A **Decision Making Guide** for the **Federal Labor Standards Act (FLSA)**

New Exempt Employee Minimum Salary Rule, effective July 1, 2024

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PART ONE

FLSA Changes

DECISION MAKING GUIDE

This guide is the first of a two-part series to assist employers in complying with the new minimum salary threshold that applies to many exempt employees.

What do you mean by "New Rule"?

The Fair Labor Standards Act (FLSA) requires that employees earn a minimum wage as well as overtime pay for hours worked over 40 in a week, but it also provides exemptions for employees that meet certain criteria. The U.S. Department of Labor (DOL) has the power to make rules that relate to these exemption categories, including what duties will qualify an employee for an exemption, how they are paid, and how much they are paid.

Executive, Administrative, and Professional Employees
Under the new rule, exempt executive, administrative, and professional employees (often referred to collectively as EAP employees) must be paid at least:

- $844 per week ($43,888 per year) beginning July 1, 2024
- $1,128 per week ($58,656 per year) beginning January 1, 2025

Teachers and practicing doctors and lawyers are exempt from these minimum salary requirements under federal law but may be subject to different state minimums. School-specific minimums apply to academic administrative employees.

Computer Employees
Exempt computer employees can be paid on a salary or hourly basis. If salaried, they're considered part of the EAP group and need to make the minimums listed above. Alternatively, they can be paid at least $27.63 per hour—this hourly rate was not changed by the rule.

Highly Compensated Employees (HCE)
Employees who are exempt under the HCE exemption must be paid at least the minimums listed above on a salary basis and receive total annual compensation of at least:

- $132,964 beginning July 1, 2024
- $151,164 beginning January 1, 2025

What should we do first?

We recommend that employers decide on a course of action and start planning for how those changes will be implemented. In this guide, we focus on the three main steps employers need to take when deciding their course of action:

1. Identify which exempt employees could be affected
2. Calculate the hours worked by affected exempt employees
3. Evaluate the options and make a decision about how, and how much, the employee will be paid

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STEP 1

IDENTIFY AFFECTED EXEMPT EMPLOYEES

Identify your exempt employees who are paid at or below the new minimums. As a best practice, consider identifying exempt employees at or below $65,000, so wage compression can be part of your big picture evaluation.

What is Wage Compression? When the salary floor for a position is increased but the ceiling is not, wage compression occurs for a particular position or tier of positions. For example: Joe is new to the company and making $56,000; Ed has the same title as Joe but has been in the position for three years and is making $59,000. The company elects to increase new-guy-Joe's salary to the new minimum so he can remain exempt, making Joe and Ed's salaries nearly equal. This is wage compression and should be avoided whenever possible, so your more experienced or higher ranking employees feel they are being treated fairly.

STEP 2

CALCULATE TOTAL HOURS WORKED by EACH EMPLOYEE from STEP 1

To properly assess compensation in the upcoming steps, it's necessary to first determine an accurate number of hours worked for each employee identified in Step 1.

Why go to the trouble? Failure to properly estimate an employee's hours worked may lead to shocking results when you reclassify them as hourly. For instance, calculating an employee's new hourly rate based on the assumption that they're working 40 hours per week could lead to a huge amount of unexpected overtime liability if the employee has actually been working more than 40 hours per week on a regular basis.

However, asking exempt employees to begin tracking hours worked without providing detailed reasoning may cause confusion. You'll want to clearly communicate with employees that this is for tracking and preparation purposes only and will have no effect on their current salary. The sole purpose is to prepare for compliance with the new laws—not micromanagement.

To get the information you need, you'll have to track your exempt employees' hours. How to go about this is up to you, but here are a few options to measure current hours worked:

→ Ask the employees to begin tracking their hours worked. This is our preferred method, as it will likely result in the most accurate timekeeping records. You can ask employees to use the same timekeeping system as nonexempt employees, have them track their time on the computer, on a paper timecard, or even on a phone app—it's up to you.

→ Ask managers to begin tracking hours worked for their exempt employees.

→ Ask managers to estimate the number of hours worked for each exempt employee.

→ Use the expected work week for the position in question to determine the number of hours worked (typically by referencing the job description or the job offer).

