Changes to Federal & Washington State Overtime Exemption Rules

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I. INTRODUCTION

In 2020, new federal and Washington State rules regarding overtime exemption will go into effect, which will impact employee eligibility for overtime pay and other worker protections.

This guide provides an overview of the basic requirements for overtime exemptions, including examples of employees who may or may not be considered “exempt” and a summary of the changes employers should expect with the implementation of these new rules, such as increased salary threshold requirements and clarification of exempt job duties. Finally, outlined below are options for how employers may incorporate these new rules into daily operations to ensure legal compliance.

II. REVIEW OF MINIMUM WAGE AND OVERTIME REGULATIONS

Washington Minimum Wage in 2020
$13.50 per hour

Seattle Minimum Wage in 2020

For Small Employers (500 or fewer employees worldwide)
$15.75 per hour without medical benefits or tips
$13.50 per hour with at least $2.25 per hour in medical benefits or tips

For Large Employers (more than 500 employees worldwide)
$16.39 per hour

**Applicability of Minimum Wage**
All individuals who provide services at an employer’s request or direction must be paid at least the minimum wage for all hours worked. Any time an individual spends providing these services for the benefit of an employer, even if for public or charitable purposes, is considered hours worked. Employees may not perform their normal work duties, or the work duties of another individual who is classified as an employee, without receiving compensation for such work. This rule applies to private, for-profit companies as well as non-profit organizations, and includes all levels of service (e.g., administrative staff, program managers, executive directors). All employees must be paid for their hours worked at a rate that is at least the minimum wage in effect at the time the services are performed.

*In Washington, employees who work more than 40 hours in a workweek must be paid overtime unless they meet all of the requirements to be exempt from overtime (discussed below).*

- Employers are allowed to require employees to work overtime.
- Overtime must be paid at 1.5 times the employee’s regular hourly rate of pay for each hour worked in excess of 40 hours.
- Employees may not waive their right to overtime pay.
- Employers must pay overtime to non-exempt employees regardless of the size of the business.
III. OVERTIME EXEMPTIONS

Employees who are classified as “exempt” are not required to be paid overtime. This means that these employees may work more than 40 hours in a workweek without having to be paid anything extra for the additional hours worked. Employers may pay these employees bonuses or additional compensation or give them time off (“comp time”) for the extra hours worked, but they are under no obligation to do so. Generally, exempt employees are managers, professionals, and other senior employees and typically they are paid a salary.

What are the requirements for an employee to be classified as exempt?

To be classified as “exempt”, an employee must satisfy ALL of the following tests:

1. Salary basis test: The employee must be paid a fixed salary
2. Salary threshold test: The employee’s salary must meet a set threshold (some exceptions apply)
3. Job duties test: The employee must regularly perform exempt job duties

It is important to remember that an employee’s exempt status is not determined by their job title or job description. Unless an exception applies (such as for certain professions), if an employee does not satisfy all the above tests, they will be considered a non-exempt employee and must be paid overtime. Non-exempt employees must be paid for any time worked in excess of 40 hours per workweek and other benefits and protections such as minimum wage, paid sick leave, and meal and rest breaks.

For purposes of legal compliance, it is up to the employer to prove that an employee satisfies all of the requirements for exemption from overtime and other regulations.

Exemption Test #1: Salary Basis Test
Is the employee paid a fixed salary?

An employee is paid on a fixed salary basis if:

- The employee is regularly paid a set amount each pay period (e.g., $3,000 every two weeks or $2,500 twice per month);
- The set amount may not be reduced because of variations in the employee’s quality or quantity of work; and
- The employee is paid their full salary for any week in which they performed any work, regardless of the actual days or hours worked in that week.

Some employees may be considered exempt even if they are not paid a salary, but instead are paid on a “fee basis” – a fixed amount for the completion of a job, rather than by the hour. The fees still must meet the minimum salary threshold (described below) in effect at the time the work is performed.

