

The Department of Labor ruling on the Fair Labor Standards Act

WHAT IS THE NEW RULE?

The Department of Labor's (DOL) final overtime rule updates the salary level required for the executive, administrative and professional ("white collar") exemption to ensure that the Fair Labor Standards Act (FLSA) intended overtime protections are fully implemented. It provides greater clarity for white collar workers and their employers, including non-profit organizations, like churches.

The final rule updates the salary threshold under which most white collar workers are entitled to overtime.

The new salary threshold increases to \$913 per week or \$47,476 annually effective December 1, 2016.

What is the FLSA?

The FLSA is a federal law that governs minimum wage and overtime pay. Unless an exemption to the FLSA applies, employers must comply with the law by:

- Pay at least the federal minimum wage or state minimum wage, if higher. Currently, North Carolina's minimum wage is \$7.25 per hour, the same as the federal minimum.
- Pay overtime after someone physically works 40 hours in one week.
- Pay overtime at a rate of at least one and one-half times an employee's regular rate.

What are the key provisions of this final ruling?

The Final Rule focuses primarily on updating the salary and compensation levels needed for Executive, Administrative and Professional workers to be exempt. Specifically, the Final Rule:

Sets the standard salary level at the 40th percentile of earnings of full-time salaried workers in the lowest-wage Census Region, currently the South (\$913 per week; \$47,476 annually for a full-year worker);

Sets the total annual compensation requirement for highly compensated employees (HCE) subject to a minimal duties test to the annual equivalent of the 90th percentile of full-time salaried workers nationally (\$134,004); and

Establishes a mechanism for automatically updating the salary and compensation levels every three years to maintain the levels at the above percentiles and to ensure that they continue to provide useful and effective tests for exemption.

Additionally, the Final Rule amends the salary basis test to allow employers to use nondiscretionary bonuses and incentive payments (including commissions) to satisfy up to 10 percent of the new standard salary level.

The effective date of the final rule is December 1, 2016. The initial increases to the standard salary level (from \$455 to \$913 per week) and HCE total annual compensation requirement (from \$100,000 to \$134,004 per year) will be effective on that date. Future automatic updates to those thresholds will occur every three years, beginning on January 1, 2020.

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WHAT DOES THE NEW FLSA LAW MEAN FOR CHURCHES?

Are churches covered by the FLSA?

This act contains no blanket exemptions for the non-profit sector, including religious employers or their employees. There are factors to consider in determining if an employee is covered by the FLSA's minimum wage and overtime protection. An employee is covered by the FLSA if they meet **one** of the following three criteria:

- The commerce or enterprise requirement: the employee is either employed by an "enterprise" engaged in commerce which generates income of at least \$500,000 annually or the employee alone is physically engaged directly in commerce through interstate transactions (ordering supplies from out of state, routinely sending emails out of state).
- The nonexempt requirement: the employee does not meet the duties test definition of an "exempt" white collar employee.
- The ministerial exception: the employee is not being compensated for services performed in the exercise of ministry.

Does the FLSA ruling apply to all businesses?

The FLSA ruling oversees two types of coverage: Enterprise and Individual.

Generally speaking, non-profit organizations are not covered by the FLSA unless they're considered an enterprise. While some churches or their employees may not be covered by the FLSA, many ministries will be covered by the FLSA under either the Enterprise test or Individual test.

It's critical that your ministry is classifying your employees accurately as either exempt or nonexempt, based on their primary job functions. Job classifications determine exempt or nonexempt status.

Job titles are insufficient for determining classification for exempt and nonexempt status.

What is Enterprise coverage?

An enterprise is an organization that engages in ordinary commercial activities that result in an annual revenue from sales or profits in excess of \$500,000. Ordinary commercial activities would be operating a thrift shop or a book store. Enterprise activities are those conducted solely for a business purpose.

What is **not** included in this enterprise income threshold are tithes, donations and special offerings.

If a nonprofit meets the \$500,000 annual income threshold, its employees (*excluding clergy*) are covered by the FLSA and entitled to overtime for work performed over 40 hours per week.

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My church is not an enterprise business. Does this mean my employees aren't covered by the new FLSA law?

