

EMPLOYMENT LAW ALERT



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WHAT EMPLOYERS NEED TO KNOW ABOUT RECENT CHANGES TO THE FLSA REGULATIONS

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On April 20, 2004, the U.S. Department of Labor (DOL) announced changes to the white collar exemptions (professional, administrative, executive, outside sales, and computer professionals) to the Fair Labor Standards Act (FLSA). The DOL estimates that 1.3 million additional employees will qualify for overtime pay under the new rules, which become effective on August 23, 2004. Employers must understand how they will be impacted by the new rules and take steps to be sure they are in compliance.

I. WHAT EMPLOYERS SHOULD KNOW

In order to qualify for an exemption to federal overtime regulations, employees must meet all three of the following tests: (1) Salary Test; (2) Salary Basis Test; and (3) Duties Test.

1. Salary Test – Minimum Salary Level Increased.

Under the old rules, an employee earning as little as \$155 per week (\$8,060 per year) could qualify as a “white collar” employee not entitled to overtime pay. The new rules have raised that salary threshold to \$455 per week (\$23,660 per year). If an employee works for less than a full year, the employer must pro-rate the salary to apply the test.

When determining an employee’s salary level, an employer may count an employee’s commission and non-discretionary bonus, but may not include board, lodging, medical insurance, life insurance, contributions to retirement plans, or fringe benefits.

- *Highly-Compensated Workers (\$100,000 or more)*

The new regulations contain a special rule for “highly compensated” workers earning an annual compensation of \$100,000 or more. An employee is exempt from overtime if (1) he earns \$100,000 or more annually, including at least \$455 per week paid on a salary basis; (2) the employee’s primary duty includes office or non-manual work; and (3) the employee customarily performs at least some of the duties of an exempt executive, administrative or professional employee.

- *Computer Employees* – Computer employees who earn at least \$27.63 per hour may also meet the salary test.
- *Outside Sales* – There is no salary requirement for outside sales employees.

- *Certain Professional Employees* – There is no salary level test for teachers, lawyers, doctors, medical interns or residents.
- *New Protected Categories* – Under the new regulations, certain categories of employees are entitled to overtime protection, regardless of how highly paid they may be:
 1. Manual Laborers (e.g., mechanics, plumbers)
 2. First Responders (e.g., police officers, fire fighters, paramedics)

2. Salary Basis Test

In order to qualify as an exempt executive, administrative or professional employee under the FLSA, an employee must be paid on a salary basis. An employee will be determined to be paid on a salary basis if the following conditions are met:

- Employee receives a pre-determined amount on a weekly or bi-weekly basis
- Employee cannot have pay reduced depending on output or productivity
- Employee must receive his/her full salary each week, regardless of how many days worked that week (unless employee did not work at all in a given week), subject to a number of permissible deductions (described below).

3. Duties Test – Discontinued Use Of Long and Short Tests (Including 20% Rule)

The new rules abandon the long and short duties tests, including the requirement that an otherwise exempt employee loses the exemption if he/she devotes more than 20% of his/her time to non-exempt work.

Executive Exemption – To qualify for an executive exemption, an employee must satisfy all 3 of the following:

- Primary duty is management of business or customarily recognized unit or subdivision thereof
- Customarily and regularly directs the work of 2 or more other employees (totaling at least 2 FTEs)
- Has authority to hire and fire or suggestions for hiring and firing accorded particular weight

Examples: Department manager, head of branch office

Note: An executive no longer qualifies as exempt simply because he/she is in charge of an independent establishment or a physically separated branch establishment.

Professional Exemption – To qualify for the professional exemption, an employee must satisfy the test for either the learned professional or the creative professional.

1. *Learned Professional* – Primary duty consists of performance of work requiring advanced knowledge in a field of science or learning customarily acquired by a prolonged course of specialized intellectual instruction; work must be predominantly intellectual in character and must include work requiring the consistent exercise of discretion and judgment.

Examples:

<u>Exempt</u>	<u>Non-Exempt</u>
chef	cook
lawyer	paralegal
registered nurse (R.N.)	licensed practical nurse (L.P.N.)
C.P.A.	bookkeeper

2. *Creative Professional* – Primary duty is the performance of work requiring invention, imagination, originality or talent in a recognized field of artistic or creative endeavor (e.g., music, writing, acting, graphic arts).