To avoid jeopardizing an employee’s exempt status, as long as the employee has performed any work in a workweek, the employee’s salary may not be reduced for the following reasons:
• Partial day absences for personal reasons, sickness, or disability;
• Absence on a day when the employee’s worksite is closed (e.g., holidays or shutdowns); or
• Absences for jury duty, attendance as a witness, or military leave in any week in which the employee has performed any work.

However, an exempt employee’s salary may be reduced for the following reasons without jeopardizing the employee’s exempt status:

• Disciplinary absences for major safety violations or serious employee misconduct;
• Full day absences for personal reasons;
• Full day absences for sickness or disability, if available paid sick leave has been exhausted;
• Intermittent absences, including partial-day absences, covered by the federal Family and Medical Leave Act, if other available paid leave has been exhausted;
• To offset amounts received as payment for jury and witness fees, military pay, or Washington’s paid family and medical leave;
• During the first or last week of employment when an employee works less than a full week; and
• Any workweek in which an employee performs no work for the employer.

An exempt employee’s salary also may be reduced for certain types of deductions, such as state and federal payroll taxes, the employee’s portion of health insurance premiums, or voluntary contributions to a 401(k) plan or other benefit plans.

Exemption Test #2: Salary Threshold Test
Does the employee’s salary meet the minimum salary threshold?

With some exceptions, employees must be paid a salary that meets a certain threshold amount in order to be considered exempt. Employees who are not required to meet this salary requirement include outside salespersons, teachers, computer professionals, attorneys, and physicians. Such employees still must satisfy all of the other exemption tests to be considered exempt.

Prior to January 1, 2020, the federal salary threshold was $455 per week, or $23,660 per year, while the salary threshold in Washington was $250 per week, or $13,000 per year. Because the state salary threshold was lower than the federal threshold, Washington employers have been required to use the federal threshold when determining an employee’s exempt status.

As of January 1, 2020, the salary thresholds under federal law and in Washington have increased and are scheduled to regularly increase throughout the next decade. These changes are detailed in Section III below.

As of January 1, 2020, the federal salary threshold increased to $684 per week, or $35,568 per year.

As of July 1, 2020, the Washington salary threshold will increase to $675 per week, or $35,100 per year. Despite the salary threshold increase at the state level, Washington employers must continue to follow the 2020 federal standard because it provides greater benefits to employees. Beginning in 2021, Washington’s threshold will be higher than the federal threshold, so employers will use that standard.
Federal law specifies that “highly compensated employees” (HCEs) may be exempt if they are paid at least $107,432 per year, but Washington does not recognize the HCE exemption, so this exemption may not be used in the state.

In order to determine whether an employee paid on a fee basis satisfies the salary threshold test, the employer should consider the time required to complete the job and divide the total fee by the amount of time required. This hourly rate must be at least the weekly salary threshold, if the employee were to work 40 hours in a workweek.

For example, a journalist who is paid $300 for writing an article that took 15 hours to complete would satisfy the salary threshold requirement because their hourly rate would be calculated as $20 per hour. Multiplying this hourly rate by 40 – the number of standard workweek hours – the employee would earn $800, which exceeds the 2020 weekly salary threshold of $684 per week.

**Exemption Test #3:**
Does the employee regularly perform exempt job duties?

Employees also must regularly perform certain exempt job duties – generally those at a professional or management level – in order to be classified as exempt.

**Definitions:**
- **“Primary duty”** refers to the main or most important duty that the employee performs. Factors to consider include the relative importance of exempt duties vs. other duties, the amount of time spent performing exempt work, the employee’s freedom from direct supervision, and the employee’s salary vs. wages paid to other employees for performing similar non-exempt duties. Generally, an exempt employee must spend more than 50% of their time performing exempt duties.
- **“Customarily and regularly”** means more than occasionally, but less than constantly, including work that is normally performed every workweek, but not isolated or one-time tasks.

**Executive Exemption**

An employee may be classified as exempt under the executive exemption if:

- Their primary duty is management of the employer’s enterprise or a department or subdivision of the enterprise;
- They customarily and regularly direct the work of 2 or more other employees; and
- They have the authority to hire or fire other employees or whose input with regarding to hiring, firing, advancement, promotion of other employees is given particular weight.

