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ALERT

THE NEW OVERTIME REGULATIONS

The Fair Labor Standards Act ("FLSA") is the federal wage and hour law that generally requires covered employers to pay overtime (at time-and-one-half of employees' regular hourly wage rates) if employees work over forty hours in a workweek. The FLSA, however, contains certain broad exemptions. If an employee is "exempt," the employer is not required to pay the employee overtime pay.

On April 20th, the U.S. Department of Labor ("DOL") issued final revised regulations defining who qualifies as an exempt employee. These regulations significantly modified long existing regulations. The final regulations went into effect August 23, 2004.

We describe below the highlights from the new regulations.

Perhaps most significantly, the regulations provide for a new exemption category of "*Highly Compensated Employees*." To qualify for this exemption, an employee must be guaranteed \$100,000 in total annual compensation (including non-discretionary bonuses, provided the employee receives at least \$455 per week) and perform any *one* – rather than all – of the standard duties that are required for the other "white collar" exemptions to apply. Thus, a highly compensated employee will be exempt, for example, if s/he customarily and regularly directs the work of two or more employees *or* performs office work directly related to business operations. This exemption is very broad, and is likely to cover the majority of non-manual workers who earn over \$100,000. While easing the requirements for highly compensated employees, the regulations make it more difficult for low wage earners to be exempt from the overtime pay requirements. The final regulations increase from \$155 per week to \$455 per week (\$23,660 annually) the minimum weekly salary level necessary, in most cases, for an employee to be exempt.

The final regulations also made important changes to the definition of whether an employee is paid on a "salary basis" and thus eligible to be exempt. It always had been, and continues to be, the rule that an employee is paid on a salary basis only if s/he receives each pay period a predetermined amount that is not subject to reduction because of variations in the quality or quantity of the work performed. Most deductions from an employee's

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predetermined wage have had the potential to destroy an employee's exemption from receiving overtime pay. The final regulations create an important new exception allowing employers to make pay deductions for suspensions of one or more full days for violations of the employer's workplace conduct rules, such as violations of the employer's sexual harassment policy. In addition, the final regulations create a new "safe harbor" for improper deductions. If the employer has a written policy prohibiting improper deductions, including a complaint mechanism, notifies employees of the policy, and reimburses employees for improper deductions, the exemption will not be lost unless the employer repeatedly and willfully violates the overtime rules.

Finally, the final regulations replace the two tests under the former FLSA regulations with a single test for each exemption category, as follows:

- To satisfy the "*Executive Employee Exemption*," the employee's primary duty must be managing the enterprise, or a recognized department or subdivision thereof. In addition, the employee must (1) customarily and regularly direct the work of two or more employees, and (2) possess the authority to hire or fire other employees, or have his/her recommendations on employment status decisions given particular weight.
- To satisfy the "*Administrative Employee Exemption*," the employee's primary duty must (1) be performing office or non-manual work directly related to the management or general business operations of either the employer or its customers, and (2) include the exercise of discretion and independent judgment.
- To satisfy the "*Professional Employee Exemption*," the employee's primary duty must require advanced knowledge in a field of science or learning customarily acquired in a prolonged course of specialized intellectual instruction (unless the employee meets the standard of a creative professional, such as an artist).

The regulations discuss in further detail these exemptions, as well as special rules for other exemptions (e.g., outside sales employees, academic administrative employees, teachers, computer employees, and employees in the motion picture industry).

CLARIFYING THE ADMINISTRATIVE EXEMPTION

The administrative employee exemption traditionally has been the most difficult to apply. The new regulations provide helpful guidance. For example, work considered "directly related to the management or general business operations" includes work in functional areas such as finance, accounting, budgeting, research, human resources, etc.

Notably, under the former regulations an employee's use of discretion and independent judgment must have been "customarily and regularly exercised." Now, however, the use of discretion and independent judgment must be part of an employee's "primary duty." The final regulations provide that "factors to consider include, but are not limited to: whether the employee has authority to formulate, affect, interpret, or implement management policies or operating practices; whether the employee carries out major assignments in conducting the operations of the business; whether the employee performs work that affects business operations to a substantial degree; whether the employee has authority to commit the employer in

The regulations set forth new tests for qualifying for the Executive, Administrative and Professional exemptions.

matters that have significant financial impact; and whether the employee has authority to waive or deviate from established policies and procedures without prior approval."

The final regulations also add new examples particularly aimed at employees in the financial services industry. The regulations note that such employees "generally meet the duties requirements for the administrative exemption if their duties include work such as collecting and analyzing information regarding the customer's income, assets, investments or debts; determining which financial products best meet the customer's needs and financial circumstances; advising the customer regarding the advantages and disadvantages of different financial products; and marketing, servicing or promoting the employer's financial products. However, an employee whose primary duty is selling financial products does not qualify for the administrative exemption."

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Employers should review their classifications of employees as exempt or non-exempt and their pay and deduction practices, and should consider revising their policies to take advantage of the new "safe harbor" regarding deductions from wages. Class action lawsuits for overtime violations have become increasingly common and are likely to continue. These lawsuits can be extremely costly as they can result in back pay of up to six years (under New York law), double damages and attorneys' fees.

If you have any questions about the final regulations or your current overtime pay practices, please contact: **Mark E. Brossman** at (212) 756-2050, **Ronald E. Richman** at (212) 756-2048, **Holly H. Weiss** at (212) 756-2515, or **Scott A. Gold** at (212) 756-2051.

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