Department of Labor’s Final Rule Increasing FLSA Salary Thresholds for Exempt Employees

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DOL's Rule Increasing FLSA Salary Thresholds

- On April 23, 2024, the DOL issued a final rule that will increase the minimum salary threshold for some of the FLSA's overtime exemptions.

- Applicable to employees falling under the Executive, Administrative, Professional, and Computer exemptions:

  ✓ <u>July 1, 2024</u>: the salary threshold for exempt employees increased from $684 per week (i.e., $35,568 annually) to **$844 per week** (i.e., **$43,888 annually**).

  ✓ <u>January 1, 2025</u>: this salary threshold will again increase to **$1,128 per week** (i.e., **$58,656 annually**).

  ✓ The salary thresholds will increase automatically every three years thereafter to keep up with inflation.

DOL's Rule Increasing FLSA Salary Thresholds

- Applicable to employees falling under the "highly compensated employees" exemption:
  - ✓ July 1, 2024: the salary threshold for highly compensated employees increased from $107,432 annually to **$132,964 annually**.
  - ✓ January 1, 2025: the salary threshold for highly compensated employees will increase to $**151,164 annually**.

Highly Compensated Employee Exemption

Meeting the HCE exemption:

- Perform office or non-manual work;
- Paid total annual compensation of **$132,964** or more;
- Customarily and regularly perform <u>at least one of the duties </u>of an exempt executive, administrative or professional employee identified in the standard tests for exemption.

Employees can still fall under the Executive, Administrative, Professional, or Computer exemptions if they do not fall under the Highly Compensated Exemption.

Checklist for Compliance

- Review your pay policies, including job descriptions and job duties to ensure employees are properly classified.
- **Phase 1** (if you haven't already):
  - Identify all exempt employees who met the former salary requirement of $35,568 but make less than $43,888.
  - Identify all highly compensated employees who make more than $107,432 but less than $132,964.
- **Phase 2**:
  - Identify all exempt employees who make more than $43,888 but less than $58,656.
  - Identify all highly compensated employees who make more than $132,964 but less than $151,164.

Checklist for Compliance

- Notify affected employees of changes to compensation and other job conditions.
    - Increase the employee's compensation to remain exempt.
    - Re-classify the employee as non-exempt.

- Reminder: don't get so caught up on numbers that you forget about the employee's duties!

Regular Rate of Pay Calculations for Nondiscretionary Bonuses and Commissions

Overtime Overview

Regular Rate of Pay

- The regular rate is based on “all remuneration” earned from employment (except for eight specific exclusions contained in section 7(e) of the FLSA).

- The amount of overtime pay due to an employee is based on the employee’s regular rate of pay and the number of hours worked in a workweek.

Regular Rate of Pay

- The regular rate includes all types of compensation – including things like non-discretionary bonuses, commissions, payments for undesirable shifts or duties, and some non-cash payments depending on the circumstances.

Regular Rate Formula Under the FLSA

Regular Rate for the workweek **=** Total compensation in the workweek (except for statutory exclusions) **÷** Total hours worked in the workweek

Calculate Regular Rate for Overtime Purposes

Step 1: Determine if the bonus should be included in the overtime calculation.

Step 2: Define the time frame.

Step 3: Calculate the regular rate of pay for the time frame.

Step 4: Calculate total compensation due.

Regular Rate Question

An intermediate care facility for the disabled pays its employees on a bi-weekly basis. If employees work all the hours that they are scheduled to work in a pay period, they are given a **$100 bonus**.

<u>Question</u>: If an employee works overtime, must this bonus be included in their regular rate of pay for overtime purposes?

Answer: Yes

- In computing an employee's regular rate, the employer must add half of the bi-weekly bonus ($50) to the employee's earnings for that week.
- The resulting total compensation would be divided by the total hours the employee worked during that week to determine the regular rate.

Calculation

An employee paid biweekly at a rate of $12 per hour plus a $100 attendance bonus, working a schedule of **56 hours per week**, would be due overtime pay as follows:

- $100 (bi-weekly attendance bonus) ÷ 2 = $50 (weekly bonus equivalent).
- 56 hours worked x $12/hour + $50 (weekly bonus equivalent) = $722 (total straight time compensation).
- $722 (total ST compensation) ÷ 56 hours worked = **$12.89 (regular rate)**.
- $12.89 (regular rate) x ½ = $6.45 (half-time premium).
- $12.89 (regular rate) + $6.45 (half-time premium) = **$19.34 (overtime rate)**.

