



## **The Danger of Making the Wrong Overtime Classification Decision**

---

The Risk of Misclassifying a  
Non-exempt Employee as Exempt

Compliance **HR**  
Simplifying the Complexity of Employment Law

# Table of Contents

<b>Introduction</b> .....	<b>01</b>
<b>The Fair Labor Standards Act (FLSA)</b> .....	<b>01</b>
<b>What is an Exempt Employee?</b> .....	<b>02</b>
<b>What is a Non-Exempt Employee?</b> .....	<b>02</b>
<b>Common Exemptions to the Overtime Rule</b> .....	<b>03</b>
The amount the employee is paid.....	03
The method of payment.....	03
The duties performed by the employee.....	04
<b>The Most Common Exemptions.</b> .....	<b>04</b>
Executive Exemption.....	05
Administrative Exemptions.....	05
Professional Exemption .....	06
Computer Employee Exemption .....	07
Outside Sales Exemption.....	07
Highly Compensated Employees .....	08
<b>Examples of Workers Who Generally Do Not Qualify.....</b>	<b>08</b>
<b>Other Wage and Hour Laws</b> .....	<b>09</b>
<b>Why is Compliance Important for Employers?</b> .....	<b>09</b>
<b>Misclassification Risks</b> .....	<b>10</b>
<b>Tips for Employers</b> .....	<b>10</b>
<b>Conclusion</b> .....	<b>12</b>
<b>Appendix: ComplianceHR Navigator OT</b> .....	<b>13</b>



# The Danger of Making the Wrong Overtime Classification Decision

## Introduction

Almost every seasoned human resources and employment law professional is familiar with the significant financial and operational risk employers face when determining overtime status. In general, federal and state laws are designed to protect the employees. Further, regulatory agencies with jurisdiction over worker rights look to the employer to defend the ways in which they have classified their positions.

In this ComplianceHR whitepaper, we will explore the issue of misclassifying a non-exempt employee as exempt from overtime, highlight the risks of getting it wrong, and share some practical guidance for employers.

**The bottom line for employers:** It is vital to classify your employees correctly or risk costly compliance violations.

## The Fair Labor Standards Act (FLSA)

The tests used to determine whether a worker is an exempt or non-exempt employee are found within the Fair Labor Standards Act (commonly referred to as the FLSA) and its accompanying regulations. The FLSA was first passed by Congress in 1938 under the Roosevelt administration with the intent of banning oppressive child labor, and establishing a minimum wage and maximum weekly hours for workers. At the time, it was very controversial, and when passed, it was viewed as revolutionary.

The FLSA applies to most private and public employees and sets the federal minimum wage, overtime, recordkeeping, and youth employment standards. More than 143 million U.S. workers are protected (or “covered”) by the FLSA, which is enforced by the Wage and Hour Division of the U.S. Department of Labor (DOL).

The FLSA generally requires employers to pay all covered non-exempt employees the statutory minimum wage and overtime pay (“time and one-half”) for hours worked in excess of 40 hours in a workweek (with some exceptions for some industries).

## What is an Exempt Employee?

**Exempt employees are paid by their employer not for the hours that they work, but because they are performing tasks related to a special type of skill, are supervisors or managers, or perform administrative tasks.**

The term “exempt employee” is used to describe an employee who is not entitled to, or “exempt”, from overtime and minimum wage provisions of the law. The reason the exemptions exist is because exempt employees are paid by their employer not for the hours that they work, but because they are performing tasks related to a special type of skill, are supervisors or managers, or perform administrative tasks for their employer. Conversely, non-exempt employees are paid for the hours in the day they spend performing the job.

There are many different exemption types that can be found in federal and state law. The most common require that exempt employees be paid in a particular manner, which is typically, but not for all exemptions, by a salary or fee basis. There are also different requirements under each exemption type that concern the job duties that employees perform in the position. The most common exemption types include employees that work in an administrative, professional, executive, computer, or outside sales role. Employers are not required to pay overtime to employees who are properly classified as exempt.

## What is a Non-Exempt Employee?

**Non-exempt employees are entitled to minimum wage and overtime pay when they work more than 40 hours per week.**

The term “non-exempt employee” is used to describe an employee who is entitled to, or “non-exempt”, from overtime and minimum wage provisions of the law. Non-exempt employees are usually paid an hourly wage or may earn a salary that’s less than a minimum amount determined by the DOL. If employees are non-exempt, it means they are entitled to minimum wage and overtime pay when they work more than 40 hours per week.

