt from the FLSA's overtime provisions. To be exempt under one of the covered exemptions under the proposed rule, employees must receive a salary of at least $970.00 for each week they work and meet the exemption's duties test.

On first glance, options available for complying with the changes seem straightforward. Employers with a $40,000.00-salary employee working 50 hours a week will need to either (1) increase the salary by $10,400.00 to reach the threshold, (2) limit the employee to 40 hours per week and assign the work to other employees (which may result in hiring more employees), or (3) pay time-and-a-half overtime pay which would amount to $15,000.00 per year. Employers with a significant amount of salaried employees between $23,660.00 and $50,400.00 will face substantial heightened labor costs by adopting one of these options.

No doubt, most employers addressing the changes will choose one of these three options for bringing their formerly-exempt employees who have been paid between $23,660.00 and $50,439.99 per year into compliance. However, the FLSA does allow for other creative alternatives for those employers who cannot absorb the increased labor costs the above options would entail or have other reasons for not wanting to choose one of those options. The most common options are described and compared below, including the three listed above, plus (4) modifying the employee's pay by adjusting the salary or hourly rate, (5) paying a salary that compensates for more than 40

[1] The rule does not revise the outside sales exemption, one of the "white collar" exemptions. The outside sales exemption does not have a salary basis or level requirement as outside sales employees may be paid by commission.

hours in a week, or (6) adopting the fluctuating workweek method. The option that works for a particular employer will depend on that employer's needs and the pay and time worked of its employees.

1) RAISE SALARY TO THRESHOLD

HOW IT WORKS: Simply increase the employee's current salary to the new $50,440.00 annual threshold. Because the proposed regulations call for the Secretary of Labor to publish a revised threshold each year based on the 40th percentile of earnings for full-time salaried workers, the salary may have to be adjusted upwards each year to satisfy the threshold.

COST INCREASE: For an employee with a $40,000.00 annual salary, the yearly labor cost increase would be $10,440.00 for 2016 with the potential to increase each year due to the yearly threshold adjustment.

PROS: The employee will be happy with the salary increase. The position can be maintained as a salaried exempt position without paying overtime pay.

CONS: The labor cost increase is significant for employees with a salary that is not close to the threshold. The proposed automatic threshold escalation may result in a required increase every year.

MAKES SENSE FOR: Employees with salaries already near the $50,440.00 threshold.

2) LIMIT TO FORTY HOURS

HOW IT WORKS: The employee works a set schedule and is prohibited from working over 40 hours. Alternatively, the employee may work overtime only upon receiving proper authorization, which is provided only under limited circumstances.

COST INCREASE: None, if the employee works no overtime.

PROS: The labor costs will not increase unless additional employees must be hired to cover for the reduced hours. The employees' families will see them more.

CONS: Limiting an employee who used to work more than 40 hours to less than 40 hours will likely require adjusting job responsibilities and/or assigning work to other staff. Depending on the positions and the work performed, it may result in a need for additional staff. Additionally, enforcing a 40-hour limitation can be difficult, but failure to do so, may cause liability for unpaid overtime. We recommend implementing a detailed timekeeping policy for salaried employees limited to 40 hours or facing strict limitations on their ability to work over 40 hours.

MAKES SENSE FOR: Generally, an absolute overtime prohibition makes sense only for salaried employees who have little need to work over 40 hours. For employees who are allowed to work some limited overtime under a detailed overtime policy, cost increases will be small for the overtime they do work.

3) PAY SALARY PLUS TIME-AND-A-HALF OVERTIME PAY

HOW IT WORKS: The employee formerly paid only by salary will now receive 1.5 times his salary divided by 40 for every hour of overtime he works. Alternatively, converting the employee to an hourly rate of his former salary divided by 40 accomplishes nearly the same result. The only difference for the hourly employee would be that he would only be paid his actual hours worked and not the full salary if he did not work 40 hours.

COST INCREASE: Potentially substantial. The sample employee would receive $15,000.00 in additional pay annually, calculated by the weekly salary divided by 40 times 10 overtime hours for 52 weeks of the year. Employees who work more than 50 hours per week would receive even more.

PROS: The employees will be happy. The calculation is easy.

CONS: Labor costs will increase substantially depending on the number of employees affected and the number of overtime hours worked.

MAKES SENSE FOR: Generous employers with cash to spare.

4) PAY OVERTIME AT MODIFIED PAY RATE

HOW IT WORKS: The new regulations do not prevent employers from modifying an employee's pay to avoid significant pay increases. Therefore, employers may either lower the salary of the employee who will now receive overtime or convert him to an hourly rate that results in a similar amount of total pay to that he received before being eligible for overtime.

