How Does the New Overtime Rule Impact Highly Compensated Employees? 5 Answers for Employers

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Many employers are scrambling to comply with the Labor Department's new salary threshold for employees who are exempt from overtime pay under the white-collar exemptions. As the July 1 deadline for phase one rapidly approaches and you review your payroll and budget, you may have detailed questions about how these significant changes impact your workplace. For instance, what exactly does it mean to be a "highly compensated employee," and do you really have to pay them $132,964 to be exempt? Here are the answers to five of your top questions on how the new overtime rule applies to highly compensated employees. *If you want to learn even more about the new overtime rule, register for our June 26 webinar where we'll take a deep dive into this topic and answer your most challenging questions about all aspects of the OT Rule.*

1. What's Changing Under the New Rule?

Under the federal Fair Labor Standards Act (FLSA), employees generally must be paid an overtime premium of 1.5 times their regular rate of pay for all hours worked beyond 40 in a workweek — unless they fall under an exemption.

Although there are various exemptions, the new salary threshold applies to the executive, administrative, and professional exemptions — which are collectively known as the "white-collar" exemptions.

Currently, the standard salary threshold for these exemptions is $684 a week ($35,568 annualized). The Department of Labor's (DOL's) new rule raises the rate first to $844 a week ($43,888 annualized), then to $1,128 (or $58,656 a year). These significant increases will require some planning if you have exempt employees who earn less than the finalized amounts.

Additionally, the threshold for the "highly compensated employee" (HCE) exemption will rise, first to $132,964 on July 1, then to $151,164 on January 1, 2025 – which is a bigger increase than the DOL initially proposed and is a significant increase from the current $107,432. Notably, the exempt salary threshold and the HCE threshold will be updated every three years under the new rule.

2. But What Exactly Is the HCE Exemption?

First, you should note that the white-collar exemptions have more requirements than just the salary threshold. To qualify for these exemptions, employees must meet three criteria:

- Be paid on a salary basis;
- Be paid at least the designated minimum weekly salary; and
- Perform certain duties.

The "duties test" for each white-collar exemption is critical to determining whether an employee actually qualifies as exempt from federal minimum wage and overtime rules. This is where the HCE exemption comes into play. The DOL applies a reduced duties test if the employee's salary meets or exceeds the HCE threshold. So, that means, an employee's exempt status will be evaluated under the more relaxed duties test if they are now earning at least $107,432 in total annual compensation, and if they earn at least $132,964 on July 1, and $151,164 on January 1, 2025.

Under the HCE exemption, employees must currently earn at least the standard $684 salary threshold each week on a salary or fee basis, and the rest can be earned through commissions, nondiscretionary bonuses, and other nondiscretionary compensation during a 52-week period (but not through credit for board, lodging, or other facilities; payments for medical or life insurance; or contributions to retirement plans or other fringe benefits).

As the standard salary threshold rises, so will the amount highly compensated employees need to earn on a weekly basis to qualify for the exemption. So, that means they'll need to earn at least $844 each week on a salary or fee basis starting July 1, and $1,128 starting January 1, 2025.

If you have more questions about how to calculate total annual compensation for the HCE exemption, register for our June 26 webinar here.

3. What Are the Duties Requirements?

Here is a summary of the basic requirements under federal law for the white-collar exemptions. Of course, the salary basis test must be met before any of these exemptions can be relied upon.

Executive Exemption:

- The employee's primary duty must be to manage the enterprise or customarily recognized department/subdivision;
- The employee must customarily and regularly direct the work of at least two or more other full-time employees or their equivalent; and
- The employee must have the authority to hire or fire employees, or the employee's suggestions and recommendations as to hiring, firing, or any other change of status must be given particular weight.

Administrative Exemption:

- The employee's primary duty must be the performance of office or non-manual work directly related to the management or general business operations of the employer or its customers; and
- The employee's primary duty includes the exercise of discretion and independent judgment with respect to matters of significance.

Professional Exemption:

- The employee's primary duty must be the performance of work requiring advanced knowledge, predominantly intellectual in character and which requires the consistent exercise of discretion and judgment;
- The advanced knowledge must be in a field of science of learning; and
- The advanced knowledge must be customarily acquired by a prolonged course of specialized intellectual instruction.

Highly Compensated Employee Exemption:

- The employee's primary duty must be office or nonmanual work.
- The employee "customarily and regularly" performs at least one of the bona fide exempt duties of an executive, administrative, or professional employee, as described above.

What sort of job may qualify for the HCE exemption? You could have a highly paid employee who manages a department and is responsible for supervising two or more full time employees but who lacks the authority to hire and fire them. Or, alternatively, the same employee could qualify even if they don't supervise anyone directly but do have the authority to hire and fire employees.

It is important to remember to always check state law, too, as your jurisdiction may have more-stringent wage and hour requirements.

4. Do You Have to Raise a Highly Compensated Employee's Salary to the New Level?

If a particular employee meets the standard duties test under the executive, administrative, or professional exemption, then they need only be paid at least the standard salary threshold ($844 on July 1) and ($1,128 in 2025).

However, if your employee does not meet the standard duties test – but they do meet the reduced duties test for the HCE exemption – then to qualify for the exemption, they must be paid at least the HCE threshold of $132,964 on July 1, and $151,164 on January 1, 2025.

5. Can You Expect a Court to Halt the New Rule?

A coalition of business groups filed a lawsuit on May 22 claiming the DOL exceeded its authority by setting the salary threshold too high and requiring automatic increases every three years.

Although the rule is now in legal limbo thanks to the lawsuit, you can't count on a court blocking it – so you should keep preparing for it to take effect as planned. You can read more about the legal challenge and your key takeaways here.

Dive Deeper!

Want to learn more? Register for our June 26 webinar where we'll take a deep dive into this topic and answer your most challenging questions.

Conclusion

We will continue to monitor developments from the DOL's Wage and Hour Division, so make sure you are subscribed to Fisher Phillips' Insight System to get the most up-to-date information. For further information, contact your Fisher Phillips attorney, the authors of this Insight, or any attorney in our Wage and Hour Practice Group.

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