

APRIL 25, 2024 | WAGE & HOUR COMPLIANCE

DOL Finalizes Overtime Rule – Significantly Increasing Salary Level Basis Threshold for FLSA Overtime Exemptions

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On April 23, 2024, the U.S. Department of Labor (“DOL”) finally released its [final rule](#) raising the salary threshold for overtime exemptions titled Defining and Delimiting the Exemptions for Executive, Administrative, Professional, Outside Sales and Computer Employees. The rule will **phase in the new salary threshold in two steps over the next eight months, and automatically update it every three years thereafter based on Census data. The increase in the salary level basis threshold is a dramatic shift from the current threshold. As such, employers should audit their current wage practices promptly to ensure they are compliant with the new rule, as the first increase is set to take effect in just over two months on July 1, 2024.**

Overview of the Executive, Administrative, and Professional Employees Overtime Exemption

Unless specifically exempted under the FLSA, U.S. hourly workers are entitled to be paid no less than time-and-half their regular rate of pay for all hours worked in excess of 40 hours a week. The additional income is called “overtime pay.”

However, up until now, a certain subset of employees – i.e. executive, administrative, and professional workers, are exempt from the FLSA’s overtime pay requirements provided they satisfy all three of the following tests:

- *The Salary Basis Test.* Employees must be paid a salary – i.e., a predetermined and fixed amount that is not subject to reduction because of variations in the quality or quantity of work performed.
- *The Salary Level Basis Test.* Employees must earn at least \$684 per week, or \$35,568 per year.
- *The Duties Test.* Employees’ duties must primarily involve executive, administrative, or professional duties as defined by the regulations. There is a less restrictive duties test for certain highly compensated employees (“HCE”) – those who are paid at least \$107,432 annually and at least \$684 per week.

DOL’s final rule significantly increases the salary-level basis thresholds for the executive, administrative, and professional workers exemption and the highly compensated employee exemption.

Overview of DOL’s Changes to Salary-Level Basis Test

On August 30, 2023, DOL proposed to change the minimum salary threshold under the salary level basis test. The salary basis test was modified previously in 2019 where the minimum salary for an exempt employee was increased from \$455 per week to \$684 per week. The changes also included a provision for total annual compensation for HCEs, which was increased from \$100,000 to \$107,432 per year. The 2019 FLSA regulations also allowed employers to use non-discretionary bonuses and incentive payments, including commissions, which are paid at least annually, to satisfy up to 10% of an employee’s standard salary when considering exempt status.

Fast forward a little over four years later, and DOL has increased the salary level test threshold again, and in a significant way. The final rule will raise the threshold to the equivalent of a \$43,888 annual salary on July 1, 2024 and then to the equivalent of \$58,656 on January 1, 2025, based on a new methodology. Those figures represent a significant increase from the current rate of \$684 a week or \$35,568 a year. The 2025 update is aligned with the 35th percentile of weekly earnings of full-time salaried workers in the lowest-wage U.S. Census region, which is the Southern United States.

The rule will also raise the overtime salary threshold for HCEs from \$107,432 to \$132,964 on July 1, 2024 and then to \$151,164 on January 1, 2025, which is aligned with the 85th percentile of salaried workers nationally.

Salary Level Threshold Changes 2004-2025

2004	Jan. 1, 2020	July 1, 2024	Jan. 1, 2025
\$455 per week	\$684 per week	\$844 per week	\$1,128 per week
(\$23,660 annually)	(\$35,568 annually)	(\$43,888 annually)	(\$58,656 annually)

Highly Compensated Employee Exemption

2004	Jan. 1, 2020	July 1, 2024	Jan. 1, 2025
\$100,000	\$107,432	\$132,964	\$151,164

DOL estimates that the rule will benefit nearly 4.3 million workers – with the largest number of impacted workers being employed in professional and business services, health care and social services, and financial activities

Automatic Triennial Updates

Importantly, automatic updates will take place every three years based on the latest earnings data. Previously, DOL updated the threshold through formal rulemaking. Going forward, DOL now will look at the available U.S. Census salary data every three years and publish a new threshold. That threshold might be delayed in some circumstances when unforeseen economic or other conditions warrant, but future changes will otherwise take effect automatically. DOL believes that this updating mechanism will ensure the earnings thresholds keep pace with changes in earnings and remain useful in the future in helping to delineate executive, administrative, or professional (“EAP”) employees from non-EAP employees and the triennial updates would provide greater certainty and predictability for the regulated community.

