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DOL Proposes Significant Salary Level Increase for FLSA's White Collar Exemptions

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Executive Summary

- On August 30, 2023, the United States Department of Labor ("DOL") issued a [notice of proposed rulemaking](#) to increase the minimum salary requirements for the "white-collar" exemptions which apply to executive, administrative, and professional employees to exempt them from minimum wage and overtime pay requirements under the Fair Labor Standards Act ("FLSA").
- Under the DOL's proposed rule, the salary level for the white-collar exemptions would increase from the current \$684 per week (\$35,568 per year) to \$1,059 per week (\$55,068 per year), and the annual compensation level for highly compensated employees would increase from the current \$107,432 per year to \$143,988 per year.
- The proposed rule was published in the Federal Register on September 8, 2023, and is subject to a 60-day comment period that expires on November 7, 2023.

CURRENT LAW

Under existing law, executive, administrative and professional ("EAP") employees can be exempt from the FLSA's overtime requirements if they qualify for at least one of the white-collar exemptions. For decades, the DOL has used a three-part test for these exemptions: An employee must (1) perform exempt duties, (2) be paid a fixed salary and (3) be paid a high enough salary.

Currently, to qualify for one of these white-collar exemptions, EAP employees generally must:

- primarily perform executive, administrative, or professional duties as provided in the DOL's regulations (the duties test);
- be paid on a salary basis, meaning that the employee is 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); and
- be paid more than a specified salary threshold, currently \$684 per week or \$35,568 annually (the salary level test).

Additionally, under the highly compensated employee (“HCE”) test, certain employees are currently exempt from the FLSA’s overtime pay requirements if they: (1) are paid total annual compensation of at least \$107,432; (2) receive at least \$684 per week paid on a salary or fee basis; (3) perform office or nonmanual work; and (4) customarily and regularly perform at least one of the exempt duties or responsibilities of an executive, administrative, or professional employee.

THE PROPOSED RULE

Under the DOL’s proposed rule, the salary level for the white-collar exemptions would increase from the current \$684 per week (\$35,568 per year) to \$1,059 per week (\$55,068 per year). That would be about a 55% increase over the current salary level that has been in effect since January 1, 2020. However, the DOL clarified that when it announces the final rule, it will use the most recent earnings data available at that time. This could result in a salary level even higher than \$55,068. For example, the DOL projects that by the fourth quarter of 2023, the salary threshold could be as high as \$1,140 per week (\$59,285 annualized), and that by the first quarter of 2024, the salary threshold could be as high as \$1,158 per week (\$60,209 annualized). The DOL also proposes automatic increases to these salary thresholds every three years to reflect current earnings data (but it would be able to temporarily delay a scheduled automatic update if warranted by unforeseen economic or other conditions).

Additionally, under the DOL’s proposed rule, the annual compensation level for highly compensated employees would increase by 34% from the current level of \$107,432 per year to \$143,988 per year. Under the proposed rule, the amount needed to qualify for the HCE test would be based on the annualized weekly earnings of the 85th percentile of full-time salaried workers nationally. Based on 2022 data, the DOL reports that the HCE test would require total annual compensation of \$143,988. Again, however, the DOL indicates that it will use the most recent earnings data available at the time the final rule is promulgated, which may lead to a higher annual threshold. Also, like the salary level for the white-collar exemptions, the salary level for the HCE exemption is also subject to automatic increases every three years based on applicable earnings data.

IMPACT AND CONCERN FOR EMPLOYERS

If the proposed salary levels are carried over into a final rule, the DOL estimates that 3.6 million workers would see salary increases or changes in their FLSA classification, and that there would be an income transfer of \$1.2 billion from employers to employees in the first year alone. Accordingly, the increase in the compensation required to meet the proposed salary level test will have a material economic impact on many employers nationwide that currently have exempt workers who earn more than \$684 per week, but less than \$1,059 per week, yet satisfy the requirements of the duties test. If a final rule is implemented in a form that mirrors the proposed rule, employers will need to implement new overtime premiums or salary increases for an increased number of employees who are currently not eligible for overtime but will be once the final rule goes into effect, in order to preserve their exempt status.

Additionally, employers may find that the DOL’s proposed rule results in higher market compensation benchmarks for the affected employees, and that increasing compensation levels becomes necessary to stay competitive in recruiting and retaining employees. To this end, some employers may need to increase budgets to account for salary increases or overtime payments to the impacted employees. Moreover, the DOL’s

proposed rule could also result in employers increasing job duties to account for higher wages being paid, or simply reclassifying currently exempt employees to be non-exempt.

RECOMMENDATIONS FOR EMPLOYERS

Employers are encouraged to reassess their employee classifications to ensure that employees are properly classified, both in terms of salary threshold and job duties.

Employers may also wish to start tracking the average hours worked by their exempt employees earning less than \$55,068, to assess the impact of this proposed rule. If those employees rarely work more than 40 hours a week, the practical effect of converting the employee to non-exempt may be limited. Conversely, if those employees routinely work more than 40 hours per week, employers may wish to consider cost-cutting strategies, such as reallocating workloads, bringing in part-time or contract workers, or reducing less critical work assignments. Employers not prepared to raise wages sufficient to meet the proposed salary thresholds should review the impacted employees' average hours per workweek to estimate future overtime costs or consider whether their work can be redistributed in a manner to reduce or eliminate the need for overtime hours. It is important to note that to calculate overtime for non-exempt employees, employers must factor nondiscretionary bonuses, commissions and other such types of compensation into the employee's regular rate. Also important for employers to keep in mind is the impact on employee morale when classifying previously exempt employees to non-exempt status, including but not limited to the loss of schedule flexibility and newly imposed timekeeping obligations.

Interested employers and business groups have an opportunity to submit comments to the DOL on the proposed rule. The proposed rule was published in the Federal Register on September 8, 2023. The 60-day comment period closes on November 7, 2023. While employers are recommended to wait until the final rule is actually published before implementing any changes, it is believed that the final rule is likely to become effective 60 days after its publication. Therefore, it would be prudent for employers to conduct a preliminary review and assessment of potentially impacted employee classifications in the near future.

If you have any questions about the DOL's proposed rule or its impact on your company's employee classifications, please contact Naureen Amjad, Kevin S. Borozan or any other member of Masuda Funai's Employment, Labor and Benefits Group.