The Legal Intelligencer
THE OLDEST LAW JOURNAL IN THE UNITED STATES 1843-2016
PHILADELPHIA, MONDAY, OCTOBER 3, 2016 VOL 254 • NO. 65 An ALM Publication

WAGE AND HOUR

Groups Sue to Enjoin DOL's Final Rule on Salary Exemptions

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Special to the Legal

On May 23, the U.S. Department of Labor (DOL) published in the Federal Register its long-awaited final rule implementing new minimum salary thresholds for the "white-collar" exemptions to the Fair Labor Standards Act's (FLSA) overtime requirements. On Sept. 20, 21 states and the U.S. Chamber of Commerce, joined by numerous business groups, filed separate lawsuits seeking to enjoin the final rule from taking effect on Dec. 1.

BACKGROUND

The most significant aspect of the DOL's final rule more than doubles the minimum salary level for employees to qualify for the executive, administrative, and professional exemptions to overtime pay to $47,476 per year ($913 per week) from the current level of $23,660 per year ($455 per week). The minimum salary amount for the highly compensated employee exemption also was increased to $134,004 per year from $100,000 per year. The final rule permits up to 10 percent of the required salary to be met through payment of nondiscretionary bonus, commission, and/or incentive compensation so long as such compensation is paid at least quarterly. No discretionary payments can be counted toward the 10 percent.

Another key provision of the final rule provides for automatic increases every three years indexed to the average salary levels for full-time employees for the lowest wage region (currently the South), which removes the current obligation to jump through administrative rule-making hoops each time the DOL seeks to increase the salary level.

In the first year, the DOL estimates that 4.2 million workers who are exempt under the current regulations, and who earn at least the current weekly salary level of $455, but less than the salary level of $913 would, without some intervening action by their employers, become entitled to overtime protections under the FLSA, thereby increasing wages owed to these individuals by approximately $1.2 billion per year.

LAWSUIT FILED BY THE COALITION OF STATES

On Sept. 20, 21 states, led by Nevada and Texas and joined by Alabama, Arizona, Arkansas, Georgia, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maine, Mississippi, Michigan, Nebraska, New Mexico, Ohio, Oklahoma, South Carolina, Utah and Wisconsin filed a lawsuit against the


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DOL in the U.S. District Court for the Eastern District of Texas seeking to set aside the final rule. Specifically, the states have asked the court to enjoin the DOL's final rule as unconstitutional and unlawful, as applied to the states. The complaint's challenges fall into three general categories.

First, the complaint alleges that the DOL's Final Rule "relegates the type of work actually performed to a secondary consideration while dangerously using the 'salary basis test,' unencumbered by limiting principles, as the exclusive test for determining overtime eligibility." According to the complaint, this approach runs contrary to the statutory basis for the exemption codified at 29 U.S.C. Section 213(a)(1), which contains no salary basis requirement and instead focuses exclusively on job duties. The complaint further contends that the DOL's decision to permit only 10 percent of the required salary to be met through payment of nondiscretionary bonus, commission, and/or incentive compensation is arbitrary and capricious.

Second, the complaint alleges that the automatic indexing provision flouts the notice and comment requirements of the Administrative Procedures Act (APA) as well as the "statutory command to delimit the exception from 'time to time.'" The complaint cites the DOL's own statement from April 23, 2004, when the "white-collar" regulations were last revised, that adopting such a mechanism was "both contrary to congressional intent and inappropriate." Nevada Attorney General Adam Paul Laxalt added additional color to these allegations by issuing a statement that the automatic indexing provisions are a deliberate attempt to circumvent the APA and ensure that the "pernicious effects" of the final rule persist long after "President Obama leaves office in a few months."

Employers have a multitude of options to mitigate against the potential for increased labor costs attendant with a rise in the salary basis.

The final challenge raised by the states, while fascinating, would not apply to private employers. Specifically, the states contend that the DOL's final rule infringes upon state sovereignty and undermines bedrock principles of federalism by dictating the wages that states must pay their employees, thereby intentionally depleting state budgets in a Machiavellian attempt to "dragoon and, ultimately, reduce the states to mere vassals of federal prerogative."

