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The Honorable R. Alexander Acosta
Secretary of Labor
c/o Ms. Melissa Smith, Director
Division of Regulations, Legislation & Interpretation
Wage and Hour Division
United States Department of Labor
200 Constitution Avenue N.W., Rm S-3502
Washington, DC 20210

RE: RIN 1235-AA20, Request for Information, *Defining and Delimiting the Exemptions for Executive, Administrative, Professional, Outside Sales and Computer Employees,* 82 FR 34616 (July 26, 2017)

Dear Mr. Secretary:

The International Franchise Association ("IFA") submits these comments in response to the Request for Information by the Department of Labor (the "Department" or "DOL") published in the Federal Register on July 26, 2017, regarding defining and delimiting the exemptions for executive, administrative, professional, outside sales and computer employees in Section 13(a)(1) of the Fair Labor Standards Act ("FLSA" or the "Act"), 29 U.S.C. § 213(a)(1).

The IFA's members include franchise companies in over 300 different business format categories, individual franchisees, and companies that support the industry in marketing, law, technology, and business development. The IFA's mission is to protect, enhance, and promote franchising. The IFA works through its government relations and public policy, media relations, and educational programs to further the interests of over 733,000 franchise establishments that support nearly 7.6 million direct jobs, over $674 billion of economic output for the U.S. economy, and over $404 billion of Gross Domestic Product. The IFA's members operate in all 50 states and in all facets of industry. Most franchisees are small businesses, without human resources departments or in-house legal counsel. They rely upon information and support provided by the IFA and other resources.

The IFA supports the Department's decision to revisit its 2016 changes[1] to the regulations[2] defining and delimiting the executive, administrative, and professional exemptions in Section 13(a)(1) of the Act.[3] The members of the IFA share the concerns of the various stakeholders identified by the Department in its request for public comment[4] that the 2016 Final Rule set a new salary level inappropriately high, excluding from overtime exemption too many employees who would otherwise satisfy the exemption duties tests. The 2016 Final Rule, which more than doubled the minimum salary level for exemption from $455 per week ($23,660 annualized) to $913 per week ($47,476 annualized), was found to be contrary to Congressional intent and exceeding the Department's authority in *State of Nevada, et al. v. U.S. Department of Labor*.[5] As the court in *Nevada* explained, "it is clear Congress defined the EAP exemption with regard to duties. In other words, Congress unambiguously intended the exemption to apply to employees who perform "'bona fide executive, administrative, or professional capacity' duties."[6] Although the FLSA gives the Department broad authority to define and delimit the exemption, that authority "is limited by the plain meaning of the words of the statute and Congress's intent."[7] The Department "does not have authority to use a salary-level test that will effectively eliminate the duties test as prescribed by Section 2013(a)(1)."[8]

"While the plain meaning of Section 213(a)(1) does not provide for a salary requirement," before 2016, the Department used "a permissible minimum salary level as a test for *identifying* categories of employees Congress intended to exempt."[9] The Department set "the minimum salary level as a floor to 'screen out the obviously nonexempt employees, making an analysis of duties in such cases unnecessary.'"[10] Setting a minimum salary level "somewhere near the lower end of the range of prevailing salaries" is "consistent with Congress's intent because salary serves as a defining characteristic when determining who, in good faith, performs actual executive, administrative, or professional capacity duties."[11]

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[1] 81 FR 32391 (May 23, 2016) ("2016 Final Rule").

[2] 29 C.F.R. Part 541.

[3] 29 U.S.C. § 213(a)(1) (the "EAP exemptions").

[4] 82 FR 34618 (July 26, 2017) ("Proposed Rules").

[5] CA No. 4:16-CV-731, 2017 WL 3837230 (E.D. Tex. Aug. 31, 2017).

[6] *Nevada*, 2017 WL 38377230 at *7.

[7] *Id.*

[8] *Id.*

[9] *Id.* at *8.

[10] *Id*. (*citing* Harry Weiss, *Report and Recommendations on Proposed Revisions of Regulations, Part 541* (June 30, 1949) (the "1949 Weiss Report") at 7-8.

[11] *Id.*

A $913 weekly salary requirement goes far beyond the mandate of setting a minimum floor to "screen out the obviously nonexempt employees". Instead, the prospect of a minimum salary level at this amount has had – and will have – a significant adverse impact on businesses, particularly in low-wage regions and industries, which encompasses many of IFA's members. Moreover, it is the opinion of the IFA and its members that the changes made through the 2016 Final Rule run counter to President Trump's Executive Order 13777 because they negatively impede job creation, the increased salary level unnecessarily excludes from the overtime exemptions many employees who would otherwise meet the duties tests, and the changes impose significant costs which far exceed any benefits.

The 2016 Final Rule and its increased salary level and scheduled indexing are greatly concerning to the IFA and its members between (add dates of survey). To better assess the impact of the 2016 Final Rule on its membership, the IFA surveyed its members. The IFA received nearly 300 responses from franchisees and franchisors, with over 55% of respondents reporting having less than 50 employees, and over 80% reporting annual revenue of less than $10 million in 2016. These respondents reported significant tangible and intangible impacts on small businesses as a result of the 2016 Final Rule. Almost 75% of all respondents reported a substantial increase in operating costs including an increase in overtime labor costs, increased timekeeping and payroll administration costs and costs associated with providing additional training and modifying policies and procedures. The average amount of estimated costs expected by members to comply with the 2016 Final Rule was just over $60,000, although some estimates went as high as $5 million. In response to these escalating costs, members reported taking different mitigating actions including increasing costs to customers, decreasing or eliminating employee bonus and incentive programs and investigating additional automation options aimed at reducing labor costs.