“**Management**” includes setting employees’ rates of pay and hours of work; directing the work of employees; appraising employees’ productivity and efficiency; handling employee complaints and grievances; disciplining employees; planning the work of and apportioning work among employees; determining the type of materials or tools to be used; and planning and controlling the budget.

“**Two or more employees**” means two full-time employees or their equivalent (e.g., one full-time employee and two part-time employees).
Administrative Exemption

An employee may be classified as exempt under the administrative exemption if:

- Their primary duty is the performance of office or non-manual work directly related to the management or general business operations of the employer or the employer’s customers; and
- Their primary duty includes the exercise of discretion and independent judgment with respect to matters of significance.

“Directly related to the management or general business operations” refers to assisting the running or servicing of the business, including performing administrative functions in school or university, as distinguished from working on a manufacturing production line or selling a product in a retail store.

“Discretion and independent judgment” means comparing and evaluating possible courses of conduct and acting or making a decision after the various possibilities have been considered. This requires that the employee has the authority to make an independent choice, free from immediate direction or supervision, even if major decisions or recommendations are reviewed at a higher level, but does not include clerical or secretarial work, recording or tabulating data, or performing mechanical, repetitive, recurrent, or routine work.

Professional Exemption

An employee may be an exempt professional if their primary duty consists of the performance of work:

- Requiring knowledge of an advanced type in a field of science or learning customarily acquired by a prolonged course of specialized intellectual instruction; or
• Requiring invention, imagination, originality, or talent in a recognized field of artistic or creative endeavor.

Exempt professionals include teachers, professors, instructors, and lecturers in “educational establishments,” which is defined as an elementary or secondary school system, an institution of higher education, or other educational institution. These types of employees must be paid on a salary or fee basis, but the salary threshold does not apply to them.

Exempt professionals also include practicing, licensed attorneys and physicians, and the salary basis requirement and salary threshold do not apply to them.

“Customarily acquired by a prolonged course of specialized intellectual instruction” refers to professions where specialized academic training is a standard prerequisite for entrance into the profession, as opposed to professions that may be entered through apprenticeship or on-the-job training only.

“Field of science or learning” means the professions of law, medicine, theology, accounting, actuarial computation, engineering, architecture, teaching, physical, chemical, and biological sciences, pharmacy, and other occupations that have a recognized professional status.

“Recognized field of artistic or creative endeavor” includes music, writing, acting, and graphic arts.

“Work requiring advanced knowledge” means work that is predominantly intellectual in character, including work requiring the consistent exercise of discretion and judgment, as distinguished from performance of routine mental, manual, mechanical, or physical work. An employee who performs work requiring advanced knowledge generally uses the advanced knowledge to analyze, interpret, or make deductions from varying facts or circumstances. Advanced knowledge cannot be attained at the high school level.

Exemption in Practice:
Terry, Music Instructor

Terry is a music instructor for a music school. Terry has played the piano as a hobby for 10 years, and was hired by the owner of the music school to provide one-on-one piano lessons as an instructor at the school. Terry provides weekly music lessons to 10 students on a weekly basis. Because Terry did not complete a prolonged course of specialized instruction in music or piano studies and is not a certified teacher at an accredited educational institution, Terry is a non-exempt employee and must be paid overtime.

Computer Professional Exemption

An employee may be classified as exempt under the professional exemption if they are a computer system analyst, computer programmer, software engineer, or similarly skilled worker and their primary duty consists of one of the following:

• The application of systems analysis techniques and procedures, including consulting with users, to determine hardware, software, or system functional specifications;
• The design, development, documentation, analysis, creation, testing, or modification of computer systems or programs;
• The design, documentation, testing, creation, or modification of computer programs related to machine operation systems; or
• A combination of the above duties.

Currently, exempt computer professional employees must meet the salary threshold requirement unless they are paid on an hourly basis, in which case they must be paid at least $27.63 per hour.

