Outsmart the Pending Changes to the Overtime Law with Advance Planning

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In June we alerted you to the fact that the Department of Labor ("DOL") was planning to increase the minimum weekly salary an employee must be paid in order to qualify for an exemption from overtime. Since that time, the DOL has published a proposed rule increasing the salary basis test from its current $455 per week minimum ($23,660 per year) to $970 per week ($50,440 per year), with incremental increases thereafter. With the comment period now closed, employers can expect that the DOL will implement a final rule (with or without changes) in the second half of 2016. Once the final rule takes effect, DOL estimates that over five million more workers will qualify for overtime payments.

Being unprepared for the potential change will leave many affected employers with no choice but to simply pay employees higher wages. But if employers prepare now by taking the following steps, they can avoid the majority of the increased costs.

Understand if your Company Will be Affected.

It is important for employers to understand whether, and to what degree, they will be affected by the new salary threshold.

While it is possible that the final rule might set the new salary threshold lower than $970 per week, it is unlikely that it will be set higher. Thus, companies are likely safe to assume that as long as their exempt employees make more than $970 per week, they will maintain their exempt status. However, the new threshold is expected to increase over time so employers are wise to re-examine this issue on a yearly basis.

Furthermore, as a practical matter, the minimum salary of an employee will not be affected even if the employee is making less than $970 per week if the employee does not work more than 40 hours in a week. Such employees can continue to be paid a salary of less than $970 per week. Of course, since the employees will now be considered non-exempt, they must be paid the overtime rate if they do work in excess of 40 hours in a given week.

However, employers should be careful to not cavalierly believe that "it won't affect us since our guys never work more than 40 hours a week." Employers need to understand that "working time" includes not just time in the office or required working time – it includes any and all work. For example, time traveling to locations that are further away than the employee's home base, taking calls outside of office hours, staying late, coming in early, working through lunch, working from home (e.g. checking those emails at night), and attending activities that are encouraged by the employer and which benefit the employer, such as client dinners, company meetings or training, ***all count as hours worked*****.**

Finally, even if an employer believes the employee will not be affected because he or she works less than 40 hours per week, those employees are now classified as non-exempt, thus entitled to all the associated benefits. For example, employers should be careful, as with all non-exempt employees, to obtain a written waiver from an employee voluntarily working through a meal break. More importantly, unlike exempt employees, non-exempt employees working in Rhode Island may often be entitled to be paid at the overtime rate for all hours worked on holidays or Sundays, and work on those days often must be voluntarily.

Track Your Affected Employee's Hours.

The critical step that employers who have employees potentially working more than 40 hours per week and making less than $50,440 in salary should implement is to require the accurate tracking of actual hours worked. As indicated above, everything from coming in 15 minutes early to checking emails for 20 minutes at night counts as work. For this reason, employers are often quite unaware of how many hours their exempt employees *really* work. Without this information it is almost impossible for the affected employer to accurately reset the now non-exempt employee's hourly rate. Moreover, even though the new rule will not go into effect for a number of months, ***tracking should start now*** because often hours may vary over time and over different seasons. In order to maximize the value of any tracking policy, employers should provide a detailed explanation of what activity "counts" as working time and should emphasize the importance of accuracy. Employers can also consider more detailed time tracking requirements (such as requiring time tracking codes or descriptions) so as to get a better understanding of what these salaried employees are doing while they work in case re-distribution of duties is ultimately necessary.

Even with the best explanation to employees, time tracking in the preparation stage may not be entirely accurate given the lack of correlation to the amount of wages. In practice, it is ultimately recommended that if and when it is time to re-set the employee's wage, employers allow some room for error and choose a slightly lower rate. Employers can always pay a bonus if the overall wages are lower than anticipated.

Get the Right Message Out to Employees.

