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- *The government has proposed to lift the required salary for employees to qualify for exemptions to overtime.*
- *If the changes take hold, non-profits will be faced with critical choices about how to treat their low-salaried staff.*
- *The basics of minimum wage and overtime laws are explained.*

Forthcoming Federal Overtime Rules Deserve Your Attention

by Eric Hoffman and Sean Kim, Sidley Austin LLP

Non-profits operating in New York are subject to an overlapping set of federal, state, and local regulations governing their relationships with employees, and these laws provide numerous traps for the unwary. In particular, the laws regulating minimum wage and overtime pay and their related "exemptions" have proven difficult to apply with precision in many circumstances, leading to a rising tide of so-called "wage and hour" litigation. Lawyers for employment plaintiffs are now sensitized to these wage and hour issues, and so disputes with workers over other matters, for example, around termination, can often lead to the discovery of lurking wage and hour liability, completely changing the complexion of such disputes. On top of that, the U.S. Department of Labor has recently proposed regulatory changes that, if adopted, could dramatically expand the population of employees entitled to receive overtime pay. Because individual officers or directors of an organization can have personal liability for wage law violations in certain circumstances, prudent managers of a non-profit will pay careful attention to these issues as they develop over the coming months. This article summarizes the basics of wage and hour laws for non-profits operating in New York and how the upcoming changes to the law may impact them.

Background and Coverage

The Fair Labor Standards Act (the "FLSA") is a long-standing federal law that established the basic minimum wage and overtime protections with which most people are familiar. In general, the law requires that most employees receive pay that meets or exceeds the hourly minimum wage rate (currently set at $7.25 per hour) and that they receive pay at "time-and-a-half" (that is, 1.5 times their regular rate of pay) for any hours worked over 40 in a workweek. In addition, New York State regulations also require that employees receive pay that meets or exceeds a specific hourly minimum wage rate – the applicable rate is currently $9.00 per hour – and that they receive pay at "time-and-a-half" for any hours worked in a workweek over 40 hours.

While federal and New York wage and hour law are fairly similar, they do differ in the scope of the employers and employees that they cover. For constitutional reasons beyond the scope of this article, the FLSA only governs employers and/or employees who engage in interstate commerce (that is, business conducted across state lines), measured either by certain revenue

thresholds or certain activities tests. More specifically, the FLSA provides two ways an employee may be covered: "enterprise coverage" and "individual coverage."

"Enterprise coverage" covers employees by virtue of the characteristics of the employer, capturing employers with at least two employees that have at least $500,000 of annual revenue (from any source, not just across state lines[1]), or employers who are hospitals, nursing homes, businesses providing medical care, schools, preschools or government agencies of any level. Additionally, even if an employer does not meet these requirements and is not subject to "enterprise coverage," its employee may nevertheless be subject to "individual coverage" under the FLSA if their work is in connection with commerce between states. In practice, this standard is readily met, and examples of employees covered include a secretary who types letters sent to another state or a janitor who works in a building that manufactures goods that will be sold across state lines.

For non-profits operating in New York State, the question of whether they are covered by the federal law is largely academic, because New York's wage and hour provisions cover nearly all employees and currently provide for equal or greater protections than federal law. Thus, all non-profits with workers in New York State should currently be focused on compliance with New York's wage and hour laws, keeping in mind that in many instances, New York's law borrows from corresponding federal law principles. However, in light of the changes on the horizon for the FLSA described below, the distinction between the coverage of the FLSA and New York law could become more significant.

The Exemptions and Proposed Changes

Both New York and federal minimum wage and overtime laws have important exceptions for certain classes of employees, often referred to as the "exemptions." Employees who fall within these defined classes are often referred to as "exempt" employees, while employees who remain subject to the laws are often called "non-exempt" employees. Employees who are exempt from the minimum wage and overtime rules do not have to be paid overtime when their hours exceed 40 in a workweek, nor does the employer have to worry about their pay dipping below the minimum wage threshold. New York generally follows the FLSA regulations regarding these exemptions, but it is not bound to do so and that compatibility could soon change.

The four main exemptions are for "executive" employees, "administrative" employees, "professional" employees, and "computer" employees – with each exemption subject to its own "duties" test that examines the responsibilities attendant to the employee's job. Despite the simplicity of these titles, the application of the exemptions is complicated and is a frequent area of litigation and legal risk. Do not take these names at face value; when in doubt, consult with counsel over the application of these exemptions to particular employees.