Even if your church is not an enterprise, you may have some employees who are still covered by the FLSA ruling under Individual coverage and would be entitled to FLSA protections.

What is Individual coverage?

Individual coverage is based on the nature of each individual employee's work activities. According to FLSA guidelines, if the employee is engaged in "interstate commerce" on a "regular and recurrent basis", they are covered by the FLSA.

What is interstate commerce?

Interstate commerce is broadly defined to include making interstate telephone calls, sending interstate mail or email and ordering, receiving or shipping goods across state lines. An example would be an employee who orders supplies from another state.

There is no clear definition as to what constitutes a "regular and recurrent basis".

Does this new ruling affect hourly employees?

There is no change to an hourly employee's pay or time tracking. Hourly employees are always nonexempt and eligible for overtime.

What is the difference between exempt and nonexempt?

These are job classifications: all positions are classified as either "**Exempt**" or "**Nonexempt**."

Classifications should be clearly stated in each job description and must be accurate to ensure paying an employee fairly.

Exempt employees are not eligible for overtime; nonexempt employees are eligible for overtime.

Is "exempt" the same as "salaried"?

No. Salary is a pay basis. Exempt is a job classification.

How do we decide between exempt vs. nonexempt and hourly vs. salary?

An employee can meet the job classification (primary duties) test but not pass the salary level test (\$913 per week). Or they may pass the salary level test but not meet the primary job duties test.

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Three (3) tests must be met in order for an employee to be considered Salaried - Exempt:

- **Salary Basis** Test: This is how you pay your employee – hourly or salary. An exempt employee is paid a set guaranteed salary per pay period in any week the employee performs work, regardless of the quality or quantity. It limits the types of deductions that may be made to this salary. Hourly employees are paid by their hours worked in any work week.
- **Salary Level** Test: This is the new FLSA rule effective December 1, 2016 and requires an employee to be paid a guaranteed minimum of \$913 per week. This new salary level will be automatically adjusted by the DOL every three (3) years.
- **Job Classification** or Primary Duties Test: An exempt employee must perform executive, administrative, professional or creative professional job duties in their core functions and responsibilities. (*explained below*)

All three tests must be met in order to classify an employee as Salaried Exempt. If not, an employee will be considered Salaried Nonexempt and eligible for overtime or Hourly Nonexempt and eligible for overtime.

NOTE: When in doubt, classify your employee as nonexempt.

What are job classifications?

Job classifications are based on position duties and position duties must meet the U.S. Department of Labor tests (outlined below) to be classified as “exempt.”

Salary Exempt

Exempt employees do not receive overtime pay. To qualify for exemption, **all** of the following tests in any one specific job classification must be met:

Executive Exemption: The employee must be compensated on a **salary basis** at a rate not less than \$913 per week. The employee’s **primary duty** must be **managing** a customarily **recognized department or subdivision** of the enterprise. The employee must **customarily and regularly** direct the work of at least **two or more** full-time employees or their equivalent. The employee must have the authority to hire or fire other employees, or the employee’s suggestions and recommendations as to the hiring, firing, advancement, promotion, or any other change of status of other employees must be given **particular weight**.

Administrative Exemption: The employee must be compensated on a **salary or fee basis** at a rate not less than \$913 per week. The employee’s **primary duty** must be the performance of office or non-manual work directly related to the **management or general business operations** of the employer or **employer’s customers**. The employee’s **primary duty** includes the exercise of **discretion and independent judgment** with respect to matters of significance.

Professional Exemption: The employee must be compensated on a **salary or fee basis** at a rate not less than \$913 per week. The employee’s primary duty must be the performance of work requiring **advanced knowledge** defined as work that is predominately intellectual in character and that includes work requiring the consistent exercise of discretion and judgment. The advanced knowledge must be in a **field of science or learning**. The advanced knowledge must be **customarily** acquired by a **prolonged course of specialized intellectual instruction**.

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Teachers' Exemption: Teachers are exempt from overtime if their primary duty is teaching, tutoring, instructing, or lecturing in the activity of imparting knowledge, and if they are employed and engaged in this activity as a teacher in an educational establishment. Exempt teachers include academic teachers, kindergarten or nursery school teachers and music teachers. The salary and salary basis requirements of earning \$913 per week do not apply to bona fide teachers.