Changing an employee from being exempt – something that is generally thought to be a higher-level, professional type role – to being non-exempt can damage employee morale. Even where employees earn more money, they may feel like they are being demoted and may not like the flexibility. Thus, it is important to communicate at the tracking stage what is happening and why. This explanation should include the fact that: (a) the employees are still exempt (at least until the rule takes effect); (b) the time is being tracked in connection with a potential law change; and (c) the goal is to keep the employee's compensation closest to the *status quo* in the event of such a change. A mantra along the lines of "our goal is to make sure that even though we may be forced to re-classify you, we want to make sure your job and pay is essentially unchanged" may soothe employee anxiety over the change.

Understand what will be Done with the Tracking Data.

The reason for obtaining the tracking data now is clear when thinking about how an employer can respond to the rule change. For example, consider the Unprepared Employer who has a human resources associate currently earning $40,000 per year ($769.23 per week). The Unprepared Employer does not ask the employee to track their time, so the "Unprepared Employer" relies upon the fact that the employee's manager expects her to be present in the office during office hours, which are 8:30am to 5:00pm with a 30 minute lunch break, and the fact that employees all enter weekly time records, although for salaried employees the time generally just says "8 hours" per day absent illness or vacation. Given the foregoing, the Unprepared Employer decides to continue to pay the employee her salary of $769.23 (giving the employee an hourly rate of $19.23) since it assumes a 40 hour week. Consider how tracking the employee's time in advance could have made a difference in the following scenarios:

Scenario 1. The human resources associate brings work with her to lunch, comes in 30 minutes early to get a jumpstart on the workday, spends 30 minutes making work phone calls on her drive home and spends 30 minutes checking work email before bed. Thus, the time tracking reveals the employee consistently works 50 hours per week. The "Prepared Employer" will smartly set the employee's new hourly rate at $13.99 per hour in order to continue paying the employee approximately $769 per week. An easy way to make this calculation is to take the number of overtime hours (in our example, 10 hours), multiply it by the overtime premium (1.5×10=15 hours) add it to the 40 non-overtime hours (40+15=55) and then divide the total hours (55) by the employee's current salary ($769.23/55 = $13.99). Thus, the Prepared Employer will pay the employee $13.99 per hour, or a total of $769.45 per 50 hour week. This is a savings of over $288 per week (***almost $15,000 per year***) from what the Unprepared Employer will pay.

Scenario 2. The human resources associate's husband has a job that requires out of state travel over one half of the time. When her husband is away, she loads up on work, coming in at the crack of dawn and bringing home work on the weekends, so that when her husband is home she can have a light workweek. The time tracking reveals the employee's hours vary per week. If the time tracked shows that a number of weeks involve work *less than* 40 hours, then the standard overtime calculation may still be the method of choice. For example, let us say the time tracked over the course of 15 weeks indicates the employee works 3 weeks each at 30 hours per week, 40 hours per week, 50 hours per week, 60 hours per week and 70 hours per week. The average is 50 hours per week ((30 + 40 + 50 + 60 + 70 = 250) x 3 / 15 weeks). However, unlike Scenario 1 where the correct rate was $13.99 for the employee consistently working 50 hours a week, in Scenario 2 the correct rate to arrive at the same $769 per week salary is $13.73 per hour (lower because employer pays time and one half for hours worked over 40 but saves straight time for hours worked under 40). This calculation is made by multiplying the total number of weeks tracked times the target salary and dividing by the sum of the adjusted hours worked (counting the overtime hours as 1.5 instead of one), as follows: (769.23*15 weeks)/((30+40+55+70+85)*3). Using this method will provide a savings of over $308 per week (***over $16,000 per year***) over what the Unprepared Employer will pay for the same employee.