A common thread that runs through all four exemptions is the requirement that the employee receive a fixed salary in excess of a particular monetary threshold set by law. Currently, the federal threshold is $455 per week ($23,660 annually) – a level that has not been changed in over a decade – while the New York state threshold has increased over the years and is currently set at

[1] "Donations" are not counted as "revenue" for the purposes of the $500,000 enterprise coverage test.

$675 per week ($35,100). (Employees meeting the criteria for the "computer" employee exemption must be paid either a salary above the threshold or an hourly rate at or above $27.63 per hour. Also, certain professionals, most notably teachers, are not subject to the minimum salary requirement.) Under the Department of Labor's proposed regulatory changes, the federal salary threshold for the exemptions would initially increase to $970 per week ($50,440 per year). This threshold would be adjusted annually thereafter to an amount equal to the 40th percentile of weekly earnings for salaried workers (as determined by the Department of Labor's surveys). Given New York's history of staying above the federal level, it is highly likely that New York State will raise its salary threshold to a level at or above the federal threshold once the federal regulations are finalized, but it is possible that there may be some period of time when federal law once again sets the minimum salary for exempt employees in New York.

Commentators have speculated that the federal regulations are likely to be finalized in the spring or summer of 2016 – indeed, the Department of Labor recently took the preliminary step of providing the final rules (which are still not available to the public) to the Office of Management and Budget in March, which suggests that the final rules may be published in early May and effective as soon as July. There is also newly introduced legislation before both houses of Congress that, if passed, could reverse the Department of Labor's proposed changes. Additionally, the Department of Labor has suggested that it may tinker with the "duties" tests for the various exemptions, but so far nothing concrete has been proposed in that regard. In short, there is still a great deal of uncertainty over when the new rules will take effect and what they will say, but employers will have only a short period of time to comply with the rules once they are published (likely 60 days), and so planning must begin now.

A Hobson's Choice

Many non-profits currently employ salaried workers who fit within the administrative or executive exemptions and are making salaries that are only slightly above New York's threshold ($35,100 annually). Thus, if and when the salary thresholds are increased – to above $50,000 if the proposed regulations are adopted – non-profits will have to confront two difficult questions.

First: Is the non-profit covered by the FLSA? As noted above, the "enterprise" and "individual" coverage tests are construed broadly and sweep in a great number of employees – however, some smaller operations may be able to argue that they and their employees are not covered by the FLSA. This is a question that should be tackled with the assistance of counsel. It should also be noted that New York is likely to act to raise its own salary threshold for the exemptions after the federal rules are finalized, such that any escape from the new federal salary thresholds could be exceedingly short-lived for New York non-profits.

Second: Should the non-profit maintain the pay levels of the affected employees and convert them to non-exempt status (which could lead to untold overtime pay), or should they raise the salaries of these employees to meet the new minimum threshold? In making this decision, employers should factor into their budgets not only the expected salary increases or overtime costs, but also the compliance-related costs of tracking hours where the employer previously did not. For operations that currently have no or only a few non-exempt employees, the administrative costs and burdens of tracking hours and calculating overtime pay for the affected

employees could be significant and may weigh in favor of increasing salaries to maintain exempt status.

Employers who choose to convert exempt employees to non-exempt status will want to carefully select the pay rate for these newly non-exempt employees. In conducting such conversions, employers may find it useful to estimate the expected overtime for a given role and then select an hourly rate that, once overtime is factored in, causes the combined straight-time and overtime compensation to approximate the prior salary level. New York state law also obligates employers to provide a written notice to employees of their pay rate change at least seven days before the change occurs.

Many employees who are converted to an hourly rate will find the transition demoralizing or irritating, as they will no longer have the prestige of a salary and will be required to keep track of the hours they work like other non-exempt employees. Some employers will want to explore arrangements to have salaried, non-exempt workers, which is permissible under certain circumstances, so long as the employee receives overtime premium pay when working more than 40 hours in a week – but there is simply no way to avoid tracking the hours worked by non-exempt employees.

The silver lining to this expected transition is that many lower-salary workers who are currently treated as exempt but whose exemption status is questionable under the "duties" test of the various exemptions will be reclassified as non-exempt, bringing their employers into compliance with the law. At the same time, many employees will experience a much-deserved bump in pay. Executive directors, boards, and treasurers will need to budget accordingly.

A Note of Caution

Finally, some employers faced with the dilemmas wrought by the new salary levels will be tempted to take shortcuts, such as reclassifying employees as independent contractors or attempting to replace employees with interns or volunteers. These are incredibly risky maneuvers, as incorrect classification of workers can result in penalties, interest, audits, and litigation. Before treading in such treacherous waters – and, again, mindful of the potential for individual liability on the part of officers and board members – any sensible soul will seek the advice of an attorney.

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