

Understanding the New Overtime Final Rule

On September 24, 2019, the U.S. Department of Labor announced its [Overtime Final Rule](#) that adjusts the salary level test, part of a three-part test for determining when white-collar workers are exempt or must be paid overtime for working more than 40 hours in a week. Effective January 1, 2020, the **salary threshold** for the white-collar exemption from overtime pay will rise to \$684 per week (\$35,568 per year). The Final Rule also raises the salary threshold for **highly compensated employees** who are exempt from FLSA overtime pay requirements from \$100,000 per year to \$107,432 per year and allows employers to satisfy up to 10 percent of the standard salary level by using nondiscretionary bonuses and incentive payments.

The Overtime Final Rule: In a Nutshell

At issue is the provision of the federal Fair Labor Standards Act (FLSA) that exempts certain employees from the requirement that they receive time-and-a-half overtime pay for work in excess of 40 hours in a work week. The salary threshold is one of a three-part test that must be satisfied before a person can be deemed “exempt”; each exempt employee must **(1)** be paid on a salary basis; **(2)** be paid at least the salary threshold set forth by DOL (at issue in the Final Rule); and **(3)** satisfy a duties test as [executive](#), [administrative](#), or [professional](#) workers. The Final Rule does not change the salary basis or duties tests; only the salary threshold is at issue.

The Overtime Final Rule does three things of significance to charitable nonprofits:

1. Updates the **standard minimum level for salaried workers**, raising it from \$455 per week (\$23,660 per year) to \$684 per week, or \$35,568 per year. The Department has retained the existing methodology for setting the level, using the 20th percentile of earnings of full-time salaried workers in the lowest-wage census region (the South) and in the retail sector. As a result of the adjustment, the new level is 50 percent higher than the current level that was last updated in 2004. The new level is only half as much as the increase (to \$955/week; \$47,476/year) approved by the Obama administration in 2016, but that was blocked by a federal court.
2. Raises the salary minimum for **highly compensated employees** (HCE) from \$100,000 a year to \$107,432 annually, of which \$684 must be paid weekly on a salary or fee basis. The new minimum is set at the annualized value of the 80th percentile of weekly earnings of full-time salaried workers. This is lower than the 90th percentile methodology initially proposed earlier this year.
3. Permits employers to treat **nondiscretionary bonuses and incentive payments** (including commissions) paid on an annual or more frequent basis to satisfy up to 10 percent of the standard salary level. The Obama Administration had also adopted this change.

The Labor Department announced further that it intends to propose updates to the salary and compensation levels on a regular basis, to ensure that these levels provide useful tests for exemption. It declined, however, to set a regular schedule, e.g., every four years.

The Final Rule goes into effect on **January 1, 2020**. It does not include a phase-in period or carve-outs for nonprofits or other sectors, as some commenters had requested. The new rule does not alter the existing duties tests for executive, administrative, or professional employees.

Background

Under the Fair Labor Standards Act (FLSA), employees are entitled to wages at or above the federal minimum wage and must be paid time-and-a-half overtime for work after 40 hours in any work week. In enacting the federal wage and hour law, Congress exempted from these standards executive, administrative, and professional employees, and left it up to the Secretary of Labor to define the terms of the exemption.

Persons who are properly classified as executive, administrative, or professional employees are considered “exempt employees.” All others are “non-exempt” and must be paid at least the minimum wage and overtime after 40 hours worked in a week.

Generally, employers have the burden of demonstrating that a worker is exempt from the overtime provisions by satisfying three tests. The **salary basis test** requires that the employee be paid a predetermined salary, rather than on an hourly basis, and that the amount paid is not adjusted based on whether the person worked certain hours. The **duties test** requires that the individual’s job duties must primarily involve [executive, administrative, or professional](#) duties as defined by the Labor Department regulations. The **salary level test** – which is the subject of the Final Rule – requires that an employee be paid at or above a minimum specified amount. That amount is currently set in regulations at \$455 per week, or \$23,660 per year, and requires regulatory action by the Department of Labor to change it.

There is a special category in the regulations that exempts “highly compensated employees” if their total annual compensation exceeds \$100,000 and they customarily and regularly perform at least one of the exempt duties or responsibilities of an executive, administrative, or professional employee.

In 2016, the Obama Administration issued regulations to raise the salary threshold to \$913 per week (\$47,476 per year) and the minimum threshold for highly compensated employees to \$134,004 per year. A federal district court in Texas [struck down those regulations](#), ruling that the Labor Department exceeded its authority. Many nonprofits expressed concern that the Obama Administration's 2016 overtime rule would have created significant [new costs for their organizations](#). Other nonprofits appreciated that the DOL's 2016 overtime rule would have raised pay and reduced working hours for many nonprofit employees, and helped lift out of poverty many individuals that the nonprofits served.

Analysis and Nonprofit Perspective

The Overtime Final Rule implements a 50 percent increase in the salary level test that was last set 15 years earlier, a period that saw a 33 percent increase in the federal poverty level. The Labor Department estimates that 1.2 million additional workers will be entitled to minimum wage and overtime pay as a result of the increase to the standard salary level. It also estimates that a little more than 100,000 employees will be entitled to overtime pay as a result of the increase to the HCE compensation level.

