

The U.S. Department of Labor Moves to More Than Double Minimum Salary Levels

Proposed changes may impact millions of exempt employees.

By Julia E. Judish, John Scalia and Paula M. Weber

On July 6, 2015, the U.S. Department of Labor published a long-awaited Notice of Proposed Rulemaking (NPRM) to amend the Fair Labor Standards Act (FLSA) regulations implementing the exemption from minimum wage and overtime pay for executive, administrative, professional, outside sales and computer employees (known as the “white collar” or “EAP” exemptions). The proposed rule would more than double the minimum salary level required to meet the executive, administrative, or professional exemption, to \$50,440 annually—much higher than any current state law requirement—with automatic increases in that threshold every year. The DOL estimates that of approximately 144.2 million wage and salary employees in the United States, 21.4 million are currently exempt EAP employees who would become eligible for overtime payments if the proposed rule goes into effect.

Background on the FLSA

The FLSA mandates that employers pay employees a minimum wage and pay premium overtime at 1.5 times their regular rate for all hours worked over 40 in a workweek, unless the employee is classified as exempt from these requirements. To qualify for the executive, administrative or professional white-collar exemptions, a position must meet three tests: (1) the employee must be paid a predetermined and fixed salary that is not subject to reduction because of variations in the quality or quantity of work performed (the “salary basis test”); (2) the amount of salary paid must meet a minimum specified amount (the “salary level test”); and (3) the employee’s job duties must primarily involve executive, administrative or professional duties as defined by the regulations (the “duties test”). The proposed rule was developed to fulfill President Obama’s March 13, 2014 Presidential Memorandum that directed the Department of Labor to “modernize and streamline the existing overtime regulations,” which has led to widespread anticipation of revisions to the duties tests. The proposed rule, however, amends only the salary level test, although it hints at further

changes to come. The NPRM does not include any proposed changes to the exemptions for highly paid hourly computer employees or outside sales employees.

Since 2004, when the regulations were last amended, the minimum salary for the EAP exemption has been set at \$455 per week, or \$23,660 annually. The Department of Labor proposes instituting an automatic annual salary level update using either a fixed percentile of wages or the Consumer Price Index for All Urban Consumers (CPI-U). For 2015, the proposed rule would set the minimum EAP salary level at \$970/week or \$50,440 annually, equivalent to the 40th percentile of earnings for full-time salaried workers, based on first quarter 2015 data. Although the specific proposed regulatory language does not address including non-salary compensation in this measure, the NPRM mentions that “the Department is also considering whether to allow nondiscretionary bonuses to satisfy some portion of the standard test salary requirement,” with a “cap[] at 10 percent of the salary level if such a provision were adopted” and a requirement that such bonuses be paid at least on a monthly basis.

Highly Compensated Employees Are also Impacted

The proposed rule also addresses the salary level for the existing white collar exemption for highly compensated employees (HCEs), which exempts from overtime eligibility any employee whose total annual compensation is at least \$100,000, if the employee’s primary duty includes performing office or non-manual work and the employee customarily and regularly performs any one or more of the exempt duties or responsibilities of an executive, administrative or professional employee, even if the employee does not meet the other requirements for EAP exemption. Under the proposed rule, the annual compensation level for the HCE exemption would be set at the 90th percentile of earnings for full-time salaried employees, or \$122,148 annually in 2015.

In addition to the proposed changes to the salary level regulations, the NPRM explains that the Department of Labor is “considering whether revisions to the duties tests are necessary in order to ensure that these tests fully reflect the purpose of the exemption.” Although it includes no specific proposals relating to the duties tests, the NPRM expressly invites comments on whether the current duties tests “may allow exemption of employees who are performing such a disproportionate amount of nonexempt work that they are not EAP employees in any meaningful sense.” The NPRM signals some potential changes: “Possible revisions include requiring overtime-ineligible employees to spend a specified amount of time performing their primary duty (e.g., a 50 percent primary duty requirement as required under California state law) or otherwise limiting the amount of nonexempt work an overtime-ineligible employee may perform, and adding to the regulations additional examples illustrating how the exemption may apply to particular occupations.” Any changes would likely make it more difficult to classify an employee as exempt.

The Government Describes Its Rationale as Supporting “The Heart of What It Means to Be Middle Class in America”

In a [column published on June 29, 2015](#), in the *Huffington Post*, President Obama explained that the amended FLSA regulations are designed under the principle that “a hard day’s work deserves a fair day’s pay,” which he describes as “the heart of what it means to be middle class in America.” There is no question that the current minimum salary levels for the EAP exemptions are too low to bring an employee’s family into the middle class, as the \$23,660 annual minimum salary falls below the [2015 federal poverty guidelines](#) for a family of four.

The NPRM acknowledges that the proposed FLSA amendments would entail a significant cost for employers, as the new salary level standards would “transfer income from employers to employees in the form of higher earnings,” and implementation of the rule will also entail adjustment and managerial costs. On the other hand, the Department of Labor anticipates benefits to employers from a reduction in litigation costs as a large set of lower paid exempt employees who are more likely to challenge non-payment of overtime are converted to overtime eligibility. In addition, the NPRM cites expected societal benefits from

these changes, as higher incomes “may result in reduced need for social assistance (and by extension reduced social assistance expenditures by the government).”

The good news for employers is that the changes proposed in the NPRM will be simple to identify and implement, and that there is still ample time to anticipate and effect these changes. Public comments on the proposed rule may be submitted on or before September 4, 2015. After the 60-day comment period closes, the Department of Labor will revisit the proposed amended regulatory language before publishing the final rule. Employers should also keep in mind that some jurisdictions, such as California, will continue to set a higher bar for exempt classifications under more stringent duties tests.

If you have any questions about the content of this alert, please contact the Pillsbury attorney with whom you regularly work, or the authors below.

Julia E. Judish [\(bio\)](#)
Washington, DC
+1.202.663.9266
julia.judish@pillsburylaw.com

John Scalia [\(bio\)](#)
Washington, DC
+1.202.663.8174
john.scalia@pillsburylaw.com

Paula M. Weber [\(bio\)](#)
San Francisco
+1.415.983.7488
paula.weber@pillsburylaw.com

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