Exclusions From Regular Rate of Pay

29 USC § 207(e) provides an exhaustive list of types of payments that can be excluded from the regular rate of pay when calculating overtime compensation. There are eight categories of pay that may be excluded from the regular rate. This includes **discretionary bonuses**.

Discretionary Bonuses

Three requirements need to be met to be considered discretionary:

1. The employer has the sole discretion whether or not to pay;
2. The employer has sole discretion to determine the amount of the bonus; and
3. The payment is not made pursuant to a contract, agreement or promise causing employee to expect the payments regularly.

Nondiscretionary Bonuses

Examples of nondiscretionary bonuses that must be included in the regular rate include:

- Bonuses based on a predetermined formula, such as individual or group production bonuses;
- Bonuses for quality and accuracy of work;
- Bonuses announced to employees to induce them to work more efficiently;
- Attendance bonuses; and
- Safety bonuses (i.e., number of days without safety incidents).

Discretionary Bonuses

True or false: most bonuses are non discretionary.

Look Back Calculation

Employee's hourly rate is $15 per hour. Employer gives employee a non-discretionary bonus of $200 at the end of the month for reaching certain goals during that month.

Employee worked the following hours:

Week 1 – 40
Week 2 – 42
Week 3 – 40
Week 4 – 45

Look Back Calculation

To calculate the total additional overtime due related to the bonus, consider the following:

- 167 hours worked at $15 per hour = $2,505.
- $200 end of month bonus.
- Total Remuneration = $2,705 ($2,505 + $200).
- Regular rate = $16.20 ($2,705/167).
- Overtime premium = $56.70 ($16.20 per hour regular rate x .5 overtime premium x 7 overtime hours).
- **Total compensation due = $2,761.70** ($2,705 + $56.70).

Weighted Average Method

What if an employee is paid at more than one rate of pay?

Employee works a total of 50 hours during the week. This consists of 40 hours at his ordinary rate of pay of $25 per hour, and 10 hours at the travel rate of pay of $15 per hour.

Weighted Average Method

The weighted average would be calculated as follows:

$25 per hour x 40 hours = $1,000
$15 per hour travel rate x 10 hours = $150
Employee's total hourly pay = $1,150

Weighted average rate of pay = $23 per hour ($1,150 / 50 total hours)
Overtime premium = $115 ($23 per hour x 0.5 x 10 overtime hours)
Total compensation = $1,265 ($1,150 hourly pay + $115 overtime pay)

Takeaway

- When calculating overtime for employees, ensure that the regular rate of pay is being used.
- Make sure you are prorating non-discretionary bonuses and commissions over the appropriate time period in which they were earned. This will require the look-back calculation.
- Ensure that *all* rates of pay have been factored into the regular rate.
- Conduct internal wage and hour audit with outside counsel.

De Minimis Doctrine under the FLSA

De Minimis Doctrine

- Employees generally cannot recover for otherwise compensable time if that time is de minimis.

- The US Supreme Court first articulated the so-called de minimis doctrine in *Mt. Clemens*, concluding that employers are not required to include in an employee's hours worked "insubstantial and insignificant" time spent performing otherwise compensable preliminary or postliminary activities.

De Minimis Doctrine

In *Lindow v. United States*, the Ninth Circuit established a three-prong test for determining whether otherwise compensable time is de minimis. Using that test, the court considers:

- The practical administrative difficulty of recording the additional time.
- The aggregate amount of compensable time.
- The regularity of the additional work.

Cariene Cadena v. Customer Connexx LLC

- The case involves Nevada call-center workers who allege that their employer, *Connexx*, violated the Fair Labor Standards Act (FLSA) by failing to pay employees overtime wages for the time spent booting up and shutting down their computers each day.

- The Ninth Circuit recently held that the de minimis doctrine remained applicable for overtime wages under 29 U.S.C. § 207.

What can be done?

Ensure timekeeping policies provide that employees must be compensated for all hours worked.

Provide a mechanism to request that time is added in the event of a slow computer boot up – such as in the event of a software update, a bug, or some other obstacle – that takes the employee more than a mere few seconds or minutes.

Enforce the policies.

Train employees on the policy.

Train supervisors on documenting timekeeping adjustments.