Creative Professional Exemption: To qualify for the creative professional employee exemption the employee must be compensated on a salary or fee basis at a rate not less than \$913 per week and their primary duty must be the performance of work requiring invention, imagination, originality or talent in a recognized field of artistic or creative endeavor.

Exemption as a creative professional depends on the extent of the invention, imagination, originality or talent exercised by the employee. Whether the exemption applies, therefore, must be determined on a case-by-case basis. The requirements are generally met by actors, musicians, composers, soloists, writers, novelists, and others as set forth in the regulations.

Is everyone who earns less than \$913 per week an hourly employee?

No, not all employees who earn less than \$913 per week must be "hourly". An employee may be paid on a salary basis and still qualify for overtime. They would be classified as **salaried nonexempt**.

NOTE: Salaried nonexempt employee hours must be tracked by a timekeeping method to calculate all hours worked including any overtime pay for over 40 hours in a work week. Overtime is calculated on actual hours worked over 40 in a weekly pay period - not including holidays or vacation days.

What is a Salaried Nonexempt employee?

Salaried nonexempt employees will be paid overtime for all hours worked in excess of 40 in a work week.

Salaried nonexempt employees are expected to work a normal workday and workweek, unless their manager authorizes overtime **in advance** and will either pay the employee overtime or arrange for time off within the same week that the overtime would be earned.

Salaried nonexempt employees must maintain a true, accurate record of hours worked and are covered by the FLSA.

How do we manage employee overtime?

The most common way to manage your budget is to know the schedule your employees are working.

"Comp" time is not legal but if you have employees who will exceed their 40 hours in a work week, you may be able to offer flex time in lieu of overtime pay **in that same work week** if scheduling permits. If flexible scheduling isn't an option, the employee must be paid overtime.

It will be important for managers to be aware of their employees' pending schedules and projects. Ideally, an employee should only work overtime when a supervisor has authorized it.

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Isn't there a "ministerial exception"?

The courts have created a "ministerial exception" that exempts "clergy" from federal wage and hour laws. This exception is straightforward when applied to traditional clergy positions. It is intended to apply to pastors, ministers, religious students and other employees who are ordained or who function in a similar religious capacity. This can become confusing when applying to positions not traditionally known as – or clearly associated with – clergy.

How do we know who's covered by the "ministerial exception"?

Because this exception generated from the courts, different courts have used different criteria in evaluating who might be considered a minister for the purpose of this exception. Below are a sampling of what courts across multiple state jurisdictions have used as evaluators:

- Did the religious institution (church/school) make its decision to hire a particular individual for a particular position based "largely on religious criteria"?
- Is the individual authorized to perform ceremonies of the church?
- Does the ministry (church/school) publicly consider this person a member of the clergy?
- Does the individual engage in ecclesiastical or religious activities and attend to the religious needs of the faithful as part of their primary job function?
- Did the individual complete a formal process such as ordination, licensure or certification or obtain a divinity degree in order to perform the position's duties?
- **Be clear about whom you consider to be a minister under this exemption and why:**
 - Is their job description clear?
 - Do their primary duties as stated in the job description reflect their ministerial role?
 - Does the employee meet the minimum requirements for their role, particularly as they relate to religious responsibilities and functions?
 - Is the exempt/nonexempt job classification status clearly written in their job description?
 - Are your church mission and all job-related responsibilities detailed in the job description?
 - Does your employee know and understand your performance expectations as they relate to the church's beliefs, mission and core values?
 - Have they agreed to and signed their job description?

NOTE: For a role to be ministerial in nature, the primary functions must be in promoting the faith through spiritual and pastoral duties and both you and your employee consider and recognize their position to be ministerial. Courts decide on ministerial exemptions on a case-by-case basis.

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Are Youth Pastors and Directors of Children's Ministries exempt?

According to case law, if the primary job duties are to promote the faith and, in varying capacities, supervise and lead worship services, then the employee may be exempt from the FLSA. The primary duties must be ministerial in nature and stated in the individual's job description. (example: They are exempt if they are responsible for creating a curriculum designed to lead the children to a greater appreciation and understanding of the faith; leading children's worship services; creating or leading Bible discussions or conversations about the Christian faith and the furtherance of the Church's mission and vision. The job description should contain this language in the job summary and the specifics should be detailed as the primary responsibilities).

