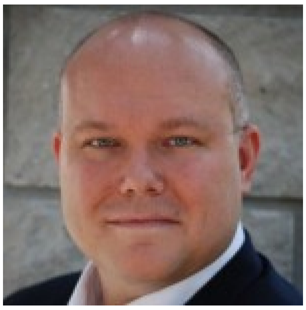
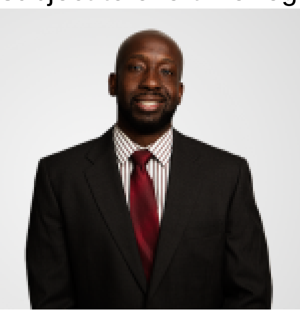
5 considerations for startups grappling with new overtime rules

This column, originally posted on Startland News, was co-written by EBCFO founder Dan Schmidt and Mark Opara, a general business and corporate law attorney at Seigfreid Bingham.



Dan Schmidt

Low pay, long hours, and maybe some future benefits — it's the startup way! In early stage companies, it's a tradeoff of current pain for future gain (or is that the CrossFit motto?), and the chance to be involved with projects that might change the world. But what happens when the startup world itself is disrupted? Such is the case with the new federal overtime regulations. The regulations, which go into effect Dec. 1, 2016, raise the minimum salary for an employee to be considered "exempt" — i.e., not subject to overtime regulations — from $23,660 to $47,476.



Mark Opara

With the estimated impact of the new regulation at a whopping $295 million per year in the first 10 years, small and big businesses alike are scrambling to figure out a game plan. After all — especially in the world of startups — a 40-hour work week just doesn't happen. That means overtime will quickly become a juggle of cash flow and burn rates. Here are some of the options you'll want to consider: **1. Determine your status.** If you're a sole proprietor, partner or LLC member with no employees, you're likely exempt from the new regulations. If you've made the decision to set up as a Delaware corporation, however, you may also be classified as an employee, and therefore subject to the labor standards. Either way, talk to your accountant to be sure. **2. Pay more — it's the first and easiest solution**. And most of the time, a $50,000 salary is considered a living wage anyway. But there are times, especially in pre-revenue startups, that this could pose a significant cash flow problem.
3. Consider giving employees quarterly bonuses to meet the threshold. Bonuses must be "non-discretionary" — i.e., commissions and bonuses tied to profitability or productivity. They must be paid at least quarterly, and can only make up 10 percent — or $4,747 — of the required salary amount. **4. Employers can make a "catch-up" payment at the end of each quarter to fill the gap.** If the

company doesn't have a bonus/commission sale, or if certain employees haven't qualified for enough in bonuses, quarterly "catch-up" payments are the way to go. If not made, employees are entitled to be paid for all overtime hours worked that quarter. **5. Hire additional part-time employees to cover the workload and keep everyone at 40 hours or less.** Of course, this does have the effect of increasing your total payroll expense to cover the additional, now-paid hours, but it avoids the overtime pay. Either way, it's not doing much for your burn rate. In summary, for most growth-stage companies, this likely won't cause many difficulties. This will hit the small, early-stage firms the hardest — they're the ones working long, long hours but with little cash flow. In general, we do not expect this change to have a significant impact on Kansas City's startup ecosystem. Many positions at early stage companies are on the tech side, and salaries for these nearly always range higher than the new threshold. One specific place the new rule might be problematic is in a new company with only founders that has chosen to be a corporation. Since the founders may be deemed to be employees of the corporation — rather than partners in a partnership — they may need to comply with the overtime rules. And as we well know, founders work overtime. Usually a lot of overtime.

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