

**Observations on the Department of Labor's Final Regulations
"Defining and Delimiting the [Minimum Wage and Overtime] Exemptions for
Executive, Administrative, Professional,
Outside Sales and Computer Employees"**

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Forward

About the Authors

John Fraser served as Deputy Assistant Secretary for Employment Standards in the U.S. Department of Labor (USDOL) from 1987 to 1990, and as Deputy Wage and Hour Administrator from 1990 through 2000. Monica Gallagher served as Associate Solicitor for Fair Labor Standards in the USDOL from 1985 to 1995. Gail Coleman served as Counsel for Trial Litigation, Fair Labor Standards, in the USDOL from 1982 to 1986, and as Deputy Associate Solicitor for Fair Labor Standards from 1986 to 2002. In these capacities, working for both Republican and Democratic administrations, we gained considerable collective experience in administering the Fair Labor Standards Act (FLSA), including Section 13(a)(1), which provides an exemption from the Act's minimum wage and overtime provisions for *bona fide* executive, administrative, professional, and outside sales employees, and employees in certain computer-related occupations. All of us are retired from the USDOL.

Neither Mr. Fraser nor Ms. Coleman has worked on FLSA-related matters since retiring from the Department, though Ms. Coleman is currently engaged as Senior Editor of a treatise on the Family and Medical Leave Act. Ms. Gallagher was engaged as Senior Editor in the production of the treatise *The Fair Labor Standards Act* (Kearns, Bureau of National Affairs, 1999) and continues as Editor-in-Chief of the annual Cumulative Supplements to that volume. She also has served as a consultant on FLSA matters to attorneys representing both employers and employees.

Purpose

We were asked by the AFL-CIO to conduct an independent review of the USDOL's final regulation (69 FR 22122, published on April 23, 2004) revising the criteria for the Act's Sec. 13(a)(1) exemptions, and to report our assessment of the changes made.

None of us were involved in any way in the development of the Department's rulemaking proposal (68 FR 15560, published on March 31, 2003) or in the development of the final rule although, of course, we were aware that these activities were occurring.¹ Nor have we sought any "inside information" from former colleagues (or others) regarding the

¹ One of the authors, Ms. Gallagher, did submit comments on the Department's proposed rule.

rulemaking proposal or the considerations and decision-making involved in promulgating the final rule.² None of us have previously done any work for the AFL-CIO or any of its affiliated unions on this or any other matter.

The observations contained in this paper are truly independent; they represent our collective, consensus views, not those of the AFL-CIO or any other organization or party. This was the essential condition of our agreeing to undertake this effort. Nonetheless, the reader will discern (and we readily acknowledge) that all of us are fervent supporters of the purposes of the FLSA and firm believers in the crucial mission of the Department of Labor to promote and protect the interests of working people and working families in their inherently unequal relationships with their employers.³

We should note that we did not set out to conduct a comprehensive analysis of the final rule as if we intended to provide comments to the Department in the (now completed) rulemaking process. Rather, we have limited our review and the following observations, comments and criticisms to what we regard as significant issues about which we believe we may have some useful understanding and insight. There are important parts of the final rule, such as the regulatory and economic impacts analyses, that we have not tried to penetrate and where any commentary occurs at the most general level.⁴

² We are, of course, aware of some of the positions taken by the AFL-CIO in commenting on the Department's proposed rule because we have reviewed the Preamble to its final rule, where at least some of the institution's comments are reported and discussed. We have also reviewed testimony before Congress on this subject given by the Department and other interested parties, including the AFL-CIO.

³ Some readers of this paper, especially those unacquainted with us, may come to perceive that we are myopic anti-modernists, simply stuck in the past and opposed to change on any grounds. That is not who we are. We hope readers will appreciate that we recognize that the existing rules do, indeed, have problems, some quite serious, that need to be addressed and resolved. At the same time, we believe that the fundamental concepts and principles which shape and underlie the structure of the existing regulations are as valid today as they were when the rules were originally formulated. Furthermore, as discussed later, we simply cannot accept the notion - explicitly stated by the Department in the Preamble to its final rule - that the Department's past failure to update the three decade old salary level test can justify or excuse such fundamental conceptual and structural changes in the regulatory framework as the Department would effect. It is not nostalgia for the old rules, but rather our considered judgment that the new rules fail to distinguish well between the employees Congress intended to cover under the FLSA and those it intended to exempt, that has led us to the conclusions we set forth here.

