

DOL PROPOSAL TO CHANGE STANDARDS FOR MINIMUM WAGE AND OVERTIME PAY IS FAR FROM OVER

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In a recent bold effort to change the Fair Labor Standards Act (FLSA) overtime exemption rules, the Department of Labor (DOL) issued a proposal that would have revamped standards for minimum wage and overtime pay. The proposal would have raised the current salary threshold for qualifying workers, rewritten the tests used to determine whether executive, administrative, and professional employees are exempt from overtime pay rules, and offered lower paid employees greater opportunity for overtime pay while excluding certain higher-paid employees from receiving such compensation. In response to changes in the modern workplace, the Bush Administration proposed a solution in which unambiguous regulatory standards can assist employers and provide employees with what the Administration characterizes as a fair and equitable workplace. Although the Senate just last month defeated the proposed overtime regulations by a vote of 55 to 45, the matter is far from over.

Section 13(a)(1) of the FLSA, codified at 29 U.S.C. 213(a)(1), exempts employees who hold executive, administrative, or professional positions from minimum wage and overtime pay. Since the FLSA does not define these classifications, considerable confusion has resulted in determining who is exempt. Exemptions are recognized, however, when one of three tests is satisfied: (1) an employee is paid a guaranteed salary, not an hourly wage that is subject to reductions because of variations in the quality or quantity of work performed ("salary basis test"); (2) the amount of salary paid meets minimum specified amounts ("salary level test"); and (3) an employee's job duties primarily involve managerial, administrative, or professional skills as defined by the regulations ("duties test"). Though currently in use, the salary basis test has maintained its basic format since 1954, the salary level test since 1975, and the duties test since 1949.

The specific duties and responsibilities of each employee's job, salary, and whether the salary is guaranteed without regard to the quality or quantity of work performed determines whether an exemption applies. With respect to salary levels, the current rules require that most "white collar" employees earn a minimum salary level to qualify for the exemptions. Employees paid below the minimum salary level are not exempt regardless of their job duties. Those paid above the higher salary rate are exempt if they meet the "short" duties test, while those paid between the higher and lower salary rate must meet the "long" duties test. Specifically, the salary required for executive and administrative employees under the current long test is \$155 per week; professional employees are exempt at \$170 per week. The short test salary level for all three exemptions is \$250 per week. Virtually all employees are exempted under the short duties tests because these salary levels have not been adjusted in 28 years. Consequently, these outdated salary tests and complicated duties tests in the current regulation can cause employees to be erroneously classified as exempt, not properly paid, and resentful toward their employers.

In emphasizing the outdated salary levels employed by the current regulations, the DOL has noted that the issue is not whether it should raise the salary levels but by how much. Pursuant to the proposal, the minimum salary level to qualify for exemption from the FLSA minimum wage and overtime requirements as a white collar employee would be increased from \$155 per week to \$425 per week. By replacing the "short test" and "long test" terminology with the newly defined "standard test," approximately the bottom 20 percent of salaried employees would fall below the minimum salary requirement and therefore be entitled to overtime pay. The effects of this standard adversely impact highly compensated white collar employees

if their "primary" duty consists of management, they regularly direct the work of two or more other employees, or have authority to hire, fire, or make recommendations for those actions. It is estimated that about 640,000 high-wage professionals, or those who earn at least \$65,000 a year, would become exempt employees.

**A. EXECUTIVE EMPLOYEES,
SEC. 541.100.107**

In order to qualify as an exempt executive under the current regulations, the long test requires that an exempt executive employee have a primary duty of managing the enterprise, customarily and regularly direct the work of two or more other employees, have authority to hire or fire other employees or have particular weight given to suggestions and recommendations as to hiring, firing, advancement, promotion or any other change of status of other employees, customarily and regularly exercise discretionary powers, and devote no more than 20 percent of hours worked per week to activities that are not directly and closely related to performing exempt managerial work. The short duties test, on the other hand, requires that the employee have a primary duty of managing the enterprise and customarily and regularly direct the work of two or more other employees.