Accordingly, while the IFA agrees that the minimum salary level should be increased from the pre-2016 Final Rule level of $455 per week, it urges the Department to revisit – and substantially reduce– the $913 weekly salary requirement. In doing so, the IFA contends that the Department should utilize the same or a similar methodology as it used in its 2004 rulemaking. Aside from revising the salary level, the Department should not make any further changes to the Part 541 regulations at this time.

The Department has requested information in eleven specific areas. The IFA's responses to each of these are set forth below:

1. The 2016 Final Rule Set The "White Collar" Minimum Salary Threshold At An Unprecedented Level And The 2004 Methology Should Instead Be Used

> *In 2004 the Department set the standard salary level at $455 per week, which excluded from the exemption roughly the bottom 20 percent of salaried employees in the South and in the retail industry. Would updating the 2004 salary level for inflation be an appropriate basis for setting the standard salary level and, if so, what measure of inflation should be used? Alternatively, would applying the 2004 methodology to current salary data (South and retail industry) be an appropriate basis for setting the salary level? Would setting the salary level using either of these methods require changes to the standard duties test and, if so, what change(s) should be made?*

In the 2016 Final Rule, the Department increased the minimum salary level based upon the 40th percentile based on earnings of full-time non-hourly workers in the lowest wage Census Region, which was identified as the South Census Region. This methodology resulted in a minimum salary level of $913 per week or $47,476 annually –more than double from the requirement of $455 per week or $23,660 per year set in 2004.

The 2016 Final Rule increase and the DOL's methodology in setting the increase were unprecedented and unsupported. Bucking 77 years of regulatory tradition, the DOL used information regarding employee salaries to benchmark the salary level at the extraordinary 40th percentile. While the Department in prior rulemakings has utilized salary information in setting the minimum salary level, it has never come close to the 40th percentile. In 1958[12] and 1963[13], the Department used the 10th percentile. In 1970, the Department set the salary level just below the 12th percentile of executive employee in the West.[14] In 2004, the Department used the 20th percentile of salary levels in the South region and the retail industry.[15] This methodology was used, in part, to account for the standard duties

[12] Harry S. Kantor, *Report and Recommendations on Proposed Revision of Regulations, Part 541*, Wage and Hour & Public Contracts Division, U.S. Department of Labor (March 3, 1958) ("1958 Kantor Report") at 7-8.

[13] 28 FR at 7004 (July 9, 1963).

[14] 28 FR 7002, 7004 (July 9, 1963).

[15] 69 FR at 22167-69 and Tables 2 & 3.

test which was adopted in 2004 and resulted in the elimination of the restriction on nonexempt work in the old long duties tests.[16]

The 2016 Final Rule 40th percentile methodology results in a salary level that is substantially higher than applying the 1958 or 2004 methodology. In responding to criticism that the proposed level, which was based on salaries nation-wide, would have a disproportionate and adverse impact on businesses in lower-wage southern states, the Department determined that the salary set in the 2016 Final Rule would be based on earnings of full-time salaried workers in the lowest earning Census Region – the South Census Region.[17] However, reliance upon this methodology is disingenuous and misleading as it fails to account for the significant disparities in median income of the represented states. The Census Bureau divides the country into four large regions: Northeast, Midwest, South and West. Each region is then subdivided into smaller divisions. The states included in the South Census Region, including Maryland, the District of Columbia and Virginia, which are three of the top 11 income areas in the country.[18] Broadly including data from these areas ignores the Department's historical methodology of studying salaries paid to exempt employees in lower-wage areas and industries, resulting in an inappropriately high salary level. Averaging the salaries paid to employees in the District of Columbia – which ranks number five in median income – with Mississippi – which ranks number 51 in the country – disproportionally increases the salary levels and significantly disadvantages employers in the lowest-wage jurisdictions. Moreover, failing to consider low wage industries – such as retail, restaurants and small-businesses – further deviates from the historical methodology of studying salaries paid to exempt employee in "the lowest-wage region, or in the smallest size establishment group, or in the smallest-sized city group, or in the lowest-wage industry."[19]

Even applying the 40th percentile in the South Census Region, the DOL has not explained its failure to consider salary levels in the lowest wage subdivisions, the lowest wage industries, the smallest businesses and the smallest cities – or to include earnings data of lawyers, doctors and sales employees who are not subject to the Part 541 salary requirements. Historically, with only a few exceptions, the

[16] 2004 Final Rule, 69 FR at 22167 ("we relied on the lowest 20 percent of salaried employees in the South, rather than the lowest 10 percent, because of the proposed change from the short and long test structure and because the data included nonexempt salaried employees").

[17] 2016 Final Rule, 81 FR at 32408. The South Census region is compromised of the District of Columbia, Maryland, Virginia, Delaware, North Carolina, Texas, Georgia, Kentucky, South Carolina, Tennessee, Alabama, Oklahoma, Louisiana, Florida, West Virginia, Arkansas, and Mississippi.