⁴ In addition, we did not undertake any effort to review the final rule vis-à-vis the Department's March 2003 proposal (though there are some changes from the proposed to the final rule noted in our comments), but rather focused on the final rule vis-à-vis the existing regulations.

Finally, we wish to state our great and abiding affection, respect and profound admiration for the many career staff in the Department - especially in Wage and Hour and the Solicitor's Office - who no doubt worked, as they always have, with great talent, intensity and integrity on this rulemaking. We have at least some appreciation of what was involved in the rulemaking process, and commend them for their immense accomplishment. The views expressed in this paper are in no way intended to denigrate their remarkably valuable talents and continuing contributions to the welfare of America's working people and families. Any misunderstandings or errors in the following observations and commentary are entirely our responsibility, and we hope that our esteemed former colleagues - while they may well disagree with some or all of our views - do not perceive that our comments or criticisms are unfair, ill-intentioned, or directed to their efforts, and recognize our deep and undying respect for them.

Observations and Commentary

Importance

The FLSA provides extremely important protections for working people and families in our country. Section 13(a)(1) of the Act gives the Secretary of Labor very broad authority to "define and delimit" - through rulemaking - what has come to constitute by far the largest exception to (exemption from) the minimum wage and overtime protections otherwise afforded by the law.

In enacting the FLSA, the Congress did not undertake to delineate the contours of the Sec. 13(a)(1) exemptions,⁵ rather granting the Secretary broad authority - within certain limits - to do so through rulemaking. This approach may have been due in part to the complexity of the issues involved in operationally defining the named occupational categories (as continues to be evidenced by the recently completed rulemaking); to the recognized need to undertake careful workforce analyses (which we do not see evidenced in this rulemaking) to make reasonable, informed judgments about the proper definitional scope of the exemptions; or, to the perception that those who would qualify for the exemptions at that time constituted a relatively small portion of the national workforce⁶ whose jobs were readily distinguishable from the much larger portion of jobs to which the Act's provisions would apply.

⁵ The Congress did, however, precisely define other "special-interest" exemptions from the Act's minimum wage and overtime requirements in Sec. 13(a) or the overtime requirements in Sec. 13(b). In addition, in 1990 and 1996, Congress enacted legislation which specifically exempted certain computer-related occupations (the 1990 legislation required the Department to do so through its rulemaking authority under Sec. 13(a)(1)).

⁶ It should be noted, however, that the number of workers exempted from the FLSA's minimum wage and overtime protections under Sec. 13(a)(1) has always been large relative to the other Sec. 13 exemptions.

In any case, over the ensuing years, as the U.S. economy has evolved, the potential scope of the Sec. 13(a)(1) exemptions has grown very substantially and now potentially affects a majority of the U.S. workforce. As explained in Appendix I, if we correctly understand the Department's own estimates (from the final rule's economic impact analysis), nearly 72 million people - or more than one-half (53 percent) of the entire U.S. workforce - work in occupations that, based on job title alone, might qualify for exemption under Sec. 13(a)(1). So, redefining the scope of these minimum wage/overtime exemptions is indeed a "very big deal." Because these regulations potentially affect more than half the entire U.S. workforce, they have potentially huge ramifications for workers' earnings, business costs, job creation and retention, and the health of the U.S. economy. (It is, however, outside the scope of this review - and our competence - to estimate the proportion of this population whose compensation is likely to be affected by the Department's changes to the regulations through the loss (or gain) of overtime pay.)

It is largely because of that significance, combined with the variety, intensity and divergence of interests involved, that the Department failed, in the last 30 years, to overcome the many obstacles which met its efforts to update these rules and thus shirked its important responsibility to do so. The rules now being replaced were adopted during the Nixon and Ford administrations. The Carter administration proposed and adopted modifications to the "salary level" test in 1980, but the effective date of those modifications was "deferred" pursuant to a Presidential Directive of the newly-elected Reagan administration, and they were never implemented. Despite extensive staff work and further proposals for revision in subsequent years, none of these rulemaking efforts ultimately came to fruition. Both the Reagan and Bush I administrations declined to move ahead with, even then, long overdue rulemaking (though the Reagan Labor Department issued an "Advance Notice of Proposed Rulemaking" in 1985).⁷ And, despite earnest and persistent attempts by the Wage and Hour Administrator during the early 1990s, the Clinton Labor Department declined to undertake rulemaking or public hearings, though it was strongly urged as the single most important and necessary, if predictably controversial, step that could be taken to protect U.S. workers from the ongoing erosion of their workplace rights. One important consequence of this long period of inaction is that one of the critical components of the regulation in effect when the current Bush administration took office had become so outdated as to be quite simply ludicrous: the weekly salary amount required to meet the test for exemption as an "executive" employee was less than the minimum wage for a 40 hour work week.

