## *THE REVISED FLSA "WHITE COLLAR" OVERTIME-EXEMPTION RULES:*

What Has Changed, What You Should Do

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On Monday, May 23, 2016, the U.S. Labor Department ("DOL") officially published its revised definitions for the federal Fair Labor Standards Act's "white collar" exemptions. These provisions are scheduled to take effect on *December 1, 2016*.

This material provides background and context for these developments, summarizes what has changed, and recommends general approaches that convenience-store employers should consider as they decide what steps are now necessary. Of course, it is not possible to lay-out a detailed, one-size-fits-all plan. Instead, management's actions must ultimately be guided by the regulations' implications for the actual facts, circumstances, and business goals of each company, and sometimes even of individual stores or other facilities.

◊ *What Is This All About?*

The FLSA contains certain exemptions from its overtime requirements. That is, it sets out situations in which some employees are not subject to the requirements to pay extra for overtime hours. One group that is not subject to FLSA overtime is referred to as "white collar" employees. This group includes Executive, Administrative, Professional, and Outside-Sales employees. In relatively-recent times, DOL's regulations have introduced two more, for qualifying Computer Employees and for certain "Highly Compensated" employees.

Congress authorized DOL to "define and delimit" the white-collar exemptions. In March 2014, President Obama directed the agency to "modernize and streamline" the version of these definitions that had been published in 2004.

DOL released proposed revisions in July 2015 and sought reaction from the public. NACS responded by submitting extensive comments in September 2015. DOL evaluated the public's input (including that it expressly took note of some that NACS® presented) and has changed the 2004 definitions in these ways:

- One requirement for exempt status under most of the white-collar exemptions from the FLSA's overtime rules is that the employee be paid on a salary basis at a rate of not less than $455 per week (which annualizes to $23,660). This minimum threshold will increase to *$913 per week* (which annualizes to $47,476). There are also duties requirements that must be met.

- The total-annual-compensation threshold for the Highly Compensated exception will increase from $100,000 to *$134,004*.

- For the first time, employers will be able to *satisfy up to 10%* of the minimum-salary threshold through nondiscretionary bonuses and other incentive payments (including commissions), if the payments are made *at least quarterly*. However, this crediting *will not be permitted* as to the salaries paid to employees treated as exempt under the Highly Compensated exception (but these payments can still be taken into account for purposes of determining whether the total-annual-compensation threshold is met for that exception).

- The minimum-salary threshold and the "highly compensated" total-annual-compensation amount will now be "updated" *every three years*, beginning on January 1, 2020. DOL will announce these changes *150 days in advance*.

There was much anxiety and anticipation about whether the duties-related requirements for exempt status would be modified. NACS's comments had strenuously opposed any such revisions, and we are pleased to report that none have been made.

Some in Congress are considering action aimed at stopping these revisions from taking effect. NACS is actively engaged in those efforts. It is also possible that lawsuits will be filed with the same goal. Nevertheless, you should assume for the time being that the new requirements will take effect as scheduled.

◊ *What Should We Do Now?*

Members who have not already started reviewing the exemption status of employees currently treated as exempt FLSA white-collar employees should do so immediately. A good approach might be to identify first those employees most likely to be affected by the coming changes. Such an evaluation should include at least these steps:

- Identify employees treated as exempt who are paid in whole or in part on a "salary basis" whose weekly or weekly-equivalent salaries are less than $913 (annualizing to less than $47,476). Management should consider whether it will increase these employees' salaries to at least the minimum amount, whether an exception or another FLSA exemption permits exempt status without that step, or whether it will instead forgo exempt status for them and pay them in compliance with the FLSA's overtime requirements.

  Remember that the salary-threshold requirement is not based upon *annualized* salaries. For example, an employee might meet the weekly or weekly-equivalent salary threshold even though he or she started employment during the year, such that the employee's salary payments will not total $47,476 for the year. If the employee otherwise meets the requirements for one of the white-collar exemptions, then he or she will be exempt from FLSA overtime.

- Employers who prefer to take into account what the first "updated" threshold could be might instead use a screening figure of $1,000 per week (annualizing to $52,000), taking into account the White House's estimate that the January 1, 2020 figure might annualize to "more than $51,000."

- Some positions will have incumbents paid both above and below the minimum-salary threshold. Employers who prefer to treat *all* incumbents in a position the same way (that is, those who want to treat all of them as exempt or all of them as non-exempt) must first decide whether they want to treat all of the incumbents as non-exempt, because this leads to a different set of alternatives. Keep in mind that nothing in the FLSA *requires* an employee to be treated as exempt, even if he or she meets all of the exemption tests.

- Once the higher-priority employees have been identified, management should evaluate their status based upon the duties-related portions of the exemption requirements before deciding what to do about their compensation. Outlines and checklists can be helpful in doing this, but usually they are not a sufficient basis for arriving at a final conclusion.