Scenario 3. The human resources associate is in over her head and must spend hours of time working from home or coming in early to review her work, research how to handle situations and to catch others when they are available to coach her through her job duties. The time tracking reveals the employee consistently works a fluctuating workweek between 50 to 70 hours per week. In this scenario, the employer should consider using the fluctuating workweek method of calculating hours worked. The fluctuating workweek calculation allows employers to set a weekly salary for non-exempt employees whose hours truly fluctuate every week. Employers can calculate an employee's hourly rate for overtime purposes using the actual number of hours worked divided by the weekly set wage, and pay only the extra one half time for the hours worked over 40. So for our example, the Prepared Employer could set the salary at $662.50 per week. When the employee works 50 hours, the rate is calculated to be $13.25 per hour ($662.50/50). Since the employer has already paid the straight time amount, the overtime premium is calculated by dividing the hourly rate in half and multiplying by the number of overtime hours (($13.25/2) x10 =$66.25). Thus, when the employee works 50 hours in a week she is paid $728.75. When the employee works 60 hours, the rate is calculated to be $11.04 ($662.50/60) with an overtime premium of $110.41 ($11.04/2 x 20) and a total of $772.92 for the week. When the employee works 70 hours per week, the rate is calculated to be $9.464 ($662.50/70) with a total weekly payment of $804.46. This provides the employer the equivalent of $768.71 per week ((728.75+772.91+804.46)/3)). As compared to the Unprepared Employer, this provides an average savings of $577.44 per week.

When More Pay or Work Duty Adjustments Make Sense.

While a combination of advance tracking and solid math can provide a great way around the DOL's attempt to get employers to increase wages, there are a few situations that will likely require greater payment to comply with the new rule.

For example, in our last scenario, the employer would either have to increase human resource associate's weekly rate to $672 (in Rhode Island) or $700 (in Massachusetts) or reduce the employee's schedule to ensure that she never worked over 69 hours (in Rhode Island) or 66 hours (in Massachusetts) in order to comply with the 2016 minimum wage standards. For example, in our last scenario, the employer would either have to increase human resource associate's weekly rate to $672 (in Rhode Island) or $700 (in Massachusetts) or reduce the employee's schedule to ensure that she never worked over 69 hours (in Rhode Island) or 66 hours (in Massachusetts) in order to comply with the 2016 minimum wage standards. The first is for the lowest paid exempt employees on the spectrum who work long hours. The minimum wage in Massachusetts and Rhode Island is $9.00 per hour (increasing to $10 and $9.60 per hour, respectively, on January 1, 2016). An employee's hourly rate must never be below this amount, meaning lower-paid salaried employees working a large number of hours will either have to be paid more or required to work less. For example, in our last scenario, the employer would either have to increase human resource associate's weekly rate to $672 (in Rhode Island) or $700 (in Massachusetts) or reduce the employee's schedule to ensure that she never worked over 69 hours (in Rhode Island) or 66 hours (in Massachusetts) in order to comply with the 2016 minimum wage standards.

The second is for the highest paid affected employees who are on the cusp of keeping their exemption. For employees who are being paid close to the new threshold of $50,440 per year, the solution may be to provide more responsibilities to justify a slightly higher salary in order to maintain the exempt classification. This is particularly appealing if you are having certain hourly employees work less to avoid the newly-required overtime.

Keep your Eye on the Big Picture.

In the comments to the proposed rule, the DOL recognizes that employers will be able to make “adjustments” to try and maintain wage levels. One reason the DOL predicts employees will still effectively receive raises is that it will be administratively burdensome and costly to apply different effective hourly rates among employees doing the same job. So in our above example, if the employer has three human resources associates, each of whom fits into a different one of our time tracking scenarios, the best effective rate to avoid any changes to overall compensation will require the employer to pay one worker $662.50 per week with a slight reduction in hours, one $13.99 per hour, and one $13.72 per hour. While this is the “right” answer, it could create logistical problems and employee morale issues given the more an employee worked during the tracking period, the lower their rate would be. In addition, it will be challenging to set the rate of a new human resources associate as there will be no historical information for that new individual’s working hours. Thus, employers who have multiple employees in the same position will be more likely to use the tracking data to determine how many hours the job should take and then set the rate accordingly.

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