For the sample employee, to maintain annual total pay of $40,000.00 for a salaried employee who works 50 hours per week, the employee's salary would need to be reduced from $769.23 to $559.60 per week. Likewise, if his rate of pay were converted to $13.99 per hour and he continued to average 50 hours per week while eligible for time-and-a-half overtime pay, he would have an annual pay of $40,000.00.

COST INCREASE: Potentially nothing, depending on the calculation and if the hours worked by the employee track previous hours.

PROS: Adjusting the pay allows employers to minimize additional labor costs while maintaining the same hours worked for the employee.

CONS: Morale. Employees may not like having to work a particular number of hours to receive the same amount of pay they did before. Also, a reduction in workload would cause a pay decline.

MAKES SENSE FOR: Employers seeking to prevent any increased labor costs or to better control the increase in labor costs.

5) FIXED SALARY FOR GREATER THAN 40 HOURS

HOW IT WORKS: Contrary to popular belief, neither the Fair Labor Standards Act nor its regulations require overtime pay at 1.5 times an employee's salary divided by 40 for hours worked over 40. The appropriate calculation depends on the number of hours for which the salary was intended to compensate. If the salary is intended to compensate for 40 hours of work, the employee must receive 1.5 his hourly rate for hours worked over 40. If the employer intends the salary to compensate for a different amount of hours, it can designate in writing that an employee's salary is intended to compensate for a particular number of hours worked each week and the employee would only be entitled to 0.5 times overtime pay for hours worked over 40 up to that number. The employee would be entitled to 1.5 times the regular rate overtime pay for hours worked over that number.

For the sample employee, if he kept the same salary and the employer designated that his salary was to compensate for 50 hours, he would receive overtime pay at a 0.5 rate for time worked between 40 and 50 hours. The rate would be calculated by dividing his weekly salary of $769.23 by 50 hours, which would yield an overtime rate of $7.69 for each hour between 40 and 50. If he worked over 50 hours, he would receive pay for each hour at 1.5 times his regular rate which would be $23.07.

COST INCREASE: If the employee worked 50 hours each week with his salary compensating him for 50 hours, he would receive an additional $76.90 each week which would amount to just short of $4,000.00 per year. This amount would be larger if he ever worked more than 50 hours because he would then receive time-and-a-half pay.

PROS: Allows employers to maintain an employee's current salary without the substantial increased costs which would occur through time-and-a-half pay.

CONS: Provides for increased labor costs, albeit at a lower amount than time-and-a-half pay. Does not make sense for employees who may often work over the amount of hours the salary is intended to compensate.

MAKES SENSE FOR: Employers who want to maintain an employee's salary with limited increased labor costs and who have employees who work a fairly steady schedule.

6) FLUCTUATING WORKWEEK METHOD

HOW IT WORKS: Under the fluctuating workweek method, employees must receive at least 0.5 times their regular rate of pay for the week (calculated by dividing their weekly salary by the total hours worked for the week) for any time worked over 40 hours. The regular rate of pay for the week will vary based on the number of hours worked. To utilize this method, employees' weekly hours should actually fluctuate to some extent. Before implementing the fluctuating workweek method, employers should have a written understanding with each employee. Employers should consult with legal counsel before implementing the fluctuating workweek method to ensure the method is applied correctly and that it is appropriate for the employees covered.

COST INCREASE: For the sample employee, the additional costs would be similar to method 5 above except that if the employee exceeded 50 hours per week, the employer would still only need to pay 0.5 times the regular rate of pay for the week.

PROS: The cost increase for this method is less than any of the other methods (other than adjusting salary or limiting to 40 hours per week).

CONS: The method is more difficult to calculate and more difficult for the employees to understand. The method requires careful attention to ensure it is appropriate for the covered employees and that it is applied correctly..

MAKES SENSE FOR: Employers willing to undertake the administrative burden who have employees whose hours actually fluctuate to some extent from week to week.

To prepare for the final rule, employers should carefully analyze their employees' pay and the most effective and appropriate method for complying with the new requirements. One available option includes an attorney-client privileged FLSA audit and pay analysis to discuss the exempt status and pay options for employees covered by the proposed regulation. Burr & Forman attorneys have already begun conducting these audits to prepare for the implementation of the new rule.

Should you desire such an audit or have any other questions, please contact **me** in Birmingham at rflowers@burr.com or (205) 458-5176 or the Burr & Forman attorney with whom you normally work.