- Identify other employees whose exemption status might be questionable to determine whether to convert them to non-exempt status or to take steps to bolster exempt status.

◊ *What Standards And Principles Apply In Evaluating An Employee's Exemption Status?*

An employee is not exempt from the FLSA's minimum-wage and overtime requirements simply because he or she is salaried or commissioned, or because management thinks of the person as being a manager, or because management sees the person as being important or even indispensable, or because the employee "wants to be" exempt. Instead, there are specific criteria controlling to whom the FLSA's white-collar exemptions apply.

If there is a challenge, it is the *employer's* legal burden to *prove* that *each* exemption requirement is met. DOL and the courts construe exemptions narrowly, and doubt is frequently resolved against the employer. Management must have detailed, accurate, and current information about an employee's job duties before it can adequately evaluate his or her exemption status.

Also, exemption rules apply on an employee-by-employee basis. There's no avoiding the fact that evaluating exemptions based simply upon job descriptions (particularly out-of-date and/or vague ones), generalizations about the work that *groups* of employees do, or conventional wisdom that "everybody" treats a position as being exempt increases the risk that at least some incumbents might not meet all of an exemption's requirements.

Members *should not simply assume* that a white-collar exemption applies to, as illustrations, Store Managers, Assistant Store Managers, Fast-Food Managers, Deli Managers, Floating/Substitute Managers, "Section" or "Team" Managers, Manager Trainees, or central-office administrative employees.

The FLSA's Executive and Administrative white-collar exemptions are typically the ones of broadest interest to convenience-store employers.

## The Executive Exemption

The FLSA's *Executive* exemption applies to an employee:

- Whose primary duty is managing either the enterprise by which he or she is employed or a customarily recognized department or subdivision of that enterprise, *and*

- Who customarily and regularly directs the work of two or more other full-time employees (or the equivalent), *and*

- Who has the authority to hire or fire other employees, or whose suggestions and recommendations as to the hiring, firing, advancement, promotion, or other significant change of employee status are given particular weight, *and*

- Who is paid at least in part on a "salary basis" at not less than the required threshold amount (currently $455 per week, but rising to $913 per week).

Store Managers *might* qualify for this exemption, but, again, one should not *assume* that they do. Employers should thoroughly review the exemption's requirements in light of a *candid* evaluation of a Store Manager's actual day-to-day duties and responsibilities. It is by no means unusual for DOL to challenge an employer's having treated Store Managers as exempt, as have one or more current or former Store Managers who filed their own FLSA lawsuits.

It is conceivable that this exemption might apply to Assistant Managers and similar personnel, but this is a decision to be made with the utmost care and advance analysis.

### The Administrative Exemption

The FLSA's Administrative exemption applies to an employee:

- Whose primary duty is office or non-manual work that is directly related to the management or general business operations of either the employer or the employer's customers, *and*

- Whose primary duty includes the exercise of discretion and independent judgment with respect to matters of significance, *and*

- Who is paid at least in part on a "salary basis" (or the little-used "fee basis", which is highly unlikely to apply in the convenience-store industry) at not less than the required threshold amount (currently $455 per week, but rising to $913 per week).

Because of the vague and ambiguous words and phrases it uses, this might be the most-often erroneously-applied white-collar exemption. Employers should be very careful in evaluating whether it is available.

It is conceivable that the Administrative exemption might apply to Store Managers, Assistant Managers, and similar personnel, but this is a decision to be made with the utmost care and advance analysis. DOL's Office of Enforcement Policy concluded in at least one opinion letter that particular retail Store Managers did not qualify for this exemption.

## The Highly Compensated Variation

A shorter-hand version of the FLSA's Executive or Administrative exemption (or, for that matter, its Professional exemption) is available for certain Highly Compensated employees. It applies to an employee:

- Whose primary duty includes performing office or non-manual work; *and*
- Who customarily and regularly performs at least one exempt duty or responsibility of an exempt Executive or Administrative (or Professional) employee as those terms are defined in the regulations; *and*
- Who is paid at least in part on a "salary basis" at not less than the required threshold amount (currently $455 per week, but rising to $913 per week); *and*
- Whose total annual compensation (including salary, commissions, nondiscretionary bonuses, and other nondiscretionary compensation) is at least $100,000 for now, rising to $134,004.

## The Salary Basis

Each of these three exemptions refers to a "salary basis" of pay. This requirement stands separate and apart from the *amount* of an employee's salary. Instead, its focus is upon *how* the employee is paid.

Generally speaking, payment on a "salary basis" means that an employee regularly receives each pay period a predetermined amount of compensation that is not subject to reduction because of variations in the quality or quantity of the employee's work. Subject to certain exceptions, the employee must receive the full salary for every workweek in which he or she performs any work, without regard to the number of days or hours worked. In most circumstances, salary deductions are not permitted for absences occasioned by the employer or the employer's operating requirements, or for reasons of performance or work quality (such as deducting cash shortages or shrink from the salary).