# Common Exemptions to the Overtime Rule

Overtime exemptions are complicated and can often trip up employers, so it is very important that employers are informed and make proper FLSA classification decisions for their workers.

To classify an employee as exempt from overtime, many of the most common exemptions require employers to apply a similar three-pronged test that includes looking at (1) the amount the employee is paid, (2) the method of payment, and (3) the duties performed by the employee. Any worker who doesn't meet the criteria required by the exemption cannot be considered exempt.

## The amount the employee is paid

As of the publication date of this whitepaper (October 2023) the current federal salary threshold for most of the FLSA's white-collar exemptions is currently set at \$684 per week (\$35,568 annualized) exclusive of board, lodging, or other facilities. Employers may use 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. It is important to note that employers must also comply with any federal, state, and local laws that go beyond the FLSA (for example by setting a higher minimum salary threshold or lower maximum workweek) and with any obligations under collective-bargaining agreements.

Some of the white collar exemptions have a higher threshold (e.g. Highly Compensated). Still others do not have any salary requirement at all (e.g. Outside Sales).

## The method of payment

Being paid on a "salary basis" is the most common method of payment for exempt employees. It means an employee regularly receives a predetermined amount of compensation each pay period on a weekly, or less frequent, basis. The predetermined amount cannot be reduced because of variations in the quality or quantity of the employee's work. Besides salary, other forms of payment that you see that could work for certain exemptions include fee basis (e.g. Professional, Administrative) and even hourly (e.g. Computer Professionals).

## The duties performed by the employee

Primary duties testing that is specific to each exemption (the most common exemptions are outlined in the next section), as follows:

Each exemption comes with a specific primary duties test that must be met in order for the exemption to apply. Job titles and “white-collar” status do not determine an employee’s exempt status. In order for an exemption to apply, an employee’s specific job duties must meet all the requirements of the DOL’s regulations.

An employee’s primary duty is the principal, main, or most important duty the employee performs. The primary duties test is an employee-specific, case-by-case inquiry with the major emphasis on the character of the employee’s job as a whole. In addition, the position’s primary duty, certain exemptions have additional duties that must be performed in order to qualify, and sometimes the employee’s level of independence and discretion comes into play.

## The Most Common Exemptions

There are a few common exemptions, including those for: executive employees, administrative employees, professional employees, computer employees, outside-sale employees, and highly compensated employees.

Each of these exemptions has its own specific criteria. Following is an overview of the major requirements for these most common exemptions:

**Note:** This information on exemptions is current as of the publication date of this whitepaper (October 2023). However, readers are always encouraged to check the [US Department of Labor’s Wages and the Fair Labor Standards Act](#) website for any updates to the criteria.

## Executive Exemption

To qualify for the executive employee exemption, all of the following factors must be met:

- The employee must be compensated on a salary basis (as defined in the regulations) at a rate not less than \$684 per week;
- The employee's primary duty must be managing the enterprise, or 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 other full-time employees or their equivalent; and
- 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 Exemptions

To qualify for the administrative employee exemption, all of the following factors must be met:

- The employee must be compensated on a salary or fee basis (as defined in the regulations) at a rate not less than \$684 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 the employer's customers; and
- The employee's primary duty includes the exercise of discretion and independent judgment with respect to matters of significance.

## Professional Exemption

To qualify for the **learned professional** employee exemption, all of the following factors must be met:

- The employee must be compensated on a salary or fee basis (as defined in the regulations) at a rate not less than \$684 per week;
- The employee's primary duty must be the performance of work requiring advanced knowledge, defined as work which is predominantly intellectual in character and which includes work requiring the consistent exercise of discretion and judgment;
- The advanced knowledge must be in a field of science or learning; and
- The advanced knowledge must be customarily acquired by a prolonged course of specialized intellectual instruction.

To qualify for the **creative professional** employee exemption, all of the following factors must be met:

- The employee must be compensated on a salary or fee basis (as defined in the regulations) at a rate not less than \$684 per week;
- The employee's primary duty must be the performance of work requiring invention, imagination, originality or talent in a recognized field of artistic or creative endeavor.