Exemption in Practice:
Avery, Senior IT Help Desk Technician
Avery is a senior IT help desk technician at a financial services company. Avery has worked at the company for 15 years and has intimate knowledge of all of the company's hardware, software, and enterprise applications. Avery typically works 45 to 50 hours per week, setting up hardware and software for new employees, resolving high-level technical issues that have been escalated by lower level IT help desk staff, and managing the help desk software system. Because Avery's primary duty does not consist of exempt computer professional duties and does not manage other employees or manage the company's business operations, Avery is a non-exempt employee and must be paid overtime for all hours worked in excess of 40 per workweek.

Outside Salespersons
An employee may be an exempt outside salesperson if their primary duty consists of:

• Making sales, including any sale, exchange, contract to sell, consignment for sale, or shipment for sale or other disposition; or
• Obtaining orders or contracts for services or for the use of facilities; or
• Demonstrating products or equipment for sale; or
• The sale of services and performance of the service sold when the compensation to the employee is on a commission basis.

Exempt outside salespersons must be customarily and regularly engaged away from the employer's place of business (i.e., "outside") and may spend no more than 20% their time performing work other than those listed above plus work incidental to making outside sales, such as deliveries and collections.

Outside salespersons must be compensated on a guaranteed salary, commission, or fee basis, but they are not subject to the salary threshold requirement.

IV. CHANGES TO OVERTIME EXEMPTION RULES

In 2020, the rules for determining overtime exemption have changed or will change at both the state and federal level, including:

**Federal Overtime Rule Changes**
- Increased salary threshold requirement
- What may be included in salary
- Catch-up payment
- No automatic mechanism for updates

**State Overtime Rule Changes**
- Increased salary threshold requirement
- Methods for determining employer size
- Streamlined job duties test
- Automatic mechanism for updates
With the implementation of these changes, the U.S. Department of Labor (DOL) estimates that an additional 1.2 – 1.3 million American workers will become eligible for overtime pay. At the state level, the Washington Department of Labor & Industries (L&I) estimates that an additional 40,000 employees will become eligible for overtime in 2020. By the time the scheduled salary threshold increases go into effect in 2028, L&I estimates the total of workers impacted to be more than 250,000.

### Federal Changes in Overtime Exemption Requirements

**Increased Salary Threshold Requirement**

Effective January 1, 2020, the DOL increased the federal salary threshold for exempt employees from $455 per week, or $23,660 per year to $684 per week, or $35,568 per year for full-year employees. This is the first increase to the salary threshold since 2004.

Exempt employees must earn at least the new salary threshold (or the equivalent fee basis), even if they are paid a fixed salary and perform exempt duties.

**What May Be Included in Salary**

For purposes of meeting the new federal salary threshold, the federal rules now permit employers to include nondiscretionary bonuses and incentive payments, such as commissions, in the total calculation of an employee’s salary. To be included, these payments must be paid at least annually and may account for up to 10% of an employee’s salary for determining whether the salary threshold test is satisfied.

Employees must therefore be paid at least $32,012 in wages per year before including other compensation. The remaining salary, up to $3,557, may be made of nondiscretionary bonuses and incentive payments.

**Annual Catch-Up Payment**

The new federal rule permits employers to make a final “catch-up” payment within one pay period after the end of the year (or other 52-week period) to bring an otherwise exempt employee’s compensation to the required level. If an employer chooses this option, the employer must pay the employee at least 90% of the minimum salary threshold ($615.60 per week) on a regular basis. Then, if at the end of the year, the employee’s paid-out salary plus nondiscretionary bonuses and incentive payments (including commissions) does not equal at least $35,568, the employer has one pay period to make up for the shortfall.

Because employers may set their own pay periods, this length of time may vary by business and could mean that some employers have one month to make this catch-up payment, while other employers only have one week to make this catch-up payment.
No Automatic Mechanism for Updates

Despite efforts during the rulemaking process, the DOL did not adopt any formal mechanism for automatically increasing the salary threshold for overtime exemption. Any future increases to the federal salary threshold will be subject to the same notice-and-comment rulemaking process the DOL followed in passing the 2020 update and will reflect the economic conditions at that time.