LAWSUIT FILED BY TRADE ASSOCIATIONS

The states are not alone. The U.S. Chamber of Commerce, joined by more than 50 national and state business associations including the National Association of Manufacturers, the National Association of Wholesaler Distributors, the National Automobile Dealers Association, the National Federation of Independent Business, the American Hotel & Lodging Association, and the National Retail Federation, filed a separate lawsuit in the same jurisdiction, on the same day, also seeking to enjoin the DOL's final rule.

The complaint advances many of the same arguments advocated by the 21 states concerning the primacy of the DOL's salary basis test and the automatic tri-annual increases indexed to the average salary levels for full-time employees.

According to the complaint, the DOL's final rule "defies the mandate of Congress to exempt executive, administrative, professional, and computer employees from the overtime requirements of the FLSA," and raises "the minimum salary threshold so high that the new salary threshold is no longer a plausible proxy for the categories exempted by Congress."

DOL RESPONSE

Secretary of Labor Thomas Perez issued a response in which he lauded the "comprehensive, inclusive rulemaking process" and the "sound legal and policy footing on which the [final rule] is constructed," while expressing an intent to defend the final rule from legal challenges. He further noted that the percentage of nonexempt full-time salaried workers had fallen to 7 percent from 62 percent in 1975.

OUTLOOK

The lawsuits are correct that the FLSA itself does not contain any

reference to a salary basis for the white-collar exemptions. The DOL introduced the salary basis test by way of regulation in 1940 and the white-collar exemptions have been subject to a salary basis test of varying levels ever since. By challenging the "executive fiat" upon which the DOL intends to now use the salary basis as a "litmus test" for determining overtime eligibility, the lawsuits call into question a practice that has existed in some form for over 75 years (albeit a practice that kept the salary level far lower than $913 per week when adjusted to today's dollars). To the extent the DOL might respond that the absence of Congressional action to pre-empt use of the salary-basis test in the past three-quarters of a century evidences legislative approval, the plaintiffs argue that such delegation of power is, itself, unconstitutional because the DOL is acting in a legislative, not a regulatory, capacity. In light of Congress' broad delegation of authority to the DOL, however, the lawsuits face an uphill battle.

Of all of the arguments made in the complaints, the challenge to the automatic indexing provision likely will have the most traction given the DOL's own prior admission that automatic indexing is "both contrary to congressional intent and inappropriate." It is important to note, however, that even if this challenge is successful it would preclude future automatic increases to the salary level but would not prevent the new regulations from taking effect, as scheduled, on Dec. 1.

As to the states' challenge based on federalism, Congress amended the FLSA in 1974 to extend coverage to state governments, and the U.S. Supreme Court thereafter determined that it did not violate the Constitution by doing so. While the complaint argues that subsequent cases decided by the Supreme Court have cast doubt on the continued viability of that earlier precedent (and further that, to the extent it is still viable, it should be overruled), a reversal of position seems unlikely given the current composition of the Supreme Court.

CONCLUSION

If successful as to the core arguments advanced (that the final rule is an impermissible exercise of the DOL's rulemaking authority), the lawsuits would effectively invalidate the DOL's final rule and require wholesale revision of the new regulations. Also, on Sept. 28, the U.S. House of Representatives passed the Regulatory Relief for Small Businesses, Schools, and Nonprofits Act (H.R. 6094), which would delay for six months the implementation of the final rule. The measure, which passed the House with a 246-177 vote (including support from five Democratic lawmakers), now heads to the Republican-controlled Senate, but could be derailed by a Presidential veto.

Notwithstanding the filing of these two legal actions, and the pending legislation, employers should continue to proactively assess their current pay practices to determine the operational and financial impact of the DOL's final rule. In most cases, that means exempt employees' salaries must be increased to meet the revised salary basis, or that such employees will become nonexempt and therefore overtime eligible.

Employers have a multitude of options to mitigate against the potential for increased labor costs attendant with a rise in the salary basis, including considering changes to staffing or salary levels, more closely monitoring hours worked, or hiring additional workers such that there is sufficient coverage to avoid overtime costs. Because many possible strategies available to employers (and financial forecasting/budgeting to address increased overtime expenses) take time to conceive and implement, and because a stay of the final rule's effective date is speculative at this point, organizations would be well advised to assess the impact of the anticipated final regulations on their businesses now. •