Examples: composer, cartoonist, actor, journalist

Administrative Exemption –

- Primary duty consists of office or non-manual work directly related to management policies or general operations of employer or of employer's customers, or the employee performs functions in the administration of a school system or educational establishment.
- Primary duty includes exercise of discretion and independent judgment with respect to matters of significance.

The exercise of discretion and judgment is an important part of the test. Mandatory compliance with a manual as a method of operation could disqualify an employee from the exemption – but using a manual as reference would not.

Examples: Human resource managers, certain executive assistants

Computer Employees Exemption – Employed as a computer systems analyst, computer programmer, software engineer, or other similarly situated worker in the computer field.

- Primary duty consists of (a) application of systems analysis techniques and procedures, including consulting with users, to determine hardware, software, or system functional specifications; or (b) 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; or (c) design, documentation, testing, creation or modification of computer programs related to machine operating systems; or (d) a combination of duties described in a, b, and c, the performance of which requires the same level of skills.

Outside Sales Exemption –

- Primary duty consists of making sales or obtaining orders or contracts for services or the use of facilities for which a consideration will be paid by a client or customer
- Customarily and regularly engaged away from the employer's place(s) of business

Note: Employers cannot avoid overtime by asking a sales representative to work from home.

4. Payroll Deductions –

Proper Deductions: The new rules permit deductions from the salary of exempt employees in certain circumstances:

- full day absences due to employee sickness
- safety violations – if penalty is applied in good faith and for reasons of serious danger (e.g., smoking in oil refinery)
- qualified absence under Family and Medical Leave Act
- unpaid disciplinary suspension for violations of workplace conduct rules, such as workplace violence or sexual harassment, but only if pursuant to written policy

Improper Deductions: Employers who make deductions from employee pay for improper reasons risk changing the classification of not only that particular employee, but all employees similarly situated, which could have significant financial costs to the employer. Examples of improper deductions include:

- absences caused by employer where employee was ready and willing to work

Safe Harbor: Employers who take the following steps have a safe harbor that will prevent reclassification of employees for making an inadvertent error regarding wage deductions:

- Written policy
- Compliance procedure
- Reimburse employees for missed overtime pay
- Good faith effort to comply with regulations

5. Union Contracts – The new regulations explicitly provide that the regulations do not relieve employers of their obligations under union contracts.

II. WHAT EMPLOYERS SHOULD DO

- Conduct an audit – Employers should use the time between now and the effective date of the new regulations (August 23, 2004) to conduct an audit of their current employee job classifications and make any necessary changes. To conduct an audit, employers should (1) review (or create) written job descriptions, including tasks and skills; (2) compare the actual duties performed by employees to those in the job descriptions (DOL applies a functional test - actual duties govern); and (3) compare the actual duties with the DOL tests for exemption.
- Alter Responsibilities or Salary – Employers may wish to alter responsibilities or salary of certain jobs so that more employees become exempt. For example, if an employee is earning less than \$455 per week, it may be more cost effective to increase that employee's salary, making him/her exempt, than it would be to pay overtime, or it may be worth offering additional discretion or hiring/firing authority to certain employees.
- Maximum 40 Hour Week – Employers may wish to limit employee hours to a maximum of 40 hours per week, and hire more employees to work the overage. The increased costs of more employees on the payroll (benefits, etc.) may outweigh the cost of overtime pay.
- Re-classify Employees – Employers may not only need to reclassify employees to comply with the new regulations, but during the audit, may discover that certain employees have been misclassified under the old rules. Employers may be able to use a complete reclassification consistent with the new rules to correct previously improper misclassifications.
- Workplace Conduct Policies – Employers should be sure that they have written workplace conduct policies in place (e.g., sexual harassment and workplace

violence) before taking any deductions from employee pay for absence due to these reasons.

- Safe Harbor – Employers should establish written policies to further their compliance with regulations and prevent loss of exempt classifications.

If you would like further information about the new changes to the FLSA regulations, or to set up a time to conduct an audit, please speak to any of the PLGT employment attorneys. Additional information is also available on the DOL website at www.dol.gov/esa/regs/compliance/whd/fairpay/main.htm