Washington Changes in Overtime Exemption Requirements

While the DOL finalized the new federal rules for overtime exemption, the Washington Department of Labor & Industries (L&I) also updated its overtime exemption rules so that the new state rules better align with the updated federal regulations. Just as before, when federal and state laws differ, the law that provides the greater benefit to employees will apply.

Increased Salary Threshold Requirement

Beginning on July 1, 2020, the minimum salary threshold for exempt employees in Washington will be $675 per week, or $35,100 per year. Because this new state salary threshold will continue to be lower than the new federal threshold, Washington employers must use the federal threshold for 2020. In 2021, the state threshold will exceed the federal threshold and at that time Washington employers will need to meet or exceed the state threshold for employees classified as exempt.

L&I did not make changes to what may be included in salary threshold calculations, so an employee’s salary for purposes of the overtime exemption may only consist of regular, ongoing payments of salary and/or wages, and may not include bonuses, commissions, or other types of compensation.

Computer Professionals

Exempt computer professionals are subject to their own compensation thresholds if they are paid on an hourly basis instead of a fixed salary. As with the state salary thresholds, these rates will increase incrementally through 2022.

<table>
<thead>
<tr>
<th>EMPLOYER SIZE:</th>
<th>1-50 Employees</th>
<th>51+ Employees</th>
</tr>
</thead>
<tbody>
<tr>
<td>Effective Date</td>
<td>Est. Salary Threshold</td>
<td>Est. Salary Threshold</td>
</tr>
<tr>
<td>Jul. 1, 2020</td>
<td>$27.63 per hour</td>
<td>2.75 times minimum wage</td>
</tr>
<tr>
<td>January 1, 2021</td>
<td>2.75 times minimum wage</td>
<td>3.5 times minimum wage</td>
</tr>
<tr>
<td>January 1, 2022</td>
<td>3.5 times minimum wage</td>
<td>3.5 times minimum wage</td>
</tr>
</tbody>
</table>

Teachers

The salary threshold continues not to apply to teachers, professionals, instructors, and lecturers in educational establishments, although they must be paid on a salary or fee basis.
Outside Salespersons
The new salary thresholds also do not apply to outside salespersons, who still must be paid on a salary, commission, or fee basis.

Methods for Determining Employer Size
Washington employers may choose between two methods of determining their size for purposes of the overtime exemption:

- Count the number of employees the employer has in Washington (full-time and part-time) at each effective year of the new overtime thresholds (i.e., count employees on July 1, 2020, January 1, 2021, and so on); or
- Follow the formula provided by the Employment Security Department for paid family and medical leave (i.e., the average number of employees reported by the employer over the last four completed calendar quarters).

Employers should use utilize the method that is most consistent with their business practices.

Streamlined Job Duties Test
Washington’s new rules also eliminated the state’s previous “long” and “short” job duties tests and replaced them with a standard test that more closely aligns with the federal rules. In addition, the exempt duties for computer professionals have been simplified and refined and the definition of outside salespersons has been clarified and made more consistent with the DOL’s definition. The new state job duties tests are described above under the descriptions for each exemption.

Automatic Mechanism for Updates
To determine future salary thresholds under the new state rules, L&I will phase in a state minimum wage multiplier that will increase each year until 2028. By using a minimum wage multiplier, in addition to the annual adjustments to the minimum wage, the state will be able to more predictably calculate the salary threshold for exempt employees and make annual adjustments to keep pace with cost of living adjustments for Washington workers.

Beginning on July 1, 2020, Washington’s salary threshold for exempt employees will be calculated by multiplying the new state minimum wage by 1.25, setting the new state salary threshold at $675 per week, or $35,100 per year. This standard will be applicable to all Washington businesses, regardless of their size. Because this threshold continues to be lower than the new federal standard of $684 per week, or $31,568 per year, Washington employers must use the federal threshold in 2020.

