

Department of Labor Proposes Significant Changes to “White Collar” Overtime Exemption

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In a long-awaited 295-page Notice of Proposed Rule Making, the **Department of Labor's** Wage and Hour Division (DOL) has released its proposed changes to the “white collar” overtime exemption for executive, administrative, and professional employees. The new regulations are anticipated to go into effect in 2016.

Significantly, the DOL proposes to increase the minimum salary an employee must earn to be exempt from federal overtime pay requirements. Specifically, the DOL proposes the following:

- To increase the current exempt salary level from \$455 per week (\$23,660 annually) to \$970 per week (\$50,440 annually), which is expected to be the 40th percentile of weekly earnings in 2016 when the new regulations are anticipated to go into effect.
- To increase the exemption threshold for highly compensated employees (a special rule for highly paid employees who perform office or non-manual work and customarily and regularly perform at least one of the duties of an exempt executive, administrative, or professional employee) from \$100,000 per year to \$122,148 per year, which is the 90th percentile of weekly earnings currently. Notably, the proposed changes do not project the salary for 2016 when the new regulations are anticipated to go into effect.

The DOL's proposed change to the salary threshold is its first since 2004, when the salary threshold was increased to the current level of \$455 per week after it had been \$155 per week for 30 years. As a result, the DOL also is seeking to develop a method for automatically changing the salary thresholds to keep up with their respective percentages to weekly earnings.

The DOL's proposed changes are not law yet. The DOL must follow the rulemaking process set forth in the Administrative Procedure Act. The DOL is providing a 60-day comment period on the proposed rule changes. After the comment period closes and comments are reviewed, the DOL will hear testimony and finalize the proposed rules. This process may take another 90 to 120 days. After the rules are finalized, we expect the DOL to provide limited time for employers to comply with the rules. Employers should not expect a compliance period of more than the 120 days that the DOL afforded employers in 2004, and in fact, the DOL may impose a shorter compliance deadline with these new changes.

Of course, earning a salary that meets or exceeds the threshold is not the only requirement to be considered exempt from the overtime pay requirements. In addition, the duties employees perform in their day-to-day employment also must satisfy certain longstanding criteria articulated by the DOL in its regulations. Although the DOL has not submitted a proposal to alter the duties test at this time, changes may be in store, as the DOL has asked for comment on a number of questions focused on changing the duties test. Its goal seems to be to limit the amount of time an employee can spend on work that is not part of their “primary duties” (duties that render them exempt). If an alteration of the duties test is eventually added, this may become another means by which employees currently considered exempt may lose their exempt status, thus entitling such employees to overtime pay if they work more than 40 hours in a week.

Now that employers know this major proposed change will likely become law sometime soon, they need to start planning for this change, as it will affect the status of all salaried employees now treated as exempt who are earning less than \$50,440 annually. It is estimated that this change will affect 5 to 15 million employees, depending on the source of the estimate.

Employers facing these changes will need to budget for salary increases and/or increased overtime costs beginning sometime in 2016. Employers can reduce or avoid those payroll increases by taking measures such as reducing or eliminating the number of hours worked by salaried employees who are below the minimum threshold and are now treated as exempt. For example, employers may consider it cheaper to hire a part-time hourly worker to cover the extra hours the formerly exempt employee previously worked. Some employers may react by reorganizing their workforces with layoffs and job consolidations.

Another possibility will be to convert a salaried employee to an hourly employee at a lower hourly rate to offset any overtime the employee will be owed. For example, if an assistant manager earns \$42,000 per year (about \$808 per week), and usually works about 50 hours per week, the employer can set the hourly rate at an amount that, based on overtime hours historically worked, will approximate or even exceed the same amount the employee earned as an exempt employee. This is generally permissible, because the overtime laws do not direct an employer as to how much it should pay its employees; the laws dictate only that the employer must pay premium rates for hours worked over 40 in a single week. Naturally, the principal drawback with this approach is one of employee morale, as some employees may not appreciate being converted to hourly, at a lower rate no less, whatever the explanation. In fact, some employees may view this change as a demotion.

Another area of potential fallout from this rule change may be the ripple effect of an exempt employee becoming reclassified as a non-exempt employee. Some employers offer less generous benefits to non-exempt employees than those offered to exempt employees based on that status. This change, therefore, may affect vacation pay entitlement, eligibility for certain bonuses or profit-sharing, or even participation in certain types of insurance programs.

These are just some of the considerations regarding the adaptations many employers will need to consider once the proposed rule crystallizes and takes final shape.

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