The proposed regulations sought to replace the long and short tests with a single standard duties test. The new standard test consists of the current short requirement plus a third objective requirement from the long test. It provides that an exempt executive employee must have a primary duty of managing the enterprise in which the employee is employed, customarily and regularly direct the work of two or more other employees, and have the authority to hire or fire employees or have particular weight given to suggestions and recommendations regarding the status of other employees.

**B. ADMINISTRATIVE EMPLOYEES,
SEC. 541.200 – .207**

To qualify as an exempt administrative employee under the current regulations, an employee must be compensated on the same salary basis as an executive employee. Among the requirements for the long test, an administrative employee must customarily and regularly exercise discretion and independent judgment. Significant to employers is the reality that the description, "exercise discretion and independent judgment," has generated great confusion and litigation.

The proposed regulations would have replaced such duty with a new requirement that the employee hold "a position of responsibility." In an attempt to clarify foreseeable confusion, the DOL defined the term as requiring an employee to either perform work of substantial importance or perform work requiring a high level of skill or training.

It should be noted that the common goal woven throughout the proposal sought to "reorganize, simplify, streamline, and update the regulations" by implementing objective, plain language, eliminating outdated and uninformative examples, and updating key terms and phrases.

In compliance with this goal, the proposal preserved the definition of "work of substantial importance," which means "work that, by its nature or consequence, affects the employer's general business operations or finances to a significant degree" and supplemented it with a revised list illustrating the types of activities that are generally considered of "substantial" importance for purposes of the exemption.

C. PROFESSIONAL EMPLOYEES, SEC. 541.300.304

Employees may qualify for exemption as a "learned professional" if their primary duty is to perform office or non-manual work requiring advanced knowledge in a field of science or learning, which is customarily acquired by a prolonged course of specialized intellectual instruction or acquired through equivalent combinations of formal education and work experience. Learned professionals have acquired equivalent knowledge and skills through a combination of professional experience, military training, technical school or community college. In recognizing the value of work experience, the proposal emphasized the importance of hands-on training rather than the necessity of structured education. Therefore, the proposed regulations rejected the tendency of satisfying the advanced knowledge requirement with academic instruction rather than work experience for a more expansive definition.

D. ECONOMIC IMPACT FOR EMPLOYERS

The proposal posited that its economic impact includes two components: (1) one-time implementation costs and (2) recurring incremental payroll costs incurred by employers for those employees exempt from overtime under the current rule, who may become nonexempt as a result of raising the salary levels and revising the duties tests. The implementation costs involve the length of time employers would need to comprehend the proposed rule, update and formulate their overtime policies, and notify employees of any changes and other procedural measures. The second part of the implementation costs is the length of time necessary for employers to review employees' job categories in order to assess whether its description should be exempt and how to adjust to the new salary levels and duties tests.

The DOL predicted that employers will choose the most cost-effective compensation adjustment method that "maintains the stability of the work force, pay structure, and output levels." The proposal opined that affected employers would have four choices concerning potential payroll costs: (1) adhering to a 40 hour work week, (2) paying statutory overtime premiums for hours worked in excess of 40 per week, (3) raising employees' salaries to levels required for exemption by the proposed rule, or (4) converting salaried employees' basis of pay to an hourly rate (no less than the federal minimum wage) that results in virtually no additional compensation paid to those workers. Employers would also have been able to change the duties of currently exempt and nonexempt workers to comply with the proposed rule.

E. OVERALL IMPACT OF PROPOSED CHANGES

The proposed changes would have provided significant protection to many employees and employers. The increase of the minimum salary level would guarantee overtime to 1.3 million additional low-wage workers. By updating and clarifying outdated regulatory language, employees would be able to ensure that they are rewarded *quantum meruit* for their work. This concept of employers adequately paying employees should yield a stronger work ethic, greater loyalty, and a higher quality of work product on the part of employees.

Pursuant to a 2001 American Bar Association report indicating FLSA lawsuits have surpassed class-action job discrimination suits, the immense legal fees paid by employers clearly forces them into vulnerable financial position. The proposed regulations would have enabled employers to fulfill their obligations and comply with the law, and allowed the DOL to reduce regulatory red tape and litigation costs. Consequently, businesses would be more likely to stimulate economic growth where updated wage regulations would prevent employers from being hauled into court.

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