## Computer Employee Exemption

To qualify for the computer employee exemption, the following factors must be met:

- The employee must be compensated **either** on a salary or fee basis (as defined in the regulations) at a rate not less than \$684 per week **or**, if compensated on an hourly basis, at a rate not less than \$27.63 an hour;
- The employee must be employed as a computer systems analyst, computer programmer, software engineer or other similarly skilled worker in the computer field performing the duties described below;
- The employee's primary duty must consist of:
  1. The application of systems analysis techniques and procedures, including consulting with users, to determine hardware, software or system functional specifications;
  2. The design, development, documentation, analysis, creation, testing or modification of computer systems or programs, including prototypes, based on and related to user or system design specifications;
  3. The design, documentation, testing, creation or modification of computer programs related to machine operating systems; or
  4. A combination of the aforementioned duties, the performance of which requires the same level of skills.

## Outside Sales Exemption

To qualify for the outside sales employee exemption, all of the following factors must be met:

- The employee's primary duty must be making sales (as defined in the FLSA), or obtaining orders or contracts for services or for the use of facilities for which a consideration will be paid by the client or customer; and
- The employee must be customarily and regularly engaged away from the employer's place or places of business.

## Highly Compensated Employees

Highly compensated employees performing office or non-manual work and paid total annual compensation of \$107,432 or more (which must include at least \$684 per week paid on a salary or fee basis) are exempt from the FLSA if they customarily and regularly perform at least one of the duties of an exempt executive, administrative or professional employee identified in the standard tests for exemption.

### Examples of Workers Who Generally Do Not Qualify

Two major categories where large classes of employees do not qualify for overtime exemptions include blue-collar workers and public safety workers:

- **Blue-Collar Workers**

The exemptions provided by FLSA Section 13(a)(1) apply only to “white-collar” employees who meet the salary and duties tests set forth in the Part 541 regulations. The exemptions do not apply to manual laborers or other “blue-collar” workers who primarily perform work involving repetitive operations with their hands, physical skill and energy. FLSA-covered employees in production, maintenance, construction and similar occupations such as carpenters, electricians, mechanics, plumbers, iron workers, craftsmen, operating engineers, and longshoremen are entitled to [minimum wage](#) and [overtime](#) premium pay under the FLSA, and are not exempt under the Part 541 regulations no matter how highly paid they might be. It is possible that an employee performing this work is also designated as a manager or lead and can meet a white-collar exemption if their pay and job duties qualify them. On the flip side, a manager title alone will not exempt them – they must meet the duties test under the Executive exemption. If that are spending most of their time performing the manual work, they are likely non-exempt.

- **Police, Fire Fighters, Paramedics & Other First Responders**

Public safety workers generally do not qualify for exemptions from minimum wage and overtime. Public safety workers include positions such as police officers, detectives, deputy sheriffs, state troopers, highway patrol officers, investigators, inspectors, correctional officers, parole or probation officers, park rangers, fire fighters, paramedics, emergency medical technicians, ambulance personnel, rescue workers, hazardous materials workers and similar employees, regardless of rank or pay level, who perform work such as preventing, controlling or extinguishing fires of any type; rescuing fire, crime or accident victims; preventing or detecting crimes; conducting investigations or inspections for violations of law; performing surveillance; pursuing, restraining and apprehending suspects; detaining or supervising suspected and convicted criminals, including those on probation or parole; interviewing witnesses; interrogating and fingerprinting suspects; preparing investigative reports; or other similar work. However, an analysis of the position’s job duties and pay basis may still be a worthwhile endeavor if there is a chance the work performed by the position could qualify.

## Other Wage and Hour Laws, and Collective Bargaining Agreements

The FLSA governs federal minimum wage, overtime, record-keeping and youth employment for individuals working in both the private and public sectors. Employers should be aware that in addition to the federal FLSA, some state and local jurisdictions have their own wage and hour laws. In these cases, the DOL says that employers must apply the minimum wage or overtime rate that is most favorable to the employee.

In other words, the FLSA provides minimum standards that may be exceeded, but cannot be waived or reduced. Employers must comply, for example, with any Federal, State or municipal laws, regulations or ordinances establishing a higher minimum wage or lower maximum workweek than those established under the FLSA. Similarly, employers may, on their own initiative or under a collective bargaining agreement, provide a higher wage, shorter workweek, or higher overtime premium than provided under the FLSA. While collective bargaining agreements cannot waive or reduce FLSA protections, nothing in the FLSA or the Part 541 regulation relieves employers from their contractual obligations under such bargaining agreements.

