

# Will Your Exempt Employee Still Be Exempt?

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In March of 2014, President Obama asked the Department of Labor to update the overtime regulations under the Fair Labor Standards Act (FLSA). On May 17, 2016, the Department of Labor released its Final Rule ("Final Rule") which only provides changes for the minimum salary requirements for exempt (white collar) employees. The Final Rule revises the federal regulations related to the FLSA. The last time overtime regulations were revised for white collar workers was in 2004. Normally, federal laws and regulations do not impact California employees because California's laws are generally more stringent than federal laws and regulations, however, this new rule will impact California exempt employees.

## New Federal Salary Minimum for Exempt Employees

Under both California and federal law, in order to classify an employee as exempt from overtime and other wage and hour requirements, the employee must meet both a salary and duties test. The Final Rule provides that exempt employees must earn a minimum salary of \$46,467 in order to be exempt. The new federal salary requirement is effective **beginning December 1, 2016**. In California, the salary minimum for an exempt employee is two times the minimum wage which is currently \$41,600 (2 x \$10 x 2080 hours). As of **December 1, 2016**, California exempt employees will also need to be paid a minimum of \$46,467.

Under both California and federal law, employees must also meet the duties test (executive, administrative, professional) to be exempt. The duties test for an exempt employee has always been more stringent under federal law which requires that exempt employees spend more than 80% of their time on exempt duties as compared to California which only requires that exempt employees spend more than 50% of their time on exempt duties. The Final Rule does not affect the duties test for exempt employees.

Many California employers took a business risk that their determination of which employees were exempt would never be reviewed by the Department of Labor. Now that the federal salary minimum will be higher, California employers may see more Department of Labor complaints which may result in a review of whether not exempt employees are actually exempt under federal law. This article does not discuss the specific duties test for each exemption, but they are similar under federal and state law and can be found in the California wage orders or in the federal regulations.

Under the Final Rule, exempt salaries will be automatically updated every three years based upon wage growth over time. The Department of Labor anticipates that the minimum salary will rise to \$51,168 in 2020 and will post new salary levels six months prior to their effective date with the first posting on August 1, 2019.

## Non-Discretionary Pay and Catch Up Provisions

The Final Rule also allows employers to pay up to 10% of the increased salary in non-discretionary bonuses, commissions or other incentive payments. The key word is "non-discretionary." Employers may pay any shortfall in the salary minimum if the employee does not earn the required amount in non-discretionary income at the end of any quarter. Any shortfall must be paid by the employer in the first pay period following the quarter (the prior 13 weeks) and can only be used to catch up the amount paid to the employee in the prior quarter.

California law does not have a catch up provision and as the California or local minimum wage rises, the minimum salary for California exempt employees may be less than 10% of the newly established federal minimum of \$46,467. For example, in Los Angeles County the minimum wage will be \$10.50 as of **July 1, 2016** which means that an exempt employee will need to earn \$43,680 as of that date under California law in addition to meeting the duties test for the exemption. Therefore,



employers in Los Angeles County would have to either pay a minimum salary of \$46,467 or pay non-discretionary bonuses, commissions, etc. in the amount of \$2,787 to meet the federal minimum salary requirements.

Employers also need to be mindful of city ordinances regulating the pay of employees in specific cities. Los Angeles, Santa Monica, San Francisco and San Jose have already established separate minimum wages for their cities and this trend will continue. Thus an increased burden is placed on employers to keep track of what local governments are doing in cities where employers maintain their businesses or where employees perform work in those cities.

### **Highly Compensated Employees**

Under federal law, a highly compensated employee is exempt if they earn a minimum salary, have primarily office or non-manual duties and “customarily and regularly” perform at least one of the duties of the applicable exemption. The Final Rule raises the minimum salary for highly compensated employees from \$100,000 to \$134,004. California does not have a similar provision so any exempt employee would need to meet all requirements of the duties test to be exempt.

### **Steps California Employers Should Take**

All employers should make sure that their exempt employees are paid the highest applicable minimum salary (federal, California or local) as of December 1, 2016. If employees classified as exempt do not meet the salary test, employers can do one of the following:

1. Increase the salary of the employee to maintain their exempt status (assuming they also meet the duties test); or
2. Reclassify the exempt employee as non-exempt and have that employee record their hours worked, including their meal breaks each day. In this case, you need to pay the employee overtime for all hours worked over 8 in a day or 40 in a week. The overtime requirements are also contained in the California Wage orders. (The Wage Orders can be found on the California Division of Labor Standards Enforcement website – [dlse.ca.gov](http://dlse.ca.gov).)

*If you need assistance in determining whether or not an employee is exempt or whether they are being paid appropriately, please contact Deborah Petito or Leonard Brazil in the Clark & Trevithick Labor and Employment Department.*