[18] The District of Columbia ranks as having the fifth highest median income of all states in the country with median weekly earnings for salaried FLSA covered workers of $1,352 per week or an annual equivalent of $70,311. Maryland ranks number nine with median weekly earnings of $1,265 per week and an annual equivalent of $65,782 and Virginia ranks number eleven with median weekly earnings of $1,233 per week and an annual equivalent of $64,134. *See* Current Population Survey, Outgoing Rotation Series, pooled May 2014 to July 2017. Earnings data adjusted by CPI-W to July 2017 dollar equivalent.

[19] 1958 Kantor Report at 7-8.

DOL has increased the salary levels at a rate of between 2.8% and 5.5% per year. The DOL's 2016 Final Rule represented an increase of almost 10% per year.

Since 2004, salaries have not increased by over 10% annually. The DOL has never before doubled the salary levels for the white-collar exemptions in a single rulemaking, let alone more than doubled the salary levels as set forth in the 2016 Final Rule.

Staggeringly, the NPRM's proposal wholly discounts the significant impact increasing the salary level at the proposed rate will have upon the majority of the country, particularly in areas and in industries where the identified 40% threshold is entirely disproportionate to actual average salaries. Similar to the 2004 methodology, consideration needs to be paid to regional and industry averages. The 2016 Final Rule salary level has a disproportionate impact on many industries – and in particular small businesses. Millions of employees who work for smaller employers will clearly meet the white collar duties requirements but earn below $47.476 a year. IFA respectfully requests that the Department significantly reduce its proposed standard salary level for exemption. As the Court noted in the *Nevada* decision, the DOL's 2016 Final Rule undermines the purpose of the salary threshold. For almost 70 years (since 1949):

> The Department has long recognized that the salary paid to an employee is the "best single test" of exempt status (Stein Report at 19) and that setting a minimum salary threshold provides a "ready method of screening out the obviously nonexempt employees'' while furnishing a ''completely objective and precise measure which is not subject to differences of opinion or variations in judgment.'' Weiss Report at 8–9. The Department reaffirmed this position in the 2004 Final Rule, explaining that the ''salary level test is intended to help distinguish bona fide executive, administrative, and professional employees from those who were not intended by Congress to come within these exempt categories[,]" and reiterating that any increase in the salary level must "have as its primary objective the drawing of a line separating exempt from nonexempt employees." [20]

Thus, to implement Congress' intent, the DOL should not set the minimum salary threshold at a level that excludes a significant number of employees who obviously meet the duties tests for exemption.

[20] 2015 NPRM at 38524 (citing 69 Fed. Reg. 22165).

The salary level must be appropriate across the "many thousands of different situations throughout the country."[21]

As the Department stated in 1949: "To be sure, salaries vary, industry by industry, and in different parts of the country, and it undoubtedly occurs that an employee may have a high order of responsibility without a commensurate salary." [22] Thus, to avoid excluding millions of employees from the exemption who do perform exempt job duties, the Department has recognized that "the same salary cannot operate with equal effect as a test in high-wage and low-wage industries and regions, and in metropolitan and rural areas, in an economy as complex and diversified as that of the United States. Despite the variation in effect, however, it is clear that the objectives of the salary tests will be accomplished if the levels selected are set at points near the lower end of the current range of salaries"[23] of exempt employees "in the lowest-wage region, or in the smallest size establishment group, or in the smallest-sized city group, or in the lowest-wage industry."[24]

Continued utilization of the 2016 Final Rule methodology is unworkable and will render the duties test superfluous. The DOL should not set the level so high that it expands the number of employees eligible for overtime beyond what Congress envisioned when it created the exemptions. Yet, this is exactly what the DOL did through the 2016 Final Rule. This is particularly true for many of our members' businesses who operate in regions where the 40th percentile is far below $47,476 salary and who have employees who clearly meet the duties tests. Accordingly, the IFA recommends that the Department revisit the minimum salary levels, utilizing the same – or similar – methodology used in establishing the salary levels in the 2004 rulemaking. A salary level set near the lower end of current salaries in the lowest-wage region, the smallest size establishments, in the smallest-sized city group, or in the lowest-wage industry establishes a bright and reasonable line between exempt and nonexempt employees.

2. A Single Minimum Salary Level Should Be Set Nationwide.

> *Should the regulations contain multiple standard salary levels? If so, how should these levels be set: by size of employer, census region, census division, state, metropolitan statistical area, or some other method? For example, should the regulations set multiple salary levels using a percentage based adjustment like that used by the federal government in the General Schedule Locality Areas to adjust for the varying cost-of-living across different parts of the United States? What would the impact of multiple standard*

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[21] *Report and Recommendations on Proposed Revisions of Regulations, Part 541*, at 9, Harry Weiss, Presiding Officer, Wage and Hour and Public Contracts Divisions, U.S. Department of Labor (June 30, 1949).

[22] *Id.* at 11.

[23] 1958 Kantor Report at 5.

[24] *Id.* at 6-7.

salary levels be on particular regions or industries, and on employers with locations in more than one state?

The Department should not adopt multiple standard salary levels, as doing so adds unneeded additional complexity and makes it exceedingly difficult for employers to engage in multi-jurisdictional operations.