Consequently, we applaud the Labor Department - and Secretary Chao and former Wage and Hour Administrator McCutchen in particular - for their courage, fortitude, and persistence in undertaking and completing this rulemaking. The Department and its staff deserve great credit and

⁷ The first Bush administration undertook a rulemaking to revise the "salary basis" regulations as they affect public sector employees.

appreciation - despite our serious concerns, reservations and criticisms with respect to what they've done in the rulemaking - for doing something to stop the extremely deleterious effects of the erosion of workers' rights through what can only properly be called the negligence of three prior administrations. We thank the Department for this accomplishment.

Some readers of this entire paper may, no doubt, be tempted to accuse us of "damning with faint praise." Nothing could be farther from the truth. We do know too well, from first-hand experience, how extremely difficult, contentious, risky, controversial, and vexing this rulemaking must have been. We know too well how complex the many and varied issues are; how interrelated and potentially contradictory they are; how rife with problems, inconsistencies, and troublesome, clumsy, vague or ambiguous language the old (as of this writing, still effective) regulations are; how these problems have been exploited and the purpose and intent of these regulations misunderstood by some courts; and, how strongly held and utterly incompatible and irreconcilable are interested parties' views on many of the issues that must be confronted. We do have, and will describe, serious concerns about and criticisms of the substance of the Department's rulemaking, but we fully recognize and appreciate that something had to be done, even if merely to provoke an ongoing debate about the "right" outcome of this rulemaking and future action to that end. For doing something, the Department deserves - and from us gets - an honest and hearty "Bravo"!

This said - that doing something was extremely important and may ultimately prove beneficial in the short or long terms - we are of the view that an assessment of what has been done can't stop there; that doing something should not mean that doing anything is acceptable.⁸

⁸ In this regard, we are of the view that it would be inappropriate to assess what the Department has done in its rulemaking from the perspective - which seems to have infected many - that it's "not as bad as it could have been." Indeed, some observers seem to believe that in March 2003 the Department cynically put forward an extremely one-sided - employer-friendly, worker-hostile - rulemaking proposal with the foreknowledge that it would be politically unsustainable and that subsequent retreat from its more extreme proposals would have the result of making the final rule look positively moderate. We neither subscribe to that view nor believe that the Department could have been quite so Machiavellian in its public conduct. Rather, we accept that the Department's rulemaking proposal was made in good faith, even if naïve and, in our view, in many ways quite extreme.

We also do not subscribe to the view that the rulemaking process, and its ultimate outcome, can or should be properly evaluated based merely on a balancing of interests - a scorecard of winners and losers; of how many comments from various and contending interested parties were accepted and accommodated, ignored or refuted. This kind of scorecard is fundamentally vacuous - it rarely conveys anything meaningful about the fairness or propriety of a rulemaking outcome.

We should also note that we are not equipped to assess this rulemaking in the broader context of the effects on U.S. workers and their families of the Bush Administration's (or its Department of Labor's) other economic and workforce policies, though this rulemaking indisputably constitutes an important economic policy decision with potentially far-reaching consequences. How its effects should be considered in parallel with other economic/workforce policies (such as

Our substantive comments on and criticisms of this extremely important rulemaking are, therefore, based on an assessment - from our own experience and admittedly personal, professional perspectives - of the extent to which the Department has achieved a reasonable, coherent, and fundamentally fair rulemaking outcome consistent with its core mission to promote and protect the interests of U.S. workers and their families.

Unfortunately, based on the discussion that follows, we have concluded that in its new rule - while adjusting the compensation level required for exemption to a more realistic amount - the Department has:

- moved the line of demarcation between those employees protected by the FLSA and those who are exempt substantially in the direction of exemption, so that more classes of workers, and a greater proportion of the workforce overall, will be exempt than we believe the Congress could have originally intended;
- removed existing overtime protection for large numbers of employees currently entitled to the law's protections;
- failed to restore the overtime protections intended by the FLSA to large numbers of workers who would have been protected if the "salary level" requirement had not been so substantially eroded over time (and the Department's previous negligence);
- failed to make needed substantive revisions to the rules to provide overtime protection to the kinds of workers the Act was intended to protect;
- failed to establish reasonable and clear criteria for determining which workers are *bona fide* executive, administrative, professional, and outside sales employees whom the Congress intended to exempt from the protections of the minimum wage and overtime laws; and,
- failed to protect and promote the interests of working people in the United States consistent with its core organizational mission.