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STEP 3

EVALUATE the OPTIONS and DECIDE on APPROPRIATE COMPENSATION

Identify each employee's current base salary and total incentive pay (bonuses, commissions, any other incentive pay). Add these amounts to get their total annual earnings.

Compare this amount to the following pay options:

→ **Increasing the employee's pay to $58,656 (by January 1, 2025).**

→ **Reclassifying the employee as hourly nonexempt and paying them at a rate determined by their current salary divided by 2,080.** This simple equation works best if the employee currently works around 40 hours per week on average (2,080 hours per year).

- o Calculation for hourly for rate of pay: total annual earnings ÷ 2,080 hours
- o Example: 41,600 ÷ 2,080 = $20 per hour

→ **Reclassifying the employee as hourly nonexempt and calculating a cost-neutral rate of pay.** This rate of pay accounts for overtime the employee is doing currently and provides an hourly rate of pay that will result in the employee making approximately the same amount annually when paid by the hour as they did when they were on salary. This equation works best for employees who regularly work overtime. However, if they work a lot of overtime in a state with a higher than federal minimum wage, their rate could end up at or below minimum wage.

- o Calculation for cost-neutral hourly rate of pay: annual earnings ÷ (2,080 + [annual overtime hours x 1.5])
- o Example: $41,600 ÷ (2,080 + [260 x 1.5]) = $16.84 per hour

→ **Reclassifying the employee as salaried nonexempt and paying them the same each week they work 40 hours or fewer, and overtime when they work more than 40 hours.** With this classification, you may continue to pay an employee on a salary basis—meaning a fixed base amount each week—but you'll still have to pay them time and a half for hours over 40 each week. You'll need to continue to carefully track their hours to ensure they always receive overtime pay if due. If using this classification, you should use their base weekly or yearly salary to determine their overtime rate.

- o Calculation for overtime rate of pay: total annual earnings ÷ 2,080 hours x 1.5
- o Example: $41,600 ÷ 2,080 x 1.5 = $30 per hour, for hours over 40 in a workweek

Salaried nonexempt is a somewhat risky classification, so we recommend caution here. This pay classification requires strict timekeeping, just as for all nonexempt employees, in order to determine overtime eligibility. This includes keeping track of when these employees begin and end work each day, as well as compliance with any state-mandated meal period requirements.

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CONSIDER the BIG PICTURE

Wage compression was mentioned above, but you should also consider the effects of giving certain employees raises while others stay at the same rate of pay—even if they are in different job types. For instance, if several male employees received raises to bring their salary up to the new threshold, but a female employee who was already above the threshold did not receive a raise (or even received a pay cut to help balance the books), it could cause considerable trouble, even if only from a morale perspective.

Whenever possible, attempt to classify all employees in a particular job group or position the same way. If this can't be done, document your business reasons for the different classifications.

Also consider whether incentive pay will continue to be provided to employees who will not be classified as nonexempt. Providing incentive pay to nonexempt employees can complicate overtime calculations, since those incentive payments must be included in an employee's base pay when determining their overtime rate. Essentially, incentive payments will increase an employee's base pay rate and thus increase their overtime rate for that week as well. Although incentive payments can continue to be a great motivator, a little more math is required when they are provided to nonexempt employees who work overtime.

* ***Incentive what?*** Incentive pay includes non-discretionary bonuses, commissions, and any other non-hourly pay.

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PART TWO

FLSA Changes

IMPLEMENTATION GUIDE

This guide will assist you in making changes in order to comply with the new exempt employee minimum salary rule, effective July 1, 2024.

What should we be doing now?

Here we focus on implementation of changes your organization may need to make in the wake of the final rule. These are the steps in that process we'll be looking at:

1. Considering the company's policies and practices

2. Communicating the changes internally

3. Conducting training to ensure understanding and compliance

4. Monitoring and revising company budgets and processes

This guide also features the following resources:

→ **Sample FLSA reclassification letter to employees**

→ **FAQs**

STEP 1

CONSIDER THE COMPANY'S POLICIES & PRACTICES

With the possible reclassification of a number of your organization's employees, we recommend reviewing your current policies and procedures. This is especially important for organizations that don't currently have many nonexempt employees and may not be as focused on policies that deal with timekeeping and work hours. If these policies and practices aren't currently covered in your employee handbook, we recommend adding them now, or distributing them separately as handbook amendments. Once distributed, employees should sign off to acknowledge their acceptance and understanding of these important policies. If your policies and practices are already covered in your handbook, now is a good time to re-emphasize them with the newly classified employees.