Are teachers exempt from the FLSA?

Yes, there is an exemption to the FLSA for teachers. The salary level and salary basis tests do not apply to bona fide teachers. A bona fide teacher has a **primary** duty of teaching, tutoring, instructing or lecturing in the activity of imparting knowledge and is employed and engaged in this activity as a teacher in an educational establishment.

Does this include preschools?

Yes, preschools and kindergartens are exempt from FLSA when the teacher's primary duty is **teaching and not caring for the physical needs of children.**

Are school administrators covered by FLSA?

School administrators and directors are exempt from the FLSA provided they earn at least the minimum starting salary for a bona fide teacher in their school.

The teacher's exemption also includes administrative personnel that help run educational institutions and interact with students outside the classroom, such as department heads and academic advisors.

Office administrators and other clerical and support staff are covered by the FLSA. However, if they meet the three tests for the Administrative exemption: salary basis, salary level (\$913 per week) and job classification, they may be considered exempt from the FLSA.

What about daycare staff?

There is no exemption for daycare workers. Daycare workers are covered by the FLSA and should be nonexempt employees and eligible for overtime.

Is a choir director exempt from FLSA?

Choir Directors may be covered by the Creative Professional exemption if they meet the three tests for the Creative Professional exemption: salary basis, salary level (\$913 per week) and job classification.

However, if the Choir Director does not meet the three criteria above, they may be covered by the "ministerial exemption" which, please remember, is applied by the courts case-by-case.

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If the ministry depends on the Choir Director to promote the faith through the planning and oversight of the church's music program, choir and services and that oversight is directly tied to the church's mission, they may be considered a liturgical lay minister under the law and not subject to the FLSA.

However, if the individual is called a Choir Director and their primary function is solely to accompany musically the choir or congregation during services, they would not be exempt and would be covered by the FLSA and subject to overtime.

May we just make our Choir Director a contractor?

No. The IRS ruled recently that musicians who are paid to perform at weekly services are considered employees of the church and are not independent contractors. If you tell the musician when, where and/or how to play, they are not independent contractors. They are your employees and are covered by the FLSA.

HOW DO WE COMPLY?

KNOW THE RULES

Do we need job descriptions on everyone?

Yes. Each person on staff – regardless of position – should have a job description. This is not simply to comply with FLSA. This is considered best practice in all industries to ensure effective and satisfactory performance management.

Your job descriptions should include a brief summary of the primary functions of the role and should include the core responsibilities of the positions. This is especially critical when you're justifying a role for "ministerial exemption".

The ministerial duties must be specifically outlined in the job description and core duties. Each employee should sign their job description.

A job title alone is never used to determine job status, salary or classification.

What counts as work?

All time that employees spend doing job-related activities counts as work time, whether the employee is "on the clock" or not. This includes working from home and work performed outside regular working hours, even if the manager hasn't approved this work. (example: for nonexempt employees, checking emails after-hours is compensable work time.)

May we offer flex time?

You can't give a nonexempt employee future "comp" time instead of overtime pay but you can adjust schedules within a work week to ensure your employee isn't physically working more than 40 hours in one week. (example: your assistant works a 10 hour day instead of a regularly scheduled 8. You may adjust your assistant's schedule **within that same work week** by allowing them to leave 2 hours early or arriving 2 hours late.)

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Is an employee allowed to work “off the clock”?

No. A nonexempt employee must account for all hours worked and must be paid accordingly. If they work over 40 hours in one pay period, they are eligible for overtime or flex time in that same work week. They are not permitted to work off the clock.

May we adjust schedules over pay periods?

No. Adjusting schedules to accommodate flex time may only be done within the same pay week as the overtime would have been earned.

May we average an employee’s hours over multiple weeks?

No. The DOL does not permit employers to average work time over multiple weeks to avoid paying overtime. Overtime must be paid – Flexible hours may be offered or overtime must be paid to any nonexempt employee who works more than 40 hours in a single pay week.