## Why is Compliance Important for Employers?

**Just because an employee has the title of manager and is paid by salary, for instance, does not mean they automatically qualify to be an exempt employee.**

Employers should always closely check the exact terms and conditions of an exemption in light of the employee's actual duties before assuming that the exemption might apply to the employee. The burden of supporting the application of an exemption rests entirely on the employer.

If a worker is found to be misclassified, it can lead to significant back pay recovery, fines, and penalties. The penalties can be even more severe if the DOL's Wage and Hour Division finds willful violations.

Wage and hour is not an area of employment law that employers should take lightly, and there is little excuse for being misinformed or less-than-thorough in its application. There are many common traps to avoid. For example, the FLSA does not consider job title or the history of the position being classified as exempt when it comes to compliance. Just because an employee has the title of manager and is paid by salary, for instance, does not mean they automatically qualify to be an exempt employee.

## What are the Risks of Worker Misclassifications?

Misclassification of non-exempt employees is a common issue in the workplace. Employees are often misclassified by mistake, for example, when employers blindly follow historical precedent for a specific role, or simply have a lack of HR knowledge and experience. In other cases, employers may either “inflate” a job title, or intentionally misclassify a worker, in order to avoid paying overtime.

Misclassification can adversely affect businesses in a number of significant ways, often resulting in:

- Civil, or potentially criminal (if done willfully) fines and penalties
- Individual employee lawsuits for unpaid overtime, lost wages, and benefits, and potentially class-action lawsuits if there is a large population of similarly misclassified workers
- Costs to remedy the misclassification, including back pay recovery and attorney fees
- Management distraction, employee distrust, employer-brand damage in the marketplace

Additionally, a claim of misclassification brought against an employer can also result in regulatory enforcement action. This means the DOL (or a state agency) may conduct an audit of all wage and hour practices within the company.

## Tips for Employers

**There are a few important prudent practices for employers to consider when it comes to worker classification and overtime eligibility:**

- **Don't Guess** – It is dangerous to rely on historical precedent for a classification, so please don't guess. If unsure, consult an employment attorney, or use an expert system like ComplianceHR's Navigator OT solution (see appendix).
- **Job Descriptions Matter** – Having a well-written job description is an important artifact for supporting that an employee's job duties meet the requirements for the primary duties test.

Employers should consider an annual review of job descriptions to ensure that the essential duties listed accurately reflect the actual tasks of the position. Employers may find it useful to review the descriptions again when hiring a new employee into the position.

- **Annual Review** – Employers should consider an audit all exempt employees' job duties and basis of pay annually to ensure proper classification under the FLSA. This is particularly important anytime there are changes to the FLSA, or state-specific requirements. As part of the audit, you want to ensure you have proper documentation to justify the exemption status of each role. Multistate employers must also consider all applicable state or local wage and hour laws, which may have additional requirements to ensure compliance with all applicable laws.
- **Don't Base it Solely on Job Title** – It is very dangerous to make a classification decision based only on the job title, you must evaluate the function and the specific job duties being performed. For example, consider a recently promoted "office manager" who has authority to process and approve payroll, but who also still serves as the receptionist and meets the salary requirement for exempt. How should this employee be classified? The answer is likely as non-exempt. This person has little to no decision-making authority as it relates to the business strategy and supervises no employees. If you classify them as exempt, then they get terminated and file a lawsuit, you could owe thousands in back wages.
- **Beware of Role Scope Creep** – We can't overemphasize the importance of reviewing each job duty annually. Why? Because role "scope creep" is very common. What an employee was doing last year may have evolved into something new without a title or salary change, or an update to their job description. For example, a receptionist may have started answering the phone every day during their lunch break. If that's the case, there is now potential exposure for paying overtime.
- **Don't Get Creative with Pay** – Employers may be tempted to find alternative ways to pay extra in order to eliminate need to pay of overtime. This is very dangerous. One common practice is to raise a worker's wage just enough to meet the salary threshold for overtime. An employer may think they are doing the worker a favor, but in reality, if the worker does not meet the duties standard as well, they have only set themselves up for wage and overtime claims using that newly increased wage.