Changing habits can be a challenge, but changing the habits of your formerly exempt employees regarding timekeeping is critical to prevent a wage and hour violation. These employees are likely used to "running the clock" after hours—many of them may be used to responding to work emails, finishing up projects, taking client calls, or engaging in other work tasks during non-work hours. While intentionally working off the clock may not be your employees' goal, we want to be sure that the policies are clear about expectations with respect to off-the-clock work and the organization's commitment to recording all time worked by nonexempt employees.

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THE GOLDEN RULE

While reviewing the recommended policies, keep in mind the golden rule of wage and hour: nonexempt employees must be paid for all the time they are "suffered or permitted" to work. This doesn't mean time in the office, but all time, whether approved by the employer or not.

→ TIMEKEEPING POLICIES AND PRACTICES

Consider that your previously exempt employees may not be familiar with your timekeeping procedures, e.g., how to track time worked, limits on clocking in before their scheduled start time, how to properly track evening work to check emails, or how and when to turn in their time for each pay period.

→ OFF-THE-CLOCK WORK POLICY

All hours worked by a nonexempt employee must be recorded and compensated, even those performed outside of the employee's standard shift. Therefore, it's critical to have a policy in place that informs employees that all time worked must be tracked, and that off-the-clock work is prohibited by the company. In other words, employees must follow their written work schedule and may be disciplined for not doing so.

Note: *Refusing to pay for unauthorized time worked—whether it's regular or overtime—isn't legal.*

→ BRING YOUR OWN DEVICE POLICIES

If a nonexempt employee checks their work email on their personal device (e.g. smartphone, tablet, or home computer), time spent working on this device is considered time worked and should be tracked and paid accordingly. Many employers don't allow a nonexempt employee to use their personal devices for work purposes for this very reason, or only allow such use upon authorization from the company.

Additionally, a good bring-your-own-device policy will require that employees accessing company information from their device have security measures in place to protect the company's confidential information.

→ MEAL AND REST PERIOD POLICIES

Many states require meal and/or break periods for nonexempt employees, depending on the length of their shift, and many companies choose to provide meal and break periods voluntarily. It's important to inform employees of these breaks and your clock in/out procedures, and to notify them that no work should be performed during such breaks. Again, if work is performed, it must be compensated, so the policy should include instructions for notifying a manager or supervisor if a working meal period occurs.

→ OVERTIME POLICIES AND PRACTICES

Now is the time to ensure you're familiar with your state and local overtime laws. Although most employers will only be subject to the federal requirement to pay time and a half for hours worked over 40 in one workweek, some states have daily overtime provisions or require a premium for work on Sundays and certain holidays. It's important that employees and managers are aware of the rules for compliance.

Additionally, if the company requires pre-authorization of overtime, it's best to share these expectations in an overtime policy.

→ TRAVEL TIME POLICIES AND PRACTICES

Since nonexempt employees must be paid for all time worked, travel time for those customarily engaged in work travel may require further consideration. There are a few narrow exceptions when travel time isn't payable (e.g., when the employee is a passenger in a vehicle or during a standard morning or evening commute), but it's good to assess an employee's travel schedule to ensure proper pay.

→ PAYROLL CHANGES

Incentive Pay: Payroll changes are especially relevant as they relate to issuing incentive pay (nondiscretionary bonuses, commissions, or any other non-hourly pay) to nonexempt employees. Per Fair Labor Standards Act (FLSA) requirements, overtime must be calculated weekly based on the employee's "regular rate of pay." However, incentive pay must be included in the employee's "regular rate of pay" calculation.

For weeks in which a nonexempt employee earns both overtime and incentive pay—whether provided at the time or retroactively—the company must calculate (or recalculate) the employee's regular rate of pay so that it includes both their base pay and incentive pay for the week, then utilize the new amount for overtime calculations. See the FAQs at the end of this guide for an example calculation.

Workweek: It's important that the individuals responsible for payroll, along with managers and employees, are well aware of the company's seven-day workweek. Every company must have an established workweek that is not adjusted or altered to avoid overtime. Each workweek is assessed individually for overtime calculations, and overtime must be paid for each workweek in which it is earned.