As set forth in its response to Question 1, it is the position of the IFA that there is no need for multiple salary levels if the Department adopts a standard salary level that screens out only obviously nonexempt employees. Although stakeholders have previously suggested multiple standard salary levels, the Department has always rejected such requests.[25] The Department should not deviate from this historical standard now. Applying the 2004 or similar methodology to current BLS data which accounts for differences in salaries by setting the salary level near the lower end of current salaries in the lowest-wage region, the smallest size establishments, in the smallest-sized city group, or in the lowest-wage industry obviates the need for multiple salary levels.

3. Different Salary Levels Should Not Be Set By Exemption.

Should the Department set different standard salary levels for the executive, administrative and professional exemptions as it did prior to 2004 and, if so, should there be a lower salary for executive and administrative employees as was done from 1963 until the 2004 rulemaking? What would the impact be on employers and employees?

The Department should not adopt different standard salary levels for the executive, administrative and professional exemptions. For the reasons stated above, if the Department adopts a standard salary level "somewhere near the lower end of the range of prevailing salaries" in order to exclude only obviously nonexempt employees based on salary alone, there would be no need to add the additional complexity of different salary levels for executive, administrative and professional exemptions.

The regulated community has not been burdened with complying with multiple salary levels by exemption for more than two decades. Prior to 2004, the Part 541 regulations established different salary levels under the long duties test for the executive, administrative and professional exemptions. From 1940 to 1963, the Department adopted a lower salary level for the executive exemption. Beginning in 1963, the salary level for executive and administrative employees were the same, with a

[25] In 1940, 1963, 1970, 2004 and 2016, the Department rejected proposals based on community size, geographical variations, and/or different industries. *See* 1940 Stein Report at 5-6; 28 FR 7002, 7002 & 7004 (July 9, 1963); 35 FR 883, 884 (Jan. 22, 1970); 2004 Final Rule, 69 FR at 22171; and 2016 Final Rule, 81 FR at 32411.

higher salary level for professionals. The Part 541 regulations have never included different salary levels by exemption under the short duties test.

The salary level under the long duties test that was in effect from 1975 to 2004 for executive and administrative employees was $155 per week – equivalent to just $3.875 per hour for a 40-hour workweek, which was below the 1991 minimum wage of $4.25 per hour. For professionals, the

salary level under the long duties test in effect from 1975 to 2004 was $170 per week – equivalent to just $4.25 per hour for a 40-hour workweek, which was equal to the 1991 minimum wage and below the 1996 minimum wage of $4.75. Thus, by 1996, few employers relied on the long duties test and salary levels, and instead used the short duties test for exemption that, until 2004, required a salary level of $250 per week ($6.25 per hour for a 40-hour workweek). In short, the Part 541 regulations have not included different and operative salary levels by exemption since 1996.

In updating and streamlining the exemptions in 2004, the Department eliminated the long-duty and short-duty tests in favor, replacing it with primary duty test, and also established a singular minimum salary level. Reverting back to multiple salary levels for different exemptions now would just create confusion, increase compliance costs, and would likely result in amplified litigation efforts. Therefore, the IFA strenuously contests any effort by the Department to reestablish multiple salary levels by exemption.

4. The Department Should Not Implement The Pre-2004 Short and Long-Test Salary Levels.

> *In the 2016 Final Rule the Department discussed in detail the pre- 2004 long and short test salary levels. To be an effective measure for determining exemption status, should the standard salary level be set within the historical range of the short test salary level, at the long test salary level, between the short and long test salary levels, or should it be based on some other methodology? Would a standard salary level based on each of these methodologies work effectively with the standard duties test or would changes to the duties test be needed?*

As discussed in response to Question 1, the IFA recommends utilizing the same or similar methodology relied upon by the Department in 2004. This methodology was contrived to account for the replacement of the long and short duties tests with the more rigorous standards duties test. Accordingly, the Department should return to the 2004 methodology for setting the standard salary level and no changes to the duties tests are needed.

5. The Salary Level Should Be Set At A Level That Does Not Eclipse The Duties Tests.

> *Does the standard salary level set in the 2016 Final Rule work effectively with the standard duties test or, instead, does it in effect eclipse the role of the duties test in determining exemption status? At what salary level does the duties test no longer fulfill its historical role in determining exempt status?*

As the court found in *Nevada*, the high salary level adopted in the 2016 Final Rule unlawfully eclipsed the role of the duties test in determining exempt status. The Department admitted in the 2016 Final Rule that a $913 per week ($47,476 annualized) salary level would result in "4.2 million employees *who meet the standard duties test*" to no longer qualify for the EAP exemptions "*irrespective of their job duties and responsibilities*."[26] For those 4.2 million employees who met the duties tests but earned below $913 per week, the 2016 Final Rule was a total eclipse.

Adjusting the standard salary level using the Department's 2004 methodology would allow both salary and duties tests to fulfill their historical role. Although slight modifications to the 2004 methodology is unlikely to defy Congressional intent, predicting the exact salary level that a court might view as exceeding the Department's authority would be pure speculation.

