



## New Overtime Pay Rule

### —Overview—

On May 18, 2016, the U.S. Department of Labor (DOL) released its final rule updating overtime requirements for employers. The rule takes effect December 1, 2016 and makes three critical changes: raising the base salary employees must make to be excluded from overtime from \$23,660 to \$47,476; increasing the salary level for highly compensated employees from \$100,000 to \$134,004; and, automatically updating compensation levels every three years. This document provides guidance on these changes and the types of positions within an organization that may be exempt from overtime.

### —Background—

Enacted in 1938, the federal Fair Labor Standards Act (FLSA) (29 U.S.C. 201, et seq.) establishes minimum wage (\$8.38 in New Jersey), overtime pay eligibility, recordkeeping, and child labor rules.

With few exceptions, most businesses are covered under the law which requires employers to determine the pay status of all employees within their organization. This means deciding whether each employee is exempt from overtime, or, entitled to at least one and one-half times their regular rate of pay for any hours worked over 40 in a workweek.

Some employers consider an employee to be exempt from overtime because they pay the person on a salaried basis or provide them with a high-level title. This is not the case.

In making the decision that a worker is not eligible for overtime, there are three tests that should be considered: the *salary level test*, the *salary basis test*, and the *duties test*. In order for an employee to truly be exempt from overtime, all three tests must be met. The tests, and the impact of the new federal rule on them, are discussed below.

### —Salary Level Test—

The salary level test provides a base amount most employees must be paid to be exempt from overtime. One of the most significant changes made by the new overtime rule is increasing that base amount from \$23,660 (\$455 per week) to \$47,476 (\$913 per week) beginning December 1, 2016.

Under the rule, the new salary threshold of \$47,476 will automatically update to the 40th percentile of full-time salaried workers in the lowest wage region in the United States - currently the Southeast - every three years beginning in 2020. The first adjustment is likely to increase the salary level to \$51,168.

Being paid a salary means an employee regularly receives a predetermined amount of compensation each pay period on a weekly, or less frequent, basis. In New Jersey, most employers are required to pay wages at least twice during each calendar month, on regular paydays designated in advance by the employer. However, for certain executive, supervisory or other special classes of workers, payment can be made once a month as long as there is a regularly established schedule.

In the past, employers have not been permitted to use bonuses, commissions and incentive pay to satisfy any of the salary level test. However, under the new rule, as of December 1, 2016, employers can satisfy up to 10 percent of the salary level test with these incentives if they are paid quarterly. Employers can also make “catch-up” payments. Likewise, if an employee has not earned enough commissions to satisfy the salary level requirement on a quarterly basis, the employer can make up the difference.

### —*Salary Basis Test*—

The new overtime rule makes no changes to the salary basis test. That is, to qualify for the overtime exemption, employers must still pay employees a predetermined amount on a regular schedule; compensation can't be reduced because of problems with the quantity or quality of the work; and, the employee must be paid for a full week when any work is performed.

Generally speaking, pay deductions are only allowed for exempt (not overtime eligible) employees for the following reasons:

- An employee is absent from work for one or more full days for personal reasons other than sickness or disability;
- An employee is absent for one or more full days due to sickness or disability if the deduction is made in accordance with a bona fide plan, policy or practice of providing compensation for salary lost due to illness;
- To offset pay employees receive as jury or witness fees, or for military pay;
- For penalties imposed in good faith for infractions of safety rules of major significance; or,
- For unpaid disciplinary suspensions of one or more full days imposed in good faith for workplace conduct rule infractions.

Also, an employer is not required to pay the full salary in the initial or terminal week of employment, or for weeks in which an exempt employee takes unpaid leave under the Family and Medical Leave Act (FMLA) (29 U.S.C. 2601, et seq.).

Employers who have what's known as an “actual practice” of improper deductions risk the loss of overtime exemption status for all employees in the same job classification. An “actual practice” of improper deductions depends largely on the number of correct versus incorrect deductions; the time period over which the deductions were made; the number of employees affected; and, the geographic location of the employees affected by the deductions.

Isolated or accidental improper deductions generally will not result in the loss of the exemption if the employer reimburses the employee for the improper deductions. In fact, the DOL has a safe harbor policy for employers with: clear policies against improper deductions; established payroll complaint procedures; reimbursement policies for improper deductions; and, established efforts to comply in the future.

### **—Primary Duties Test—**

Employees who meet the salary basis and salary level tests must also meet a “duties test” to be excluded from overtime under what’s known as a “white collar exemption.” While there was much speculation that the new federal rule would change this test, it did not.

The white collar exemption excludes workers from minimum wage and overtime if they are bona fide executive, administrative, professional, outside sales employees, and certain computer employees. It also lays out a set of tasks that determine whether an employee falls into the exempt category because of their “primary duty” in any one of these areas.

Primary duty means the principal, main, major or most important duty that the employee performs. The amount of time spent performing exempt tasks can also be a useful guide. Employees who spend more than 50 percent of their time performing exempt work will generally meet the primary duty requirement. Time alone, however, is not the sole test as an employer may also want to consider the importance of the employee’s duties and the decision making power they hold.