NOTE

Arrangements where an employee receives amounts of time off (also known as compensatory or "comp time") in place of overtime wages are not permitted for nonexempt employees of private employers. ***Nonexempt employees are due all applicable overtime pay for applicable overtime hours worked in the workweek.***

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STEP 2

COMMUNICATE THE CHANGES

Applicable changes must be communicated clearly to the whole company. Things to consider:

→ WHO WILL COMMUNICATE THESE CHANGES?

Think about the size and structure of your organization and who is most capable of getting the message to all employees in an efficient and positive manner. Consider managers, the executive team, and your human resources professional.

→ WHO DO WE NEED TO COMMUNICATE WITH?

Decide if you will only discuss changes with newly nonexempt employees or if a company-wide notification makes the most sense. The latter may be preferable if the changes will impact many employees whose status is not changing. For instance, if numerous work schedules will need to be rearranged, if employees who used to answer multiple internal questions on weekends will no longer be able to, or if the lunchroom is going to be much more crowded, you may want to extend your notification to all (or most) employees.

→ WHAT WILL BE COMMUNICATED?

A sample Employee Reclassification Letter—Exempt to Nonexempt is provided at the end of this guide, and can be customized to meet your specific needs. Remember, clear and open communication can prevent many potential issues, including those related to morale. Having a template that you use for all affected employees ensures consistent communication and creates documentation.

→ HOW WILL CHANGES BE COMMUNICATED?

This communication may be in the form of an email, video conference, live meeting, or one-on-one meeting. We recommend several communications over time, beginning with a high-level overview. Reminders even after the change in classification will be necessary to make certain that new policies and practices are understood and followed.

Some states have requirements for advance notice of any changes to pay. Others require issuing written notice of the change.

For employers in states that don't have specific notice requirements, we recommend providing employees with advance notice of at least one pay period for any change to pay, but for a change in classification, two or more pay periods advance notice is best.

→ WHAT SHOULD BE DOCUMENTED?

Assuming your state does not have specific documentation requirements, we recommend clearly documenting these changes for the employee's personnel file. All details for the classification change should be documented, including their new FLSA classification as nonexempt, type of pay received (e.g., hourly, salary, piece rate), and the effective date of the change. This document should be signed by the employee and a representative of the company and then stored in the employee's personnel file. If the company makes changes to nonexempt employment policies as discussed above, updated policies should be distributed and acknowledged by each employee, and the acknowledgment form should be maintained in their personnel file.

STEP 3

CONDUCT TRAINING

Set aside time to train your supervisors and managers to ensure new and updated company policies and practices are accurately communicated, understood, followed, and enforced. Additionally, managers and supervisors must understand the company's overtime practices and the budget implications of reclassifying employees.

For example, if overtime should be avoided entirely, managers may need to adjust their scheduling to accommodate for this. Managers also may need to examine their staffing models to ensure adequate staffing for service or product output.

Employees must be trained so that they are aware of each policy and how it affects them and their work each day. Employees must also understand that once they are trained and acknowledge the policies, failure to comply will result in discipline.

Both managers and employees must be aware of what constitutes compensable time, as this is likely a sizeable adjustment. For example, travel time and time spent checking emails at night must be compensated. Employees will need to know how to report this time, and managers will need to know how to schedule accordingly.

When training employees on the relevant policies and practices, it may be worth a few minutes of your time to discuss that the driving force behind these changes is the FLSA, not your opinion of the reclassified employees. For better or worse, being exempt (or salaried) has been a status symbol in the American workplace. Given the potential for bruised egos, it's important to communicate that this change isn't a result of the employee's performance, dedication to the company, or contribution—it's simply a result of changes to federal law that the company must comply with.

NOTE

Time, energy, and money dedicated to training will be well spent. Proactive training on compliance—prior to the rule's effective date and in the following six months to a year—will cost a small fraction of the price of defending wage and hour claims.

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STEP 4

MONITOR AND REVISE COMPANY BUDGETS

Once you've decided how to deal with affected employees, you should be able to analyze company budgets to determine the impact. Depending on the scale of the changes your organization needs to make, continuous monitoring of budgets may be necessary for the first six months to a year after you implement changes.