◊ *Isn't There Also A Commission-Based Exemption?*

The FLSA's Section 7(i) provides an overtime exemption for an employee paid under a *bona fide* commission plan under certain conditions. It applies if:

- The person is an employee of a "retail or service establishment", *and*
- *More than* 50% of the employee's compensation in a documented "representative period" (of at least one month) represents commissions on goods or services, *and*
- The employee's regular hourly rate is *more than* 1.5 times the FLSA minimum wage for a workweek in which he or she works over 40 hours.

In the past, it was not uncommon for convenience-store companies to rely upon this exemption for Store Managers and/or Assistant Managers. Where Store Managers were concerned, some employers even designed pay plans based upon a guaranteed draw against commissions that were intended to provide a basis for asserting *both* Section 7(i) *and* the FLSA's Executive exemption, in case one or the other was challenged someday.

A variety of other legal principles, interpretations, recordkeeping requirements, and other considerations must be taken into account in deciding whether and how to design and implement a pay plan intended to qualify under Section 7(i). But this exemption might provide an acceptable alternative if, for example, the salary-threshold increase or the duties tests pose obstacles to relying upon the white-collar exemptions.

◊ *If An Employee Is Non-Exempt, What Are The Alternatives?*

Employees who will be treated as non-exempt in reaction to DOL's changes must of course be paid in compliance with the FLSA's minimum-wage and overtime requirements. However, this can be done in a number of ways. Some variations include:

- Paying on an hourly basis: This is the most-obvious one. The employee is paid at an hourly rate (of at least the minimum wage) for all of his or her hours worked in a workweek. The employee's pay increases when he or she works more hours and decreases when the employee works fewer hours. Overtime pay is due at 1.5 times the employee's hourly rate.

- Paying on a commission-plus-overtime basis: The employee is paid commissions that are his or her straight-time compensation for all hours worked in the workweek (regardless of the kind or number). Overtime pay is due at 0.5 times the rate figured by dividing the total of the commissions for the workweek by the hours the employee worked in the workweek. The employee's average hourly rate for a workweek can never be less than the minimum wage.

- Paying a salary as straight-time compensation for hours worked up to 40 in a workweek: The employee is paid a fixed amount (equating to at least the minimum wage) for the hours he or she works *up to 40*. Overtime pay is due at 1.5 times the rate figured by dividing 40 into the employee's salary.

- Paying a salary as straight-time compensation for all hours worked in a workweek: The employee is paid a fixed amount for *whatever* number of hours he or she works in the workweek. If he or she works fewer than the expected hours in a workweek, the fixed amount is not reduced (subject to limited exceptions). Overtime pay is due at 0.5 times the rate figured by dividing the fixed amount by the hours the employee worked in the workweek. The employee's average hourly rate for a workweek can never be less than the minimum wage.

These summaries do not and cannot cover all of the potential aspects of, or all of the possible issues or challenges that might be presented by, one of these plans. As an illustration, paying bonuses or

other compensation in addition to the sums described above is virtually certain to affect how much FLSA overtime compensation a non-exempt employee is due.

Neither do these summaries represent all of the alternatives. But it is important to remember that, while there is currently much talk about how DOL's changes will "make employees hourly", it is *not* the case that a non-exempt employee's compensation must be on a by-the-hour basis.

No matter how non-exempt employees are paid, employers cannot be sure that a pay plan is resulting in FLSA compliance in the absence of an *accurate* record of a non-exempt employee's hours worked. Among other things, management must:

- Know everything that counts as FLSA "hours worked";
- Have adequate systems and policies in place for capturing the time *accurately*;
- Train non-exempt employees in what these policies are and how to use the systems;
- Train supervisors and managers to enforce the policies and to ensure that the non-exempt employees use the systems properly and consistently;
- Check to see that the supervisors and managers are doing this; and
- Periodically check to see whether the time records appear to be accurate.

◊ *What Else Should We Be Thinking About?*

DOL's revisions have triggered a multitude of considerations too numerous to list here.

However, one thing to note is that management must take into account the applicable laws, requirements, and prohibitions of *other* jurisdictions. For example, a state's wage-hour laws might not recognize some or any of the FLSA's white-collar exemptions or might not have an exemption similar to Section 7(i); might recognize analogous exemptions only on more-restrictive terms; or might impose specific requirements, limitations, or prohibitions relating to structuring and administering pay plans. Generally speaking, when both the FLSA and another jurisdiction's wage-hour requirements and limitations apply to an employee, the employer must comply with the stricter of the laws, that is, with the one more favorable to the employee.

Also, once management decides what courses of action it will take, it should carefully design a plan for communicating the nature of and reasons for whatever changes will be made. A one-size-fits all approach is not likely to be satisfactory. Instead, the communications should be tailored to the particular employer, to the employees affected, to the changes being made, and to all the other circumstances surrounding what management has decided to do.