- **Get Educated** – For federal regulations, visit the [Department of Labor](#) and the [IRS](#) websites, as well as the relevant state agencies for your organization. These websites offer extensive guidance and resources for employers, for example, the IRS offers an in-depth review of how to correct the reporting of misclassified employees. You might also consider [ComplianceHR's Reference Center](#), which provides state and local information for a variety of topics, such as final pay, FMLA, minimum wage, predictive scheduling, and workplace posters, among many others.
- **Consult an Attorney** – Lastly, it is always a good idea for employers to consult with legal counsel if they are unsure of how to proceed with an FLSA exemption audit, or if they have a position that they believe may be at risk of misclassification. Once an employer conducts an internal audit, it is sometimes necessary to reclassify an employee to a different status. There may be some areas of risk that the employer decides would be best navigated with the help of legal counsel, such as risk surrounding employee perceptions as well as employee compensation.

## Conclusion: Next Steps for Employers

Remember, regulatory agencies will not take you on your word that an employee is exempt – you will need to show the proof. As an employer, you are required to post a notice in your workspace, notifying employees of the right to file a complaint through the U.S. Department of Labor. The department currently employs close to 1,000 U.S. Department of Labor investigators scattered around 150+ offices to field these complaints.

The result of this advocacy? There are many thousands of Fair Labor Standards Act (FLSA) lawsuits filed every year across the country. Additionally, numerous legal actions are made by the U.S. Department of Labor, along with thousands of state-level labor investigations, not to mention thousands of plaintiffs and class action lawsuits.

Misclassifying employees is a costly mistake that can happen to any company. Fortunately, it is preventable. By taking the right measures, you can save yourself and your company a great deal of money and negative exposure in the long run. **ComplianceHR can help.**

### Disclaimer

This whitepaper is intended to serve as a starting point for educating Human Resources and Legal professionals on certain aspects of legal obligations of employers. It is not a comprehensive resource or a complete explanation of requirements. It offers practical information concerning the subject matter and is provided with the understanding that ComplianceHR is not rendering legal or tax advice, or other professional services. The contents are intended for general informational purposes only, and you are urged to consult your attorney concerning any particular situation and any specific legal questions you may have.

# ComplianceHR's Navigator OT

Determining whether an employee has enough “white collar” responsibility to be exempt from overtime pay can be a difficult, time-consuming, and potentially risky decision for Human Resources and Legal Professionals to make. This is particularly true in times of change, when employers create new roles, workers are hired or fired, workers have moved between states or jurisdictions, or new legislation is pending.

ComplianceHR's Navigator OT solution eliminates much of the legwork and helps to reduce the headache of evaluating roles for overtime exemption.

## Navigator OT provides you with:

- A simple digital questionnaire to capture your specific fact pattern
- A summary of the relevant federal and state exemption standards
- Actionable risk assessment(s) driven by expert analysis of over 2,400 court cases and federal and state regulations
- Instant actionable guidance and a customized report on how to lower your misclassification risk
- A complete questionnaire transcript

### Overall Risk

Without taking compensation into account, it is **Moderately High Risk** to classify this position as exempt.



This is the lowest risk of all the exemptions the position is qualified for. Learn more about compensation requirements and each exemption below.

### Analysis of the Administrative Exemption

**Moderately High Risk**

**Compensation Requirements Met**

#### Riskiest Factors

**Discretion and Independent Judgment** To qualify for the administrative exemption, a position must exercise discretion and independent judgment on matters of significance. The exercise of discretion and independent judgment involves comparing and evaluating possible courses of conduct and acting or making a decision after the various possibilities have been considered.

### Questionnaire Transcript

Evaluation of Director X-Submitted by worth+ot@compliancehr.com

#### Answers Provided

Does this position perform work in a computer, software, or information technology field?	No
Does this position perform work in any of the following artistic or creative fields?	None or the above
Does this position sell the Company's products or services?	No
Does this position use any manuals, guidelines, or other established standard procedures (SOPs) in the performance of the job?	No

Navigator OT helps to simplify the complexity of employment law and mitigates the risk of misclassifying a non-exempt employee as exempt from overtime. If you would like to learn more about Navigator OT, an expert system built with the employment law expertise and legal knowhow of Littler, please [sign up for a demonstration](#).