FAQs

→ WHAT ARE THE NEW MINIMUM LEVELS?

As of July 1, 2024, exempt executive, administrative, computer, and (most) professional employees need to be paid at least $844 per week or $43,888 per year. This minimum will increase on January 1, 2025, to $1,128 per week or $58,656 per year.

Employees who are exempt under the highly compensated employee (HCE) exemption must be paid at least the minimums listed above on a salary basis and receive total annual compensation of at least $132,964 as of July 1, 2024, and at least $151,164 as of January 1, 2025.The HCE exemption may be used when an employee performs just one or more duties of an executive, administrative, or professional employee. They do not, however, have to meet all elements of any given duties test.

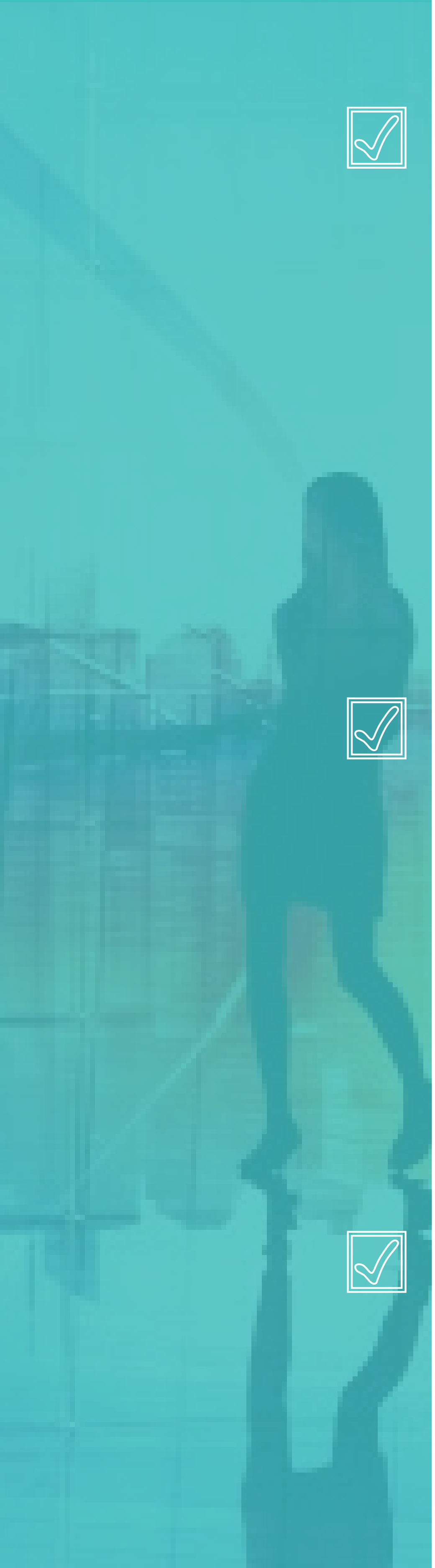
→ WHEN SHOULD I CHANGE AN EMPLOYEE'S STATUS TO NON-EXEMPT?

We recommend notifying employees of their classification change at least 30 days before their pay is impacted, and we recommend an effective date for the change no later than the start of the pay period that includes the effective date of the new minimum (either July 1, 2024, or January 1, 2025). This will prevent a mid-pay period classification change. Issuing pay to an employee for one pay period that includes classification as both exempt and nonexempt is complicated, and your payroll specialist will thank you for using a pay period start date for ease of transition.

→ IS ISSUING COMMISSIONS, NON-DISCRETIONARY BONUSES, OR OTHER PAY TO NON-EXEMPT EMPLOYEES DIFFERENT?

Yes, and it's definitely more complicated than it is for exempt employees.

The FLSA requires that overtime is calculated weekly based on the employee's "regular rate of pay." However, although they may not seem "regular," commissions, nondiscretionary bonuses and other non-hourly pay must be included in the "regular rate of pay" calculation. For weeks in which a nonexempt employee earns both overtime and incentive pay—whether provided at the time or retroactively—the company must calculate (or recalculate) the employee's regular rate of pay so that it includes both their base pay and incentive pay for the week, then use the new amount for overtime calculations.



→ WHAT'S THE DIFFERENCE BETWEEN A NON-DISCRETIONARY AND DISCRETIONARY BONUS?

