

Labor and Employment

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AALRR Alert



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U.S. Department of Labor Issues Final Regulations Increasing Salary Threshold Requirements for Exempt Employees

On May 18, 2016, the United States Department of Labor (“DOL”) published final regulations that will substantially increase the minimum salary that must be paid to exempt employees under federal law to \$47,476. The regulations will be effective December 1, 2016.

Under current federal law, each of the white collar exemptions (executive, administrative, and professional) require an exempt employee to be paid a minimum of \$455 per week, or \$23,660 per year on a salary basis as a threshold qualification for application of the exemption. Under the regulations, this will increase to \$913 per week, or \$47,476 per year.

By comparison, under California law white collar exemptions currently require a minimum annual salary of \$41,600. As employees in California may challenge their exempt classification under either the FLSA or California law, employers must comply with the exemption requirements of both federal and State law. Thus, with the federal salary threshold more than doubling and exceeding the current California

salary threshold, starting December 1, 2016 California employers will need to comply with the higher federal salary requirement.

The DOL reported that over four million U.S. employees are expected to qualify for overtime under the revised regulations.

The white collar exemptions are one of the most frequently litigated aspects of the FLSA. According to the Judicial Resource Center federal court filings alleging violations of the FLSA increased 7.6 percent from 2014 to 2015, and increased over 450 percent in the last fifteen years. It is expected that the new regulations will further increase scrutiny and litigation of employee exemption status.

DOL will publish the Fair Labor Standards Act (“FLSA”) regulations in the Federal Register, which may be viewed at [<https://www.dol.gov/WHD/overtime/final2016/>].

Increase in Salary Level Test

The new FLSA regulations focus primarily on updating the salary and compensation levels needed

for executive, administrative and professional employees to be exempt. Specifically, the final regulations:

- Set the standard salary level at the 40th percentile of earnings of full-time salaried employees in the lowest-wage Census Region, currently the South (\$913 per week; \$47,476 annually for a full-year employee);
- Set the total annual compensation requirement for highly compensated employees (“HCE”) subject to a minimal duties test to the annual equivalent of the 90th percentile of full-time salaried workers nationally (\$134,004) (Note: California does not have an

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equivalent exemption to the federal HCE exemption); and

- Establish a mechanism to automatically update the salary levels every three (3) years to maintain the level at the above percentiles and to ensure that the salary threshold continues to provide useful and effective tests for exemption. Future automatic updates to those thresholds will begin on January 1, 2020.

Additionally, the final regulations amend the salary level test to allow employers to use nondiscretionary bonuses, incentives, and commissions, which are paid quarterly or more frequently, to satisfy up to 10 percent of the new standard salary level.

Duties Tests Remain the Same

Although the DOL solicited comments regarding revising the duties tests, the DOL made no changes to the duties tests in the final regulations.

Impact on Employers

Employers in California will have to satisfy the higher federal salary level test, while also satisfying the more stringent duties test under California law for exempt employees to qualify as exempt under both federal and State law.

For California employers, the California salary exemption test is tied to the California minimum wage, which is set to increase January 1, 2017 to \$10.50 per hour (for employers

with more than 25 employees). This will increase the California minimum exempt salary level to \$43,680 per year, which will still be lower than the federal minimum salary level. In fact, California minimum salary levels will not exceed the federal minimum salary level until January 1, 2019, when the minimum wage for employers with more than 25 employees will increase to \$12.00, with a minimum salary for exempt employees of \$49,920. Both the federal and State salary levels are scheduled to increase further in 2020.

The new regulations are intended to dissuade employers from classifying employees as exempt from overtime. As a result, more employees will need to be reclassified as non-exempt and will become eligible for overtime, meal and rest periods, and the other required features of non-exempt compensation. Employers will also have to manage expectations of formerly exempt employees discouraged by the loss of freedom and esteem that comes with exempt pay status.

In order to comply with the December 1, 2016 exempt salary level increase, employers should use this time to reevaluate their use of exempt classifications and determine which employees will need to be reclassified as non-exempt. Employers who want assistance to ensure compliance with the new exempt salary level or assistance conducting an audit of existing exempt positions for future

qualification for exempt status are encouraged to contact the authors or their usual counsel at AALRR.