Based on its initial analysis, the Department estimates that about seven percent of nonprofit and government employees nationally will be affected by the higher salary threshold (compared to five percent of for-profit employees). It acknowledges, “To the extent that employers respond to this rule by restricting employee work hours, this rulemaking could negatively affect the quality of public services provided by local governments and nonprofits.”

Coverage Questions

In the past, some small employers and nonprofits have questioned whether the statute actually applies to them and their employees. Which nonprofits are covered by the new overtime rule is a simple question with a complicated answer for each nonprofit, and depends on the nature of your revenues, the work that individual employees perform, and where your employees perform their duties. Here are important considerations:

- Does the FLSA cover our nonprofit? (“Enterprise coverage.”) The [federal DOL](#) explains: “The FLSA generally applies to (‘covers’) employees employed by businesses with annual gross volume of sales made or business done of at least \$500,000.” The question becomes whether your nonprofit is an [enterprise covered](#) by the FLSA. Certain nonprofit workplaces are [automatically covered as “named enterprises,”](#) such as schools, pre-schools, hospitals, mental health centers, and residential care facilities. Other covered enterprises are those that have earned income via interstate commerce resulting in gross revenues over \$500,000. Income from charitable activities does not count towards the \$500,000 – so contributions, membership dues, in-kind donations, and proceeds from fundraising special events are not counted. (See [DOL Fact Sheet #14A.](#))
- Does the FLSA cover any of our employees? (“Individual Coverage.”) Even if your organization is not a covered enterprise under the FLSA, the law still applies to many individual employees whose job responsibilities put them under the protection of the law because they are “engaged in interstate commerce.” In the past, the Department of Labor has given clear indication that it thinks just about everything employees do these days involves interstate commerce – ranging from sending and receiving emails to counting supplies that come in from out of state. Therefore, a nonprofit employer could easily be responsible for paying overtime for some individual employees, even if the organization is not covered as an “enterprise.” (See [DOL Fact Sheet #14A.](#))
- What does state law say about labor standards? Reviewing the federal coverage rules is not the end of the inquiry. In [ten states and the District of Columbia](#)¹, the Overtime Final Rule will apply to virtually every nonprofit employer and employee because their state laws automatically incorporate DOL regulations into state law. Therefore, nonprofits in those states needn’t spend time evaluating whether they are covered enterprises or whether their employees are engaged in interstate commerce; the new rule applies to their employees via state law.

Further, the FLSA does not pre-empt state labor laws; whichever law (federal or state) provides the higher labor standards prevails. Currently, 29 states have set minimum wage levels [higher than the federal minimum wage](#) of \$7.25 per hour. California and New York have set the salary level test for exempt employees at a higher amount than is established in the U.S. Department of Labor Overtime Final Rule. Washington State is currently engaging in rulemaking to raise its salary level test higher than any other state.

Impact on Government Grants and Contracts

As of January 1, 2020, the effective date of the Overtime Final Rule, nonprofits with government grants and contracts at any level of government (local, state, tribal, or federal) will be put in the position of having to comply with new federal requirements that impose new costs that likely were not known when those grants and contracts were signed. Unlike businesses that can raise prices, or governments that can raise taxes or curtail public services, nonprofits with government grants and

¹ Alaska, District of Columbia, Illinois, Maine, Maryland, Massachusetts, Missouri, New Jersey, New York, North Carolina, and Ohio.

contracts may find themselves contractually bound to maintain services at increased costs that may not be expressly covered by existing written agreements. Federal for-profit contractors are entitled to seek “labor standards adjustments” or “equitable adjustments” to protect them from government-mandated labor cost increases, but that right is not currently available to nonprofits performing work under government grants. Nonprofits with government grants and contracts are encouraged to alert their cognizant agencies of the impact of the Overtime Final Rule on costs and to ensure that future contract and grant negotiations incorporate changes to reflect the new labor standards. Learn more about the interplay between labor regulations and grants rules by reading the [Nonprofit Joint Comments to Overtime Proposed Rule](#). See also, [The Nonprofit Overtime Implementation Conundrum](#).

Additional Resources

- DOL Overtime Final Rule: [Defining and Delimiting the Exemptions for Executive, Administrative, Professional, Outside Sales and Computer Employees](#) (RIN 1235-AA20), announced September 24, 2019
- [DOL News Release](#), September 24, 2019
- [DOL Fact Sheet](#), September 2019
- [DOL Frequently Asked Questions](#)
- [DOL Overtime Pay](#) webpage
- [Fact Sheet #14: Coverage Under the Fair Labor Standards Act \(FLSA\)](#)
- [Fact Sheet #14A: Non-Profit Organizations and the Fair Labor Standards Act \(FLSA\)](#)
- [Small Entity Compliance Guide](#)
- [Public Comments to the Overtime Proposed Rule](#), National Council of Nonprofits, May 15, 2019
- [Nonprofit Joint Comments to Overtime Proposed Rule](#), May 15, 2019, explaining the need for federal grants reforms due to changes in the overtime rules; signed by EasterSeals, National Council of Nonprofits, National Human Services Assembly, YMCA, and YWCA
- [Breaking down your nonprofit's obligation to pay overtime](#), National Council of Nonprofits website
- [Classifying Employees Correctly](#), National Council of Nonprofits website
- [The Nonprofit Overtime Implementation Conundrum](#), National Council of Nonprofits, June 2016

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