No Changes to Duties Test

DOL has again decided to make no changes to the duties test. Therefore, employers must continue to evaluate the responsibilities of an employee to determine whether they primarily perform duties appropriately characterized as executive, administrative, or professional. Even though the test has not been altered and remains a qualitative assessment, its application will likely be under scrutiny as the DOL oversees and enforces this final rule.

Legal Challenges

A legal challenge is likely given the manner in which DOL promulgated this rule. Stakeholders successfully challenged a similar proposal by the Obama Administration, which in 2016 sought to raise the salary threshold to \$47,476 with automatic triennial increases. The U.S. District Court in the Eastern District of Texas found that the updated salary threshold was so high that it made the job duties portion of the exemption test irrelevant. *Nevada v. Dep’t of Labor*, 275 F.Supp.3d 795 (E.D. Texas 2017). The court held that DOL did not lack the authority to set a salary threshold, but that the Department lacked authority to set a salary threshold so high that it defeated the purpose of the FLSA to establish a functional test for exempt status based upon job duties.

Furthermore, [a restaurant owner sued the Department of Labor](#) in 2022, arguing that the DOL exceeds its authority by imposing the current overtime exemption salary level test that took effect in 2020. A lower court ruled in favor of the DOL, but it was appealed to in the U.S. Court of Appeals for the Fifth Circuit and is ongoing. The \$58.656 salary thresholds schedule to take effect on Jan. 1, 2025 is almost 20% higher than the \$47,476 salary threshold proposed under the Obama administration, which will draw close scrutiny from a court.

Potential Impact on State Wage & Hour Laws

States are permitted to have their own wage and hour laws, as long as those laws provide more protections for employees than the federal laws. If the proposed federal regulations survive legal challenges, those updated federal regulations could be more protective than some current state and local laws. In such case, those state and local laws will also need to change.

One notable change from the initial proposed rule is that the new rule does not apply the salary level changes to the U.S. territories of Puerto Rico, Guam, the U.S. Virgin Islands, and the Northern Mariana Islands. DOL will address the salary threshold in those jurisdictions through a separate rulemaking.

Practical Takeaways

Beginning July 1, 2024, any exempt employee making less than \$844 per week, or \$43,888 per year, must be (1) paid total compensation equal to the new salary threshold; or (2) reclassified as a non-exempt employee, who will be entitled to overtime pay. The new rule will almost certainly increase the number of nonexempt employees, especially in certain areas of the country, and broaden the types of jobs that will be entitled to overtime pay. As such, employers should prepare for the proposed rule and consider doing the following:

- Review employee classifications to determine which employees qualify as exempt under the executive, administrative, and professional exemptions.
- Identify whether any of the covered employees make less than \$55,068 per year, as you will need to convert them to non-exempt status or phase in salary increases following the rule's two step salary level basis increases.
- Determine how you will track the hours worked by affected employees and manage the payment of overtime.
- If feasible, consider raising affected employees' salaries to at least \$58,656 per year, such that they will remain exempt.
- Review policies and procedures covering affected employees to ensure the guidance and rules contained therein will remain appropriate if those workers become eligible for overtime – e.g., policies that concern the use of company-issued mobile devices or access to company resources, such as email, outside of regular work hours.
- Train affected employees on the company's timekeeping policies and practices.

Our [Labor and Employment practice](#) will continue to monitor the impact of final rule on employers and any legal challenges that may be filed.