Essentially, nondiscretionary bonuses are goal based and guaranteed if goals are met. Discretionary bonuses are at the employer's whim and cannot be expected. The FLSA defines nondiscretionary bonuses as those that are announced to employees to encourage them to work more steadily, rapidly, or efficiently, and those designed to encourage employees to remain with an organization. If there is an established set criteria an employee must meet, and the bonus is guaranteed to be earned once those criteria are met, that will be considered a nondiscretionary bonus. **All nondiscretionary bonuses must be included in the regular rate of pay, as outlined above, and will impact the overtime rate when they are issued in the same workweek in which overtime is earned.**

Not many bonuses qualify as discretionary under the FLSA, but those that do are excluded from the regular rate of pay and overtime calculations. A discretionary bonus provided to an employee is just that—something an employer is not obligated to provide and can give to any employee for any reason or no reason at all. Generally, they're given out of appreciation, loyalty, or good service. Employees do not expect them.

→ WILL NON-DISCRETIONARY BONUSES AND COMMISSIONS COUNT TOWARDS THE MINIMUM SALARY THRESHOLD?

Up to 10% of the minimum salary threshold may come from nondiscretionary bonuses, commissions, or other incentive pay for executive, administrative, computer, and professional employees. These payments must be made on at least an annual basis, and if the employee does not earn enough of this incentive pay to reach the exempt salary threshold, the employer must pay the difference to keep the employee's exemption intact. The DOL calls these "catch-up payments."

HCE employees can earn most of their income through incentive pay but must receive at least the weekly salary minimum applicable to exempt executive, administrative, or professional employees.

Note: *Those exempt under the outside sales employee exemption (which is narrow) are not subject to the minimum salary requirement.*

→ CAN I CLASSIFY AN EMPLOYEE AS SALARIED NON-EXEMPT?

Yes. However, this hybrid salaried/nonexempt pay classification can present challenges.

The idea behind paying employees this way is that for weeks where they work 40 hours or fewer, you can essentially hit the "regular weekly pay" button and be done with it. Unfortunately, this tends to make both the employer and employees lackadaisical about timekeeping. But this pay classification still requires strict timekeeping to determine overtime eligibility, just as for all nonexempt employees. This includes timekeeping entries for when work begins and ends as well as compliance with the state's meal and/or rest period requirements, if applicable. If hours are not tracked properly and there is a dispute, the burden of proof will be on the employer to substantiate that pay was accurate for hours worked, which will likely be very challenging.

→ DOES THIS CHANGE EVEN APPLY TO ME?

Almost certainly.

There are two ways in which employees can be covered by the FLSA. The first is called "enterprise coverage." This applies when an employee works for an employer that has an annual dollar volume of cash sales or business of $500,000 or more. It also applies if the employer is a hospital, business providing medical or nursing care for residents, school or preschool, or government agency.

The second type of cover is called "individual coverage." Even when there is no enterprise coverage, the FLSA will cover individuals engaged in interstate commerce. If an employee makes goods that will be shipped out of state, places telephone calls to another state, sends or receives out-of-state shipments, or partakes in any number of other basic business activities, they will qualify for individual coverage.

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EMPLOYEE RECLASSIFICATION LETTER - EXEMPT TO NON-EXEMPT

[Date]
[Name]
[Street address]
[City, State ZIP]

Dear [employee],

This letter is to inform you that your position has been reclassified as nonexempt. This change will be effective [date], at which time you will be paid [per hour, salary nonexempt, per piece rate].

As a nonexempt employee, you will be asked to track and record all hours worked, and you will receive overtime if you work more than 40 hours in a workweek. For your reference, our company workweek begins at midnight on [day] and ends at midnight on the following [weekday before the start of the workweek].

There are several company policies and practices that are important to be aware of regarding your new classification, most notably that you will now need to record all time worked so that you can be correctly compensated at your new hourly rate. This includes recording all start and end times as well as meal and rest breaks.

