

# CLOCK WATCHING

BY PHILLIP M. PERRY

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**a look at the new overtime rules and how to avoid costly penalties for wage-and-hour violations**

Who gets paid overtime? If you're like most employers, that question has caused more than a few sleepless nights. After all, lots of money rides on the answer. Load up the hourly gravy train and you end up with a bloated payroll that erodes your profits. Exempt the wrong people, though, and you face a worse risk—costly litigation for back pay from employees claiming misclassification. ✦ No wonder employers often feel caught between red ink and a lawsuit. Is there a solution? Maybe. New overtime regulations from the U.S. Department of Labor provide some clarity to what has long been a woolly patchwork of regulations. ✦ The new rules, which took effect August 23, seem to be a mixed blessing for employers. On one hand it looks as though more lower-income workers will be eligible for overtime. That means you may well be paying out more in wages under the revised regulations. On the other hand, the extra expense may be more than offset by a decline in legal expenses. Because the new regulations are somewhat clearer about what types of employees must be granted overtime, the number of “wage-and-hour lawsuits” is expected to decrease.



### three key changes

The complete regulations are long and complex (see sidebar for more information). You should become aware, though, of the following three provisions. The first two are expected to substantially add to the rolls of employees eligible for overtime; the third is expected to slightly moderate that number.

1) The new rules mandate overtime for all workers earning less than \$455 per week, which translates to \$23,660 annually. This three-fold increase from the former threshold of \$155 is expected to increase the number of non-exempt workers by some 6.7 million.

2) Workers earning more than \$455 weekly and less than \$100,000 annually are subject to protections from loss of overtime pay, under standard “duties tests” that are equal to—or more protective than—former tests. This provision, then, should also increase the number of non-exempt workers.

3) Employees who earn more than \$100,000 in annual pay are subject to a new set of “duties tests,” which are less protective than the ones for the middle tier of workers. This provision is expected to result in some 107,000 highly compensated employees losing overtime protection.

### avoid costly penalties

You must take action quickly to make sure you comply with the new regulations. “Most employers are looking at jobs now and auditing their positions,” says Joseph P. Harkins, a partner at Washington, D.C.-based Littler Mendelson, the nation’s largest employment law firm. “It’s important to do this and make adjustments where required.”

Delay too long and you can get hit with costly financial penalties from two sides. First, employees may sue you for misclassifying them as exempt from overtime, leading to back wage settlements. Second, you may be hit with government fines.

“If you do not comply with the new rules, you could be penalized for any overtime that the Department of Labor believes you should have paid to

employees,” says Timothy S. Bland, a partner in the Memphis office of Ford & Harrison. Ford & Harrison is a law firm that defends businesses on employment-related matters. “You can also be assessed liquidated damages—fines totaling double the back pay you are deemed to owe misclassified employees.”

In either case, it’s clear that the longer you wait the greater the potential financial damages. Be aware that your investigation may uncover instances of what attorneys call “task creep.” This refers to the gradual modification in the duties performed by an employee, so that a formerly exempt individual becomes non-exempt or vice versa. Task creep can occur unnoticed and can lead to serious misclassifications.

### your payroll may increase

So how will this affect your payroll costs? If you are like most employers, it will mean more money spent for wages. Your own experience, though, will depend on your location and current wage structure.

“This law will impact employers very differently depending on where they live,” says Robert D. Lipman, managing partner at the employment law firm Lipman & Plesur in Jericho, N.Y. “The biggest impact may be felt in rural areas where employees may earn less than \$455, but still have a fair amount of responsibility.” Smaller employers in general may be more affected since they may have a greater percentage of employees who might not meet the minimum salary test under new rules.

The effect may be mollified in some cases by a reduction of overtime eligibility by individuals who earn a salary higher than the legislation’s “highly compensated” upper threshold. If an employee makes \$100,000 a year and the person’s “primary duty includes performing office or non-manual work,” the employer only has to justify exemption by showing that the employee “customarily and regularly performs any one or more of the exempt duties” as specified in the regulations. “This will impact those employers who have hourly jobs near the upper threshold,” says Harkins.

### the muddled middle

You are most likely to come to grief trying to classify people with earnings that are more than \$455 weekly but below the amount needed to be highly compensated.

“Most employees fall in between the lower and upper thresholds,” says Harkins. “Employers are struggling to figure out where these individuals fit.”

Unfortunately, the new guidelines are not much help. “While the law is slightly different in wording, it is basically similar to the old one,” says Harkins. “You must still deal in vague terms such as ‘independent judgment’ and ‘discretion,’ and ‘responsibility to hire and fire.’”