6. The Substantial Impact of the 2016 Final Rule on IFA Members.

> *To what extent did employers, in anticipation of the 2016 Final Rule's effective date on December 1, 2016, increase salaries of exempt employees in order to retain their exempt status, decrease newly non-exempt employees' hours or change their implicit hourly rates so that the total amount paid would remain the same, convert worker pay from salaries to hourly wages, or make changes to workplace policies either to limit employee flexibility to work after normal work hours or to track work performed during those times? Where these or other changes occurred, what has been the impact (both economic and non-economic) on the workplace for employers and employees? Did small businesses or other small entities encounter any unique challenges in preparing for the 2016 Final Rule's effective date? Did employers make any additional changes, such as reverting salaries of exempt employees to their prior (pre-rule) levels, after the preliminary injunction was issued?*

Because of the litigation challenging the 2016 Final Rule, employers reacted very differently in anticipation of the December 1, 2016 effective date – often dependent on the expected costs of providing salary increases to maintain the exemptions and additional overtime due to employees reclassified to nonexempt. As indicated above, the IFA's members represent many diverse business

[26] 2016 Final Rule, 81 FR at 32405 (emphasis added).

formats including individual franchisees and franchisors as well as companies that support the franchising industry. To better inform the Department of the unique challenges facing the members of the IFA – many of whom are small businesses - the IFA surveyed its members on the actual and prospective impact of the 2016 Final Rule. Of the almost 300 respondents, 84% were franchisees, 15% were franchisors and 1% was suppliers. Almost 99% of the survey respondents represented for-profit businesses and the majority of their employees were located in the following geographically mixed areas:

- New England – 5.37%
- NY/NJ – 6.04%
- Mid-Atlantic – 11.41%
- Southeast – 22.15%
- Midwest – 21.48%
- Mountain Plains – 9.4%
- West – 10.74%

The largest industry sectors represented were in healthcare and social assistance (22.15%), followed by restaurants and food service (19.13%) and retail (12.08%). Almost 80% of respondents had revenue of less than $10 million in 2016 and almost 55% of respondents reported having less than 50 employees with 8.06% reporting more than 500 employees. When asked if they had taken any steps to prepare for the implementation of the 2016 Final Rule, 36.58% of respondents said they had implemented such changes and 45.64% said they had made plans but did not implement changes. The steps that the respondents reported taking, or planned to take, to comply with the 2016 Final Rule included the following:

- Approximately 22% increased salaries of exempt employees to retain their exempt status;
- Approximately 6% increased salaries of exempt employees in order to retain their exempt status, but also reduce benefits, such as health care or auto or phone allowances, to minimize costs associated with the salary changes;
- Over 43% reclassified employees to non-exempt overtime eligible;
- About 6% replaced employees with automated alternatives or otherwise reduced headcount;

- Almost 11% raised prices for customers as an effect of increased labor costs; and
- Approximately 8% limited the flexibility for reclassified employees to work alternative hours or at home.

For those who reclassified employees to overtime eligible, significant changes in compensation practices and policies were reported, including: conversion from salary to hourly pay (62.61%); reducing employees' effective hourly rate so that their total pay remained the same (25.65%); requiring employees to track and record work hours (44.78%); decreasing work hours to ensure total hours were 40 or less per workweek (33.04%); reducing bonuses or commissions (22.61%); and changing benefit plans, resulting in less favorable benefits (e.g. paid leave, retirement, insurance benefits) (16.52%).

Respondents also reported a substantial increase in operational costs including: increased overtime costs (74.81%); increased training costs (17.29%); increased timekeeping and/or payroll administration costs (62.78%); increased managerial costs of supervising additional non-exempt employees (37.97%); costs associated with drafting or modifying policies and procedures (48.87%); and costs associated with benefits and/or benefit plan changes (26.32%). When asked to quantify costs, respondents who reported an increase in labor costs due to salary increases estimated an average of $36,000 in annual costs going to as much as $250,000. The total amount of additional costs due to complying with the 2016 Final Rule was reported as an average amount of just over $60,000, with other estimates going up to as high as $5,000,000.

Anecdotally, IFA members reported significant economic and non-economic impacts related to the 2016 Final Rule on both employers and employees. Many respondents identified concerns with employee morale, particularly employees who feel that they have been demoted or are less valued because they have been converted to hourly employees. Such a significant increase to the minimum salary level was also reported as impeding recruitment efforts and limiting promotional opportunities. The conversion of formally exempt employees to non-exempt status places a disproportionate burden on those individuals who remain exempt, because more responsibilities are shifted to them in an effort to manage labor and overtime costs. Members also reported having to decrease or eliminate bonus and incentive programs for employees, to mitigate increased labors costs. Many members also expressed concerns over the reduction in flexibility of employees. Having to limit hours or incur additional overtime costs places great strains on organizations, particularly those with fluctuating work needs such as healthcare and janitorial industries. Some members reported exploring ways to further automate operations to reduce labor needs, thus causing potential job reduction.

Overall, the significant increase in the minimum salary level set forth in the 2016 Final Rule, coupled with the on-going burdens of the automatic increases, placed an enormous strain on the operations of IFA's members, many of whom are small businesses operating in low-margin industries. As such, the IFA implores the Department to consider both the economic as well as non-economic impact of increasing

the minimal salary level. The IFA asks that the Department instead seek to implement a more modest increase and eliminate consideration of automatic increases going forward.

7. A Duties-Only Test Should Not Be Adopted.

> *Would a test for exemption that relies solely on the duties performed by the employee without regard to the amount of salary paid by the employer be preferable to the current standard test? If so, what elements would be necessary in a duties-only test and would examination of the amount of non-exempt work performed be required?*

The IFA does not support a duties-only test for exemption if such a test comes with any changes to the current duties tests.