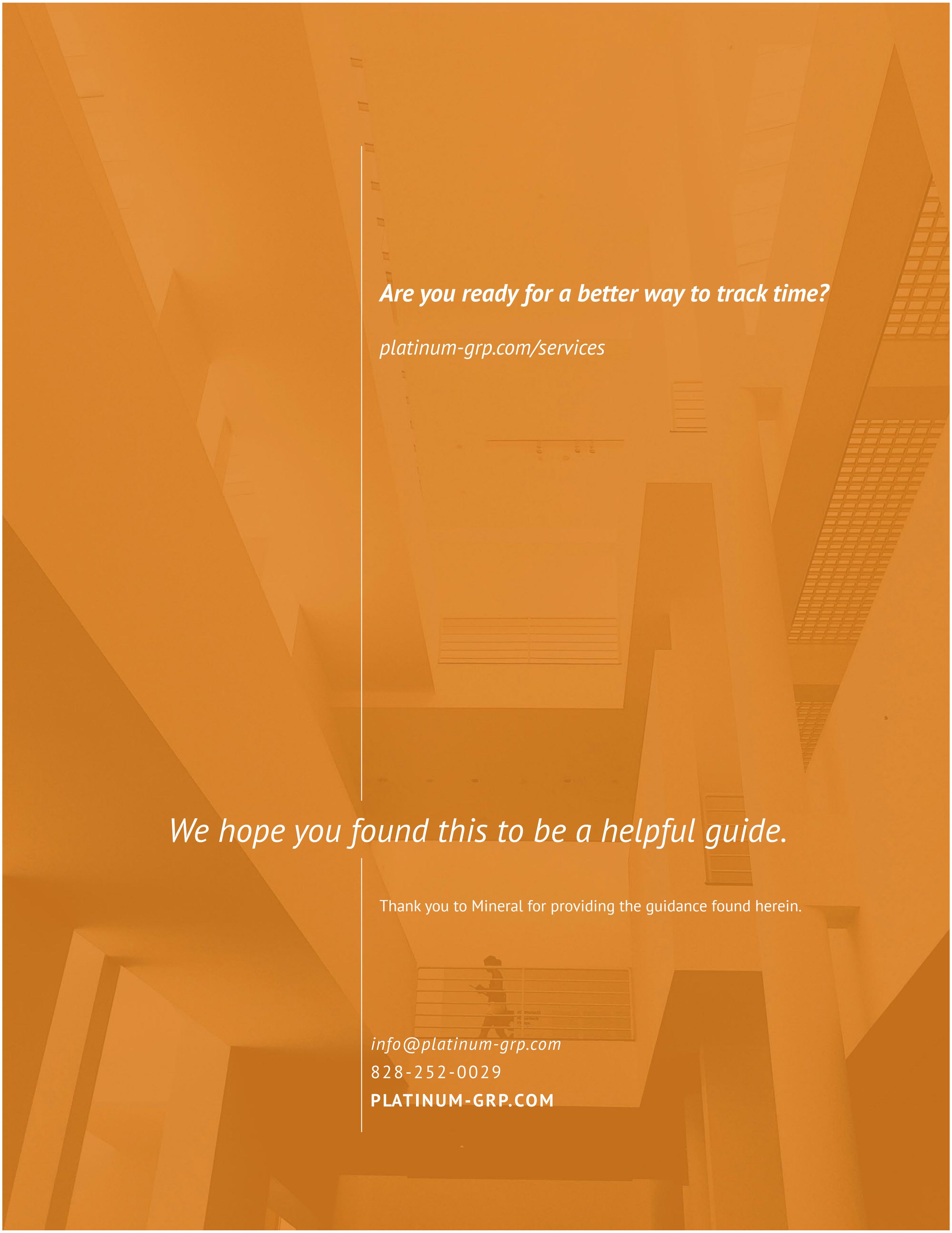
You play a key role with [company] and we assure you that this is not a demotion and has nothing to do with your value to [company]. We value your contribution and hard work for our team. Your job title and job duties will not change.

[Optional and suggested if true: Steps have been taken to ensure that reclassification does not result in a decrease in your compensation. If you work 40 hours per week, your compensation should remain the same. Because you are now eligible for overtime, your compensation may increase if you work more than 40 hours per week. Note that all overtime must be approved ahead of time by a manager.]

If you have questions or need further clarification about your classification, reach out to me, your manager, or [HR representative].

Sincerely,

[Signature]
[Name and title]



Are you ready for a better way to track time?

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We hope you found this to be a helpful guide.

Thank you to Mineral for providing the guidance found herein.

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