On January 1, 2021, the new salary threshold will be phased in at different multiplier rates based on employer size. This variation accounts for the greater implementation burden for Washington’s small businesses. In 2021, exempt employees who work for businesses with 50 or fewer employees will need to earn at least 1.5 times the state minimum wage to be exempt from overtime. Employees for large employers (with more than 50 employees) will need to earn at least 1.75 times the state minimum wage to be exempt from overtime.
The state salary thresholds will continue to increase by different multiplier rates each year until 2028. Following the last multiplier increase in 2027, the multiplier will be held constant at 2.5 times the minimum wage for all employers, regardless of size, and will only increase with adjustments to the minimum wage. The following timeline outlines the incremental changes in the salary threshold from 2020 to 2028. These estimates are based on current projections, and may change as a result of inflation and future minimum wage adjustments.

### Washington Salary Threshold Implementation Schedule

<table>
<thead>
<tr>
<th>EMPLOYER SIZE:</th>
<th>1-50 Employees</th>
<th>51+ Employees</th>
</tr>
</thead>
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<tr>
<td><strong>Effective Date</strong></td>
<td><strong>Minimum Wage Multiplier</strong></td>
<td><strong>Est. Salary Threshold</strong></td>
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<tr>
<td>Jul. 1, 2020</td>
<td>x 1.25</td>
<td>$675 / week $35,100 / year</td>
</tr>
<tr>
<td>Jan. 1, 2021</td>
<td>x 1.5</td>
<td>$827 / week $43,004 / year</td>
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<tr>
<td>Jan. 1, 2022</td>
<td>x 1.75</td>
<td>$986 / week $51,272 / year</td>
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<tr>
<td>Jan. 1, 2023</td>
<td>x 1.75</td>
<td>$1,008 / week $52,416 / year</td>
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<tr>
<td>Jan. 1, 2024</td>
<td>x 2.0</td>
<td>$1,177 / week $61,204 / year</td>
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<tr>
<td>Jan. 1, 2025</td>
<td>x 2.0</td>
<td>$1,202 / week $62,504 / year</td>
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<tr>
<td>Jan. 1, 2026</td>
<td>x 2.25</td>
<td>$1,382 / week $71,864 / year</td>
</tr>
</tbody>
</table>


Note: Multipliers and estimated salary thresholds listed here do not apply to hourly computer professionals.
COMPLYING WITH OVERTIME RULE CHANGES

L&I will be conducting extensive outreach and implementing an education program to assist employers with these changes. The efforts will include explanations of the new standards, clarification on the differences between state and federal rules changes, and updates to relevant administrative policies. L&I will provide presentations and webinars, implementation guides, and an eLearning module, among other outreach methods, for all Washington employers.

To further support employers with compliance, L&I has provided examples of means by which employers may make changes to account for the new requirements:

Reclassify Exempt Employees
Employers may change current salaried, exempt employees to salaried, non-exempt or hourly non-exempt employees. As the employees who are subject to this approach would then be considered non-exempt, this option entitles them to overtime pay for any work over 40 hours in a workweek in addition to other protections afforded by Washington law.

Employers should be aware that reclassifying formerly exempt employees may mean that the reclassified employees may be entitled to additional employee benefits or protections, including paid sick leave under Washington law (Seattle- and Tacoma-based employees are already entitled to paid sick leave regardless of exempt status, so reclassification will have less impact on employers with employees in those cities), meal and rest breaks, and timekeeping requirements.

Limit Work Hours for Non-Exempt Employees
If employers convert current salaried, exempt employees to salaried, non-exempt or hourly non-exempt employees, they may also want to consider limiting employee workweek hours to reduce overtime costs. This limit may be set at 40 hours per week, or less, depending on business needs.

Maintain Exempt Status
For employers who want to maintain employees’ exempt status, they must ensure each employee meets the appropriate duties test requirements and the salary threshold requirements in effect at that time.