The IFA opposes any revision to the duties test – particularly one which introduces a quantitative requirement – whether made in reversion to a long/short duties test or otherwise. Such a change would upend the regulated community, adding substantial unjustified (and unexplored) costs and burdens on employers, and serve to increase litigation.

Other jurisdictions that have adopted such quantitative tests, such as California, have realized the unintended negative effects of its so-called "bright-line" rule. Using California as an example, rather than decreasing litigation and uncertainty over classifications, California's rule has had the opposite effect—substantial litigation as members of the California plaintiffs' bar have come to realize (and capitalize on) the extreme difficulty employers face in proving the amount of time employees spend on exempt versus non-exempt tasks. Indeed, quantitative rules place an enormous burden on employers to engage in extensive analysis and time testing, wading through the hour-by-hour—and in some cases minute-by-minute—tasks of their employees in order to defend their classification decisions. Regardless of any effort to regulate around such ambiguities, the central issue will always remain what is—and what is not—exempt work.

The Department has already acknowledged that these precise concerns render quantitative testing impracticable. In 2004, responding to commenters who requested the addition of a quantitative test, the Department reasoned that such analysis unnecessarily adds complexity and burdens to exemption testing by, for example, requiring employers to "time-test managers for the duties they perform, hour-by-hour in a typical workweek."[27]

[27] *See* Preamble to 2004 Final Rule, 69 Fed. Reg. at 22126 (Apr. 23, 2004) (hereinafter, "Preamble").

Requiring employers to "distinguish[] which specific activities were inherently a part of an employee's exempt work proved to be a subjective and difficult evaluative task that prompted contentious disputes."[28]

The Preamble to the 2004 Final Rule identified further concerns with requiring a strict delineation of time spent on exempt and non-exempt duties:

> For example, employers are not generally required to maintain any records of daily or weekly hours worked by exempt employees (see 29 CFR 516.3), nor are they required to perform a moment-by-moment examination of an exempt employee's specific duties to establish that that an exemption is available. Yet reactivating the former strict percentage limitations on nonexempt work in the existing 'long' duties tests could impose significant new monitoring requirements (and, indirectly, new recordkeeping burdens) and require employers to conduct a detailed analysis of the substance of each particular employee's daily and weekly tasks in order to determine if an exemption applied.[29]

Rather than solve any of the perceived problems with the primary duty test, a quantitative requirement only creates tremendous recordkeeping burdens on employers and adds to employers' uncertainty over classifications. Such a quantitative requirement merely serves to incentivize plaintiffs' attorneys to systematically attack an employee's classification. No benefit is to be derived from now injecting a quantitative requirement to the well-settled qualitative approach.

The IFA urges the Department to retain its reasoned analysis conducted in 2004, establishing four nonexclusive factors for determining the primary duty of the employee:

(1) The relative importance of the exempt duties as compared with other types of duties;

(2) The amount of time spent performing exempt work;

(3) The employee's relative freedom from direct supervision; and

(4) The relationship between the employee's salary and the wages paid to other employees for the same kind of nonexempt work.

Under these factors, the amount of time spent may be considered, but is not indicative alone, of an exempt status. Although the Department has the authority to adopt regulations that define and delimit

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[28] *Id*. at 22137.

[29] *Id*. at 22126-22127.

the exemptions based solely on job duties, the Part 541 regulations have included a salary level test since they were first adopted in 1938. Employers, employees, courts and the Department have found the salary tests a useful tool to exclude obviously non-exempt employers from the exemption. If the Department applies the 2004 methodology to make any increase to the standard salary level, that salary level will fulfill its historical roll, and no changes in the duties tests are needed. The IFA implores the Department to continue its application of the holistic approach developed in 2004 and summarily reject any requirement that duties must be measured or that an antiquated two test system be reinstituted while continuing to utilize a minimum salary level as a basis to exclude those obviously non-exempt.

8. Occupations Impacted.

> *Does the salary level set in the 2016 Final Rule exclude from exemption particular occupations that have traditionally been covered by the exemption and, if so, what are those occupations? Do employees in those occupations perform more than 20 percent or 40 percent non-exempt work per week?*

Because salary levels for the same occupation can vary based on the work location of the employee (e.g., geographic region, rural v. urban), generalizations regarding occupations that would have been excluded under the 2016 Final Rule are difficult. However, our members report that a high percentage of managers and assistant managers, particularly in low-wage, low-margin industries such as healthcare, retail and restaurants, would have been excluded from an exemption under a $913 salary level.

9. Employers Should Be Able To Use Bonuses and Commissions Without Limits.

> *The 2016 Final Rule for the first time permitted non-discretionary bonuses and incentive payments (including commissions) to satisfy up to 10 percent of the standard salary level. Is this an appropriate limit or should the regulations feature a different percentage cap? Is the amount of the standard salary level relevant in determining whether and to what extent such bonus payments should be credited?*

The 2016 Final Rule permitted the inclusion of non-discretionary bonuses and/or commissions – up to 10% of the total required salary – to establish minimal salary levels. The Final Rule would have only counted bonuses paid quarterly or more frequently, excluding all annual bonuses. While IFA supports the inclusion of additional compensation in calculating an employee's salary, the limitations set forth in the Final Rule are too restrictive and represent a lack of understanding of how businesses operate.