Is an employee allowed to “volunteer” their time instead of earning overtime?

A nonexempt employee is not permitted to volunteer their time to perform the same or similar functions for which they are paid. (example: an accounting clerk handles cash as part of their job duties; they want to volunteer to collect cash at a book sale. This is not permissible because the clerk would be volunteering the same type of service for which they’re normally paid. However, the accounting clerk could volunteer to unpack books, create or distribute flyers or welcome visitors.)

How do we handle Mission trips?

Overtime rules apply to nonexempt staff unless the employee is working outside the US for the full and regular 7 day work week. FLSA employment laws do not apply outside the US.

Do we pay for travel time?

Ordinary travel to and from the regular work site (office, church) is not considered paid work time.

Travel time conducted during regular work hours is considered paid work time.

Time spent working while traveling is considered paid work time

Traveling on the weekends is considered paid work time when it occurs during hours the employee would normally work. (example: the employee normally works 9-5 Monday through Friday. Travel occurs on Saturday between 11-5. The employee is paid for 6 hours because travel is occurring during what would be routine hours of a work day.)

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May we change the days of the work week?

Your work week should be established and clearly known to all employees. You cannot change it from week to week to avoid paying overtime. Your policies should state the work week in your handbook.

You can decide when your work week will begin and end – it can begin on a Sunday and end on a Saturday; it can begin on a Wednesday and end on a Tuesday. Your timekeeping records should reflect your work week and your pay records should reflect your pay period.

Be sure that your employees are informed of the pay week as well as your pay cycle (how often you pay).

Do we need to keep records?

Yes. For all staff, you should have records that contain each employee's:

- Personal information including full name, Social Security number, home address, job title, gender (for equal pay compliance), birth date (if younger than 19) and workplace ID (could be name or number but should be unique to that particular employee)
- I9 information
- W2 withholding information
- Signed job descriptions
- Time of day and day of week when work week begins (example: 12:00 am Sunday)
- Total wages paid for each pay period
- All additions and deductions to the employee's pay (paid leave hours, insurance premiums)
- Date of payment

For all nonexempt staff, both salaried and hourly, **in addition to the above**, you must keep accurate timekeeping records:

- The total hours worked each day
- The basis on which those wages are paid (example: \$9 per hour or \$400 per week)
- The hourly rate and the overtime rate (even for salaried nonexempt staff)
- Total daily or weekly straight-time earnings
- Total overtime earnings for the work week

The timekeeping doesn't have to be a complicated or sophisticated system; it does require the employee to track their hours worked and submit those hours for payment. This can be done electronically, on a paper timesheet or even via email.

It's important that the employee account for their hours on a daily basis and generate their request for time approval and payment. (If you have an employee who is working unauthorized overtime, you're obligated to pay them for that overtime but would want to initiate a performance conversation around that.)

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While some records may be retained for a shorter time, a good rule of thumb is to keep these records for three years.

Is there a grace period before complying with the new FLSA?

There is no grace period for churches. The effective date is the same for all businesses, even non-profits: December 1, 2016.

What are the penalties for non-compliance?

All employers – even churches – who fail to comply with the FLSA ruling could face extremely harsh penalties. These include paying overtime wages that would have been earned for the past 3 years – even before the new ruling became effective. If the courts felt that the noncompliance was intentional, add another \$10,000 for each employee violation. Because wage and hour claims (FLSA) are excluded from insurance coverage, your ministry might also be liable for legal expenses incurred.

To ensure compliance, remember the following:

Make sure your hiring policies reflect the religious capacities and duties of the job in your job descriptions, job postings (ads), employee handbooks and performance reviews.

The organization's (church, school or office) religious beliefs and expectations should be clearly known if they are connected with a particular job function.

For ministerial exceptions, remember that whether an employee is considered a minister is based on job description and job function.

Case law is dependent on fact. Have all your facts outlined for clear explanation (signed handbook acknowledgement, signed job description).

Sources and resources:

Richard Hammer, *Christianity Today*

www.brotherhoodmutual.com

www.dol.gov

<https://www.dol.gov/whd/overtime/final2016/index.htm>

www.shrm.org

www.wnccumc.org