Assess the applications and programs an employee must open before they can clock in; assess how long it takes from booting up to clocking in on their computer.

Commission and Incentive Pay

Commission

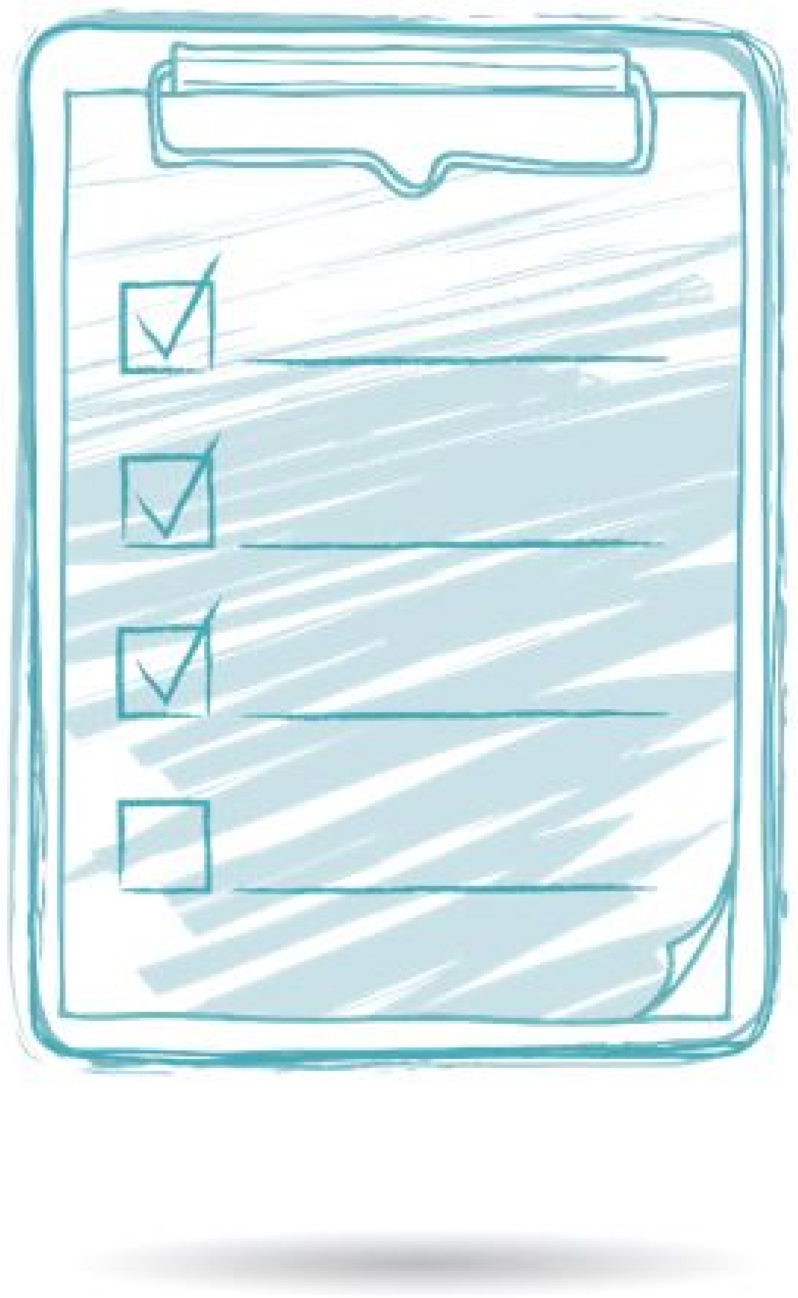
Commissions are considered **wages**.

A commission plan or agreement must be **clear**. Any ambiguity will be interpreted against the drafter.

(Some states, including CA, require written agreements.)

Agreements are key in assessing:

- Eligibility, Conditions and Prerequisites
- When Earned
- Calculations + Deductions
- When Payable
- When Forfeited
- Post-Termination Commission Payments



Commission Payments Following Termination

Your **agreement** is critical in assessing post-termination commission pay.

- Specify how and when commission are considered earned.
- Some state laws, in absence of an agreement, recognize the efforts of the individual that caused the sale/transaction to occur.

Some courts will not honor agreement providing for **forfeiture of commission** on termination when all **conditions** to earn commission were satisfied prior to termination.