Many bonuses or incentive payments earned by exempt employees are only paid annually. Excluding these payments from total compensation unduly burdens employers as they are often critical components of an employee's total wages. As the stakeholders conveyed prior to the issuance of the Final Rule, and the Department recognized, nondiscretionary bonuses and incentive payments are "an

important component of employee compensation in many industries"[30] and "such compensation might be curtailed if the standard salary level was increased and employers had to shift compensation from bonuses to salary to satisfy the new standard salary level[31]." Doing so would have a "negative impact on the workplace and would undermine managers' sense of 'ownership' in their organizations."[32]

Arbitrarily capping the amount of additional compensation that can be considered as meeting the salary threshold runs afoul of other provisions of the FLSA. For example, recognizing the realities of compensation structures, the regulations reflect that "commissions, nondiscretionary bonuses and other nondiscretionary compensation" – in addition to a guaranteed salary – may be counted towards meeting the threshold required to establish the highly compensated employee exemption.

In addition to permitting unrestricted incentive pay and commissions to comprise the required salary, the Department should also include a "make up" provision, similar to that provided by the regulations governing the highly compensated employee exemption.

In other words, employers should be given an opportunity to provide employees who otherwise meet the white collar duties tests additional compensation – on an annual basis – to ensure that they are at the minimum salary level.

10. The Highly Compensated Employee Exemption Should Not Consist Of Multiple Salary Levels.

> *Should there be multiple total annual compensation levels for the highly compensated employee exemption? If so, how should they be set: by size of employer, census region, census division, state, metropolitan statistical area, or some other method? For example, should the regulations set multiple total annual compensation levels using a percentage based adjustment like that used by the federal government in the General Schedule Locality Areas to adjust for the varying cost-of-living across different parts of the United States? What would the impact of multiple total annual compensation levels be on particular regions or industries?*

For the reasons discussed above under Questions 2 and 3, the Department should not adopt multiple annual compensation levels for the highly compensated test.

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[30] 2016 Final Rule, 81 FR at 32432.

[31] 2015 NPRM at 38535.

[32] *Id.*

The Department adopted the highly compensated test[33] in recognition that "the higher the salaries paid the more likely the employees are to meet all the requirements for exemption, and the less productive are the hours of inspection time spent in analysis of the duties performed."[34] Currently, an employee must earn $100,000 annually, with $455 per week paid on a salary basis. Employees who earn more than the required total annual compensation are not exempt unless: (1) their primary duty includes performing office or non-manual work; and (2) they customarily and regularly perform any one or more of the exempt duties or responsibilities of an executive, administrative or professional employee.[35]

The duties requirements in the Part 541 regulations are sufficient to ensure that only *bona fide* executive, administrative and professional employees qualify for the Section 13(a)(1) exemption under the highly compensated test.

Thus, the Department should revise the Part 541 regulations to remove the requirement of a weekly salary. Alternatively, the Department should not increase the $100,000 total compensation level.

11. Indexing Should Not Be Utilized.

> *Should the standard salary level and the highly compensated employee total annual compensation level be automatically updated on a periodic basis to ensure that they remain effective, in combination with their respective duties tests, at identifying exempt employees? If so, what mechanism should be used for the automatic update, should automatic updates be delayed during periods of negative economic growth, and what should the time period be between updates to reflect long term economic conditions?*

Our members are particularly concerned with the 2016 Final Rule's automatic updates adjusting the salary level tied to the applicable 40th percentile for the lowest wage census region (for white collar exempt employees) or 90th percentile nationwide (for highly compensated employees).

The IFA strongly urges that automatic increases should not be utilized. As a threshold matter, frequently adjusting the minimum salary level creates an unsustainable floor and results in instability within businesses that will be required to revisit base level salaries on a routine basis to ensure compliance. Employers operate on varying fiscal calendars. Preparing for automatic increases presents challenges in terms of budgeting and implementation. Potential annual reclassification puts an undue burden upon employers who must comply with state notice requirements, reprogram compensation systems and

[33] The highly compensated test is not a separate exemption. Rather, 29 C.F.R. § 541.600 provides a different and shorter duties *test* for highly compensated employees under Section 13(a)(1) of the FLSA. *See* 2004 Final Rule, 69 FR at 22123 ("The 'highly compensated' *test* in the final rule applies only to employees who earn at least $100,000 per year …") (emphasis added).

[34] *Id.* at 22173 (quoting the 1949 Weiss Report); *see also* 29 C.F.R. § 541.601(c).

[35] 29 C.F.R. § 541.601(a), (c) & (d).

conduct additional training. Additionally, employers must contend not only with the costs of increased wage rates, but also must incur the additional expense of routine classification analysis, decision-making, and implementation of changes in response to the new salary level when it is announced.