Below are a list of the requirements and primary duties that must be met to qualify for either an executive, administrative, professional, outside sales employee, or computer white collar exemption:

#### Executive Exemption

- Earns at least \$913 per week (as of December 1, 2016).
- Primary duty is the management of the enterprise or a recognized department or subdivision.
- Customarily and regularly directs the work of two or more other employees.
- Has the authority to hire or fire other employees (or recommendations as to the hiring, firing, promotion or other change of status of other employees are given particular weight).

#### Administrative Exemption

- Earns at least \$913 per week (as of December 1, 2016).
- Primary duty is performing office or non-manual work directly related to the management or general business operations of the employer or the employer’s customers.
- Primary duty includes the exercise of discretion and independent judgment with respect to matters of significance.

#### Professional Exemption (Learned Professional)

- Earns at least \$913 per week (as of December 1, 2016).
- Primary duty is performing office or non-manual work requiring the knowledge of an advanced type in a field of science or learning customarily acquired by a prolonged course of specialized intellectual instruction, but which also may be acquired by alternative means such as an equivalent combination of intellectual instruction and work experience.

#### Professional Exemption (Creative Professional)

- Earns at least \$913 per week (as of December 1, 2016).
- Primary duty is performing work requiring invention, imagination, originality or talent in a recognized field of artistic or creative endeavor.

### Computer Employee Exemption

- Compensated either on a salary or fee basis at a rate not less than \$913 per week (as of December 1, 2016) or, if compensated on an hourly basis, at a rate not less than \$27.63 an hour;
- Employed as a computer systems analyst, computer programmer, software engineer or other similarly skilled worker in the computer field performing the duties described below:
  - 1) The application of systems analysis techniques and procedures, including consulting with users, to determine hardware, software or system functional specifications;
  - 2) The design, development, documentation, analysis, creation, testing or modification of computer systems or programs, including prototypes, based on and related to user or system design specifications;
  - 3) The design, documentation, testing, creation or modification of computer programs related to machine operating systems; or
  - 4) A combination of the aforementioned duties, the performance of which requires the same level of skills.

### Outside Sales Exemption

To qualify for the outside sales employee exemption, all of the following tests must be met:

- Primary duty must be making sales (as defined in the FLSA), or obtaining orders or contracts for services or for the use of facilities for which a consideration will be paid by the client or customer; and,
- The employee must be customarily and regularly engaged away from the employer's place or places of business.

### **—Highly Compensated Employee—**

In addition to the executive, administrative, professional, outside sales employee, and computer white collar exemptions, an employee may be exempt from overtime because they are considered highly compensated.

One of the most significant changes made by the new federal rule is increasing the salary level for highly compensated employees (HCEs) from \$100,000 to \$134,004, effective December 1, 2016. The salary level for HCEs is based on nationwide data for full-time workers and set at the 90th percentile. It will also automatically increase every three years.

A highly compensated employee is exempt from overtime if:

- The employee earns total annual compensation of \$134,004 or more (as of December 1, 2016), which includes at least \$913 per week paid on a salary basis;
- The employee's primary duty includes performing office or non-manual work; and,

- The employee customarily and regularly performs at least one of the exempt duties or responsibilities of an exempt executive, administrative or professional employee.

—***Why is this important?***—

Employers should take note of the new federal rule and take care in deciding whether an employee is exempt or entitled to overtime because improper classification of an employee could produce disastrous consequences. Since 2009, the U.S. DOL has collected more than \$1.3 billion in back wages for overtime. The agency has also assessed millions in civil penalties against non-compliant employers. More importantly, wage hour class actions concerning white collar exemptions continue to increase each year almost exponentially.

—***Should employers revise job descriptions?***—

Generally, employers should always keep job descriptions up-to-date and employees should understand a company's expectations at all times. If a job description (or even a change in an employee's responsibilities) leads an employer to conclude that an employee's status as overtime eligible may have changed, they should engage in an analysis or consult with counsel. Additionally, since the salary level required for an exemption increased dramatically, employers may want to categorize primary responsibilities by exemption status as well as track percent of time for each task.

Employers may take a number of preventive steps in an attempt to maintain compliance with overtime regulations. A self-audit (which includes review of job descriptions and interviews with employees in those positions) is the most common tool utilized by employers in determining whether its employees are properly classified as exempt.

—***Additional Resources***—

Questions and Answers: "Overtime Final Rule:"  
<https://www.dol.gov/whd/overtime/final2016/faq.htm>

—***For More Information***—

For more information, please contact NJBIA's Member Action Center at 1-800-499-4419, ext. 3 or [member411@njbias.org](mailto:member411@njbias.org).

*Updated: August 8, 2016*

This information should not be construed as constituting specific legal advice. It is intended to provide general information about this subject and general compliance strategies. For specific legal advice, NJBIA strongly recommends members consult with their attorney.