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Overtime Rules: US Labor Department Issues Final Rule Hiking Salary Threshold for Exempt Employees

New US Labor Department regulation, to take effect January 1, 2020, raises the minimum base salary for exempt employees to US\$35,568.

Key Points:

The new regulation:

- Increases the minimum base salary for exempt employees under the Fair Labor Standards Act (FLSA) from US\$455 to US\$684 per week
- Increases the minimum annual compensation required to qualify for the FLSA's "highly compensated employees" exemption from US\$100,000 to US\$107,432
- Allows up to 10% of the minimum base salary to be paid through nondiscretionary bonuses and incentive payments
- Does not provide for automatic periodic increases to the salary level
- Formally rescinds the enjoined 2016 final rule that would have doubled the current minimum base salary for exempt employees

As reported in this [Client Alert](#), in March 2019, the US Department of Labor (the Department) proposed a new rule that would raise the minimum base salary required to qualify for an exemption from the overtime requirements of the FLSA under the "executive," "administrative," and "professional" exemptions (the so-called "white collar" exemptions). On September 24, 2019, that proposed rule became final with few significant changes, and will be effective January 1, 2020. The most notable changes from the proposed rule are a much smaller increase in the salary requirement for highly compensated employees and the lack of a schedule for future increases. The changes from the existing rules and the 2016 final rule are summarized in the table on page 2 of this *Client Alert*. Currently, employees who are classified as exempt under these FLSA exemptions must perform qualifying duties and must be paid on a salaried basis in an amount that equals at least US\$455 per week (or US\$23,660 annually). The new final rule does not modify the duties requirement.

Updates Under the New Rule

Recognizing that the current salary level, which was set in 2004, should be updated to reflect current wages, the Department has increased the minimum base salary to US\$684 per week, or US\$35,568 annually. This new salary minimum is far less than the US\$913 per week threshold the Department set in its 2016 final rule. The new rule formally rescinds the 2016 final rule, which a Texas federal court had ruled invalid shortly before it would have taken effect.

The new rule also raises the annual compensation threshold required to qualify under the FLSA’s “highly compensated employee” exemption to US\$107,432. The proposed rule raised the annual compensation level almost 50% above the current level and was, surprisingly, higher than the level set by the enjoined 2016 final rule. The new final rule raised the level just over 7% above the current level.

Similar to the 2016 final rule, the new rule permits employers to provide up to 10% of the minimum base salary (*i.e.*, up to US\$68.40 per week, or US\$3,556.80 annually) through nondiscretionary bonuses and incentive payments, including commissions, provided such payments are paid at least annually. This means an employer could pay an exempt employee at least 90% of the minimum base salary each pay period (*i.e.*, at the rate of at least US\$615.60 per week) and pay the additional 10% (*i.e.*, at most \$3,556.80 annually) at the end of the 52-week period through such alternative payment options. The new rule expressly provides that employers may use any 52-week period as the year, such as a calendar year, a fiscal year, or an anniversary of hire year.

The new rule allows employers to make a final catch-up payment within one pay period — after the end of each 52-week period — to any exempt employee who does not receive enough nondiscretionary bonus or incentive pay to cover the withheld 10% of the minimum base salary. Any such final catch-up payment will count toward the prior year’s salary, to meet the FLSA exemption salary test. Otherwise, if an employee does not receive the full minimum salary for the 52-week period needed to qualify for an FLSA exemption, the exemption would not apply, and the employee would be entitled to overtime pay for hours worked above 40 hours in a workweek.

Unlike the 2016 final rule, the new final rule does not include automatic periodic increases to the minimum base salary. The Department affirmed its intention to propose regular updates that would be subject to the standard rulemaking process, although it declined to specify the frequency of updates (while the proposed rule contemplated updates every four years).

This table sets forth a summary of the key FLSA updates under the new final rule, excluding the new special salary levels applicable to US territories, as compared to both the current rule and the enjoined 2016 final rule:

	Current Rule	Enjoined 2016 Final Rule	New Final Rule
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Minimum base salary to maintain the executive, administrative, and professional FLSA exemptions	US\$455 per week (US\$23,660 annually)	US\$913 per week (US\$47,476 annually)	US\$684 per week (US\$35,568 annually)
Minimum total annual compensation required to maintain the highly compensated employees FLSA exemption	US\$100,000	US\$134,004	US\$107,432

	Current Rule	Enjoined 2016 Final Rule	New Final Rule
Do nondiscretionary bonuses and incentive payments (including commissions) count toward the minimum base salary?	No	Yes, but only up to 10% of the minimum base salary, and provided such payments are paid at least quarterly	Yes, but only up to 10% of the minimum base salary, and provided such payments are paid at least annually
Special salary rules applicable to the motion picture producing industry, under which exempt employees need not be paid on a salaried basis, provided their base rate equals the rule's minimum level (based on a workweek of not more than six days)	US\$695 per week (or a proportionate amount based on the number of days worked)	US\$1,397 per week (or a proportionate amount based on the number of days worked)	US\$1,043 per week (or a proportionate amount based on the number of days worked)
Is there a mechanism for increasing the salary and compensation thresholds in the years to come?	No	Yes, automatic updates every three years	No; the Department intends to propose regular updates, but declined to specify the frequency of updates

The Department is hopeful the new rule will survive challenges in court this time round, given the less drastic minimum base salary increase. Further, unlike with the 2016 final rule, the Department used the same methodology to calculate the salary level it used in 2004, which has stood the test of time.

How Employers Can Prepare for the New Rule

Now that the new rule has become final, employers should review the base salaries of their exempt workforce and consider increasing base salaries or reclassifying employees as non-exempt, if and as necessary, by January 1, 2020. Employers may recall doing a similar drill in anticipation of the Department's 2016 final rule raising the minimum base salary to US\$913 per week. The new final rule provides a silver lining for employers who have already increased base salaries in anticipation of the enjoined 2016 final rule, as those employers may have little to do to prepare for the new final rule, given the proposed lower salary level.

As always, employers should ensure their exempt employees perform duties that satisfy the duties test of at least one FLSA exemption, which the final rule leaves as is. Further, employers should ensure their exempt employees are paid in accordance with applicable state or local laws that may impose stricter salary requirements, such as in California and New York, which the FLSA does not preempt.

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