You and your attorney will need to reference the complete law that defines terms, describes details and provides real world examples. Here, though, are some key points that will assist you when talking with your attorney:

The Department of Labor has stated that you may classify as exempt from overtime certain employees whose workplace activities “primarily involve executive, administrative or professional duties.” Most readers of this magazine will be concerned with the first two categories. In addition to the salary tests described earlier in this article, exempt individuals in these categories must meet the following “duties tests”:

1) For an executive employee: The “primary duty” of this individual must be the “management of the enterprise.” Additionally, this person must be one who “customarily and regularly directs the work of two or more other employees.” Finally, this individual must either have the authority to hire and fire other employees or offer suggestions and recommendations for such personnel actions that carry “particular weight.”

Retailers have typically relied on the executive exemption for their managerial personnel. So are the new rules favorable or not? “A lot depends on the size of your store,” says Harkins. “An exempt individual is required to supervise two full-time equivalents. That’s great for a branch of a big store. But a small shop might not meet the test.”

2) For administrative employees: This person’s “primary duty” must be

“the performance of office or non-manual work directly relate to the management or general business operations of the employer or the employer’s customers.” Additionally, the primary duties must include the “exercise of discretion and independent judgment with respect to matters of significance.”

Retailers typically rely on the administrative exemption for personnel who are not managers, but who are critical to store operations. Unfortunately, the language of the new regulations adds little or no clarity in this area.

“We had hoped that the administrative exemption would be cleared up and made easier to apply,” says Bland. “That’s not the case. This is unfortunate for retailers.”

Just how much “discretion and independent judgment” has to exist to meet the duties test is extremely difficult to apply in the real world. “Some employees have very little discretion in the job and are obviously not exempt,” says Bland. “A few have so much discretion they clearly are exempt. But most employees, by far, fall into a grey area, so it comes down to a judgment call.”

Be aware that the above paragraphs provide a sketch of the complete picture, the shading and color of which must be filled in by you and your attorney. They do, however, provide a basis for discussion.

### define your terms

The new regulations attempt to define the key terms used in analyzing personnel exemptions. For example, the rules provide a long list of activities that constitute the practice of “management” and what factors constitute “particular weight” for determining the

exemption of executive employees.

For administrative exemptions, the regulations attempt to define phrases such as “discretion and independent judgment” and “directly related to management.”

Reiterating such definitions is beyond the scope of this article and must be done in conjunction with your attorney to analyze the particular status of your personnel. One term, though, is particularly important because it pops up in all of the duties analyses. That is “primary duty.”

The term primary duty has been expanded from the time spent on exempt work to the perceived value of exempt work. An employer might claim that many non-exempt tasks performed by an employee are in support of exempt tasks. By way of example, an administrative assistant might be doing a lot of clerical tasks but they are all in support of getting vendor agreements in order. This person might well be classified as exempt.

The new regulations have discarded the old rule that an exempt individual could not spend more than 20 percent of time on nonexempt work. Indeed, it is not even necessary that an individual spend more than 50 percent of work time on a duty for that activity to be deemed “primary.” Rather, the determination must be made on a case-by-case basis, taking into account such matters as “the relative importance of the exempt duties” and “the employee’s relative freedom from direct supervision” and wage disparities between the individual and nonexempt employees.

By way of illustration, the regulations posit an assistant store manager who spends more than 50 percent of time “performing nonexempt work such as

running the cash register.” Such an individual may still be exempt if he or she performs managerial work such as supervising other employees and ordering merchandise. The exemption becomes questionable, though, if the individual is “closely supervised” and earns “little more than nonexempt employees.”

The regulations also note that an assistant store manager may perform concurrent nonexempt duties without losing exempt status. For example, an exempt employee can “simultaneously direct the work of others and stock shelves.”

### better safe than sorry

Given the number of people in the muddled middle and the vagueness of the applicable duties tests, it’s clear you will need to engage in serious analysis to avoid non-compliance penalties.

When faced with ambiguity, many employers are taking the “better safe than sorry” option. “I do not see a lot of clients going out of their way to make hourly people salaried,” says Harkins. “But I do see employers taking salaried people and putting them into the hourly category. So I would not be surprised if the new legislation increases the number of people eligible for overtime to a level even higher than what the DOL has predicted.”

Now is the time to take a new look at your own employees and classify them appropriately. When in doubt, remember that the law presumes your employees are hourly—it’s up to you to show otherwise. Says Harkins: “It’s always legally safer to pay wages and overtime.” ■

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## GET MORE INFORMATION

- ▶ For a complete copy of the new regulations, go to the special Fairpay section of the U.S. Department of Labor’s Web site: [www.dol.gov/fairpay](http://www.dol.gov/fairpay). Click on “regulations” then the hyperlink for either Web-view or PDF versions of the law. This site also offers online video seminars and fact sheets.
- ▶ Littler Mendelson, the nation’s largest employment law firm, has posted a document to help employers understand the new legislation. Visit [www.littler.com](http://www.littler.com), then click on “DOL Revised White Collar Regulations.”