- This underscores the importance of specifying all conditions for earning commissions.
- Example: specify the expectation to perform post-transaction services for a period of time.

Pay attention to state law:

- When is the final paycheck due?
- When are unpaid wages due?

Other Commission Considerations

- Do you offer minimum guarantees or draws against commission?
- Are commissions split among contributors?
- How are commission disputes resolved?
- What events cause deductions or forfeiture of commission?
- Do you provide paid time off to commissioned employees? (Some states require paid sick leave.)
- What types of compensation can employees expect during a leave of absence?

Executive Compensation
Hot Topics

EXECUTIVE COMPENSATION

1. Executive Agreements
2. Transactions and Change in Control
3. Incentive Plans
    1. Short-Term
    2. Long-Term
    3. All Staff v. Executive
4. Retention Agreements
5. Leaves of Absence and Departures

SECTION 409A

(1) Why comply with 409A?

- 20% penalty tax on the employee
- Interest charges
- Possible early income inclusion
- Employer has withholding and reporting obligation
- Compliance required both in operation and form

(2) Does 409A apply?

- Applies only to "deferred compensation" - any form of compensation which is or may be paid in a year following the year in which the legal right to the payment arises.
- Also important exceptions
  - Short term deferral
  - Separation pay exception (2X2 rule)

SECTION 409A

(3) How to comply -

- Deferred compensation may be paid upon 1 of 6 events:
  - On a fixed date or fixed schedule
  - Separation from service (as defined)
  - Death
  - Disability (as defined)
  - Change in control (as defined)
  - Unforeseen emergency
- Very restrictive distribution limitations
  - Payments cannot be left to discretion of the employer or employee

SECTION 280G – GOLDEN PARACHUTES

Section 280G is an important consideration when an employer undergoes a sale of the business – either an equity or asset sale

(1) What Section 280G does:

- Denies a tax deduction for the employer and imposes a 20% excise tax on an executive who receives an "excess parachute payment" as a result of a Change in Control

(2) What is an "excess parachute payment" ?

- Payment triggered by change in control that is three times (3X) the average annual W-2 compensation of an officer, 1% shareholder, or 1% "highly-compensated employee"

- Consider severance pay, transaction bonuses, pro-rated annual bonuses, acceleration of unvested equity, COBRA premiums paid by employer, auto allowance, acceleration of unvested deferred compensation, etc. —

SECTION 280G – GOLDEN PARACHUTES

(3) Action Steps

- Track all officers, shareholders, and "highly-compensated employees" eligible for deferred compensation on "Change in Control"
- Track size and number of awards and consider potential Section 280G impacts on amounts of deferred compensation
- Remember – if your company is an S-Corporation, you can avoid the implementation of Section 280G by approving the award by shareholder vote *in advance of the transaction – "280G cleansing vote*"
- Consider other exclusions

  - "reasonable compensation"

  - payments for stock

  - payments for services rendered after the transaction

SECTION 4960 EXCISE TAX

Excise tax applicable only to tax-exempt organizations (e.g., Section 501(c)(3) orgs, 501(c)(12) electric cooperatives, etc.)

(1)What is the Section 4960 Excise Tax?

- Applicable tax exempt organizations paying "remuneration" in excess of $1 Million in salary to executives are subject to a 21% excise tax (based on the corporate income tax rate)
- Tax also applies on any "excess parachute payment" (calculated similarly to the 280G excise tax)

SECTION 4960 EXCISE TAX

(2) Why does it matter in the deferred compensation context?

- If you don't work for a tax-exempt organization, it doesn't matter
- If you do – Section 4960 does not follow the regular tax treatment of deferred compensation
- Most notably – Payments under a Section 457(b) deferred compensation plan will be treated as "remuneration" for purposes of Section 4960 when no longer subject to a substantial risk of forfeiture

    - For tax purposes – 457(b) plan likely has a payout in the year following retirement/death/disability

    - BUT – for Section 4960 purposes – distribution treated as "remuneration" upon retirement/death/disability

(3) What to do?

- **Consider amending plan to spread realization for Section4960 purposes over multiple years**

SECURE ACT 2.0

(1)EPCRS Expansion
(2)Required Minimum Distributions
(3)Long-Term, Part-Time Workers
(4)De Minimis Incentives to Improve Participation
(5)Simplified Notice Requirements for Unenrolled

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