At no time has Congress granted the Department the authority to index its salary test. While the issue has been raised by stakeholders during several prior rulemakings, as far back as 1949 the DOL has rejected the imposition of automatic increases. Most recently, in 2004, the Department summarily rejected the concept of automatic increases to the minimal salary level.[36] At the time, the DOL contended that such an action is contrary to congressional intent and disproportionately impacted lower-wage geographic regions and industries:

> [S]ome commenters ask the Department to provide for future automatic increases of the salary levels tied to some inflationary measure, the minimum wage or prevailing wages. Other commenters suggest that the Department provide some mechanism for regular review or updates at a fixed interval, such as every five years. Commenters who made these suggestions are concerned that the Department will let another 29 years pass before the salary levels are again increased. The Department intends in the future to update the salary levels on a more regular basis, as it did prior to 1975, and believes that a 29-year delay is unlikely to reoccur. The salary levels should be adjusted when wage survey data and other policy concerns support such a change. Further, the Department finds nothing in the legislative or regulatory history that would support indexing or automatic increases. Although an automatic indexing mechanism has been adopted under some other statutes, Congress has not adopted indexing for the Fair Labor Standards Act. In 1990, Congress modified the FLSA to exempt certain computer employees paid an hourly wage of at least 6½ times the minimum wage, but this standard lasted only until the next minimum wage increase six years later. In 1996, Congress froze the minimum hourly wage for the computer exemption at $27.63 (6½ times the 1990 minimum wage of $4.25 an hour). In addition, as noted above, the Department has repeatedly rejected requests to mechanically rely on inflationary measures when setting the salary levels in the past because of concerns regarding the impact on lower wage geographic regions and industries. This reasoning applies equally when considering automatic increases to the salary levels. The Department believes that adopting such approaches in this rulemaking is both contrary to

[36] *See* Preamble at 22167.

congressional intent and inappropriate.[37]

Mandating automatic increases not only runs afoul of Congressional intent but also presents an issue of parity. By continuously raising the salary floor, a cascading effect necessarily occurs. Businesses must face the prospect of either continual reclassification of employees otherwise performing exempt duties or an increase to overall labor costs as, arguably, those salaries above the minimum must be equally raised or risk compensation inequity.

If an employer chooses to raise the salary levels of those currently earning the minimum salary level, they will likewise need to raise the salary level of those employees working in positions that are already paid more than the minimum proposed salary level. Failing to do so will result in a disparity between the wages of those in higher level positions, with more experience and responsibility. The Department, however, in issuing the 2016 Final Rule failed to address salary compression issues or related costs.

Moreover, tying increases to a specific percentile will quickly cause minimum salaries to skyrocket, drastically impacting not only employers, but also creates unavoidable consequences for employees who are reclassified from exempt to non-exempt, as they will lose the flexibility they have previously enjoyed. If employees are reclassified to hourly workers, they will only be compensated for those hours they work. Exempt employees, however, must be paid a guaranteed salary every week in which they perform any work, regardless of the number of hours worked. Yes, non-exempt employees receive overtime pay for working more than 40 hours in a workweek, but they also lose pay if they work less than 40 hours. Exempt employees do not receive overtime for working more than 40 hours in a workweek, but do not lose pay if they work less. This means that instead of being able to structure their day around child care needs, children's school meetings, doctor's appointments, and other personal needs without losing pay, non-exempt employees have to think carefully before taking time off work.

The Department argued in the 2015 NPRM that Congress' failure to provide "guidance either supporting or prohibiting automatic updating" indicates it has authority to do so.[38] However, equally plausible is the assumption that Congress felt no need to act because: (1) the Department, in the 79-year history of the FLSA, has never seriously considered indexing the salary levels; (2) in 2004, the Department concluded that indexing would violate congressional intent; and (3) Congress' failure to ever index anything under the FLSA is sufficient guidance.

Notice and comment rulemaking has achieved the purpose of the APA by ensuring vigorous public debate about the salary levels, including submission of salary information in public comments. The regulatory history shows that the Department usually adjusts its proposed salary levels based on the public comments. Proposed salary levels have been increased and decreased in the final regulations. For example, in 2004, in response to the public comments, the Department increased its proposed

[37] 2004 Final Rule at 22171-72.

[38] *Id.* at 38538.

standard salary level from $425 per week to $455 per week, and the annual compensation for the highly-compensated test from $65,000 to $100,000. Automatic salary increases would end this public debate forever, even in periods of economic downturns when the costs of the salary increases would be particularly harmful to the economy.

12. Conclusion

The IFA and its membership support the opportunity to revisit the 2016 Final Rule and corresponding revisions to the FLSA. As we advised prior to the issuance of the 2016 Final Rule, the IFA strenuously opposes any immediate increase in the salary level to $913 per week or $47,476 per year. As our membership has reported, such an increase will have substantial negative economic and non-economic impacts particularly on small businesses. The Department should forgo any consideration of automatic increases to the minimum salary level. Such action creates unnecessary instability within businesses and presents significant burdens in terms of budgeting and implementation upon the regulated community.

The IFA would support a modest increase to the minimum salary level and recommends utilizing the same or similar methodology used in 2004 to obtain the appropriate amount. Moreover, while IFA supports the inclusion of additional compensation in calculating an employee's salary, the limitations set forth in the 2016 Final Rule are too restrictive and represent a lack of understanding of how businesses operate. Instead, the IFA urges the Department to allow additional compensation – such as commissions, nondiscretionary bonuses and other nondiscretionary compensation – to be used, in addition to guaranteed salary, to establish compliance with the minimum salary requirements. Finally, it is the IFA's position that no changes to the current duties test should be made. Adjusting the salary level using the Department's 2004 methodology would allow both salary test to fulfill its historical role – screen those obviously nonexempt without eclipsing the standard duties requirements.

Thank you for the opportunity to respond to the Request for Information and present our views before you being a formal rulemaking. We look forward to working with the Department on this important issue.

Respectfully submitted:

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