Further, in our view, the Department has written rules that are vague and internally inconsistent, and that will likely result in a profusion of confusion and court litigation - outcomes that the Department explicitly sought to avoid.

As a result, we believe that (with the exception of the change in the salary level test) the interests of U.S. workers and their families will

tax cuts and changes, for example, in safety and health regulation) and economic conditions is well beyond the scope of this review and our abilities.

not be advanced - indeed will be harmed - by the implementation of these new regulations.⁹

The Department has articulated, in the Preamble to its final rule, an extremely broad view of the extent of its authority and discretion under Section 13(a)(1), and we do not on the whole disagree. Congress has given the Department very wide, but not unlimited, rulemaking authority in this area, consistent with the underlying purposes of the Act. While there are questions yet to be resolved as to the farthest reach of the Department's authority,¹⁰ we offer no objection to the rules on these grounds.

It is, rather, how the Department has chosen to exercise its Congressionally-sanctioned authority that, in our view, raises very serious concerns about whether the interests of U.S. workers and their

⁹ Some readers might protest that our analysis ignores the "big picture." The Department contends that the extremely difficult rulemaking decisions reflected in the final rule will, ultimately, have minimal overall economic impact. Though there will certainly be some workers who gain minimum wage and overtime protection, and some who lose it, some who read this paper may contend that minimal economic impact is the best possible outcome from this rulemaking, and entirely consistent with the Department's core mission to promote and protect the interests of U.S. workers and their families. That is because no potential for economic disruption in any sector or region means no potential adverse effect on economic growth, job creation and retention, etc. which is - in this view - the foundation on which workers' interests lie. (This perspective, of course, assumes economic disruption arising from higher wage costs to employers, but largely ignores any economic impetus that might well derive from higher earnings by employees, as consumers and savers.)

We are certainly in no position to evaluate or contest this macroeconomic argument, but we believe that we can see quite clearly how and where the Department's final rule will predictably result in loss of minimum wage and overtime protection, and the important income derived from overtime pay, for whole categories of workers now so protected. Many U.S. workers and their families simply don't operate at the "macro" level - they have to find the means to feed, house, clothe, transport, educate, and care for their families every week. Workers who lose up to one-quarter of their income (and may still be required to work excessive hours to keep their jobs) will find little solace or satisfaction in hearing that some workers someplace else may have experienced an increase in their base pay (to maintain exempt status), or started getting paid overtime (if still required to work more than 40 hours a week), or had their hours cut back (to 40 hours per week to avoid overtime pay) - any more than they are likely to derive satisfaction from learning that the closing of their plant and loss of their job resulted in job gains for Mexican, Indian or Chinese workers and, perhaps, somewhere else in the United States in the transport or import sectors.

¹⁰ For example, in the new Sec. 541.601 (discussed further below), the Department deems exempt any employee with total annual compensation of at least \$100,000 if the employee "*customarily and regularly performs any one or more of the exempt duties of an executive, administrative or professional employee.*" Whether the Department's authority to define and delimit the categories of exempt employees reaches this far has, of course, not been determined.

families are protected and promoted through this rulemaking. With the exception of the salary level adjustment, to be addressed shortly, it is our conclusion - based on the information and analysis presented below - that in every instance where the Department has made substantive changes to the existing rules (and the overall conceptual underpinnings of the regulatory framework),¹¹ it has weakened the regulatory criteria for, and thereby expanded the reach and scope of, the Sec. 13(a)(1) exemptions. Further, as the following observations will explain, the Department's final rule also:

- Lacks coherence because, while it articulates general principles regarding how the exemptions should be applied, it then ignores or distorts those principles in declaring that certain occupational categories qualify for exemption.
- Uses court cases construing the old regulations contrary to the Department's own interpretations as the justification for making changes that significantly expand the exemptions, in derogation of its responsibility to develop rules in accordance with its view of the appropriate scope of the exemptions.
- Fails to achieve the Department's own stated goals to "*simplify, clarify and better organize the regulations ...*" The Department goes on to state that, "*Rather than broadening the exemptions, the final rule will enhance understanding of the boundaries and demarcations of the exemptions Congress created.*"¹² In fact, it is our view that the Department did just the opposite - broadening eligibility for exemption without substantially clarifying the rules. Further, its rule creates new ambiguities that will invite litigation.

The Department itself only seems to contend that worker protections are strengthened by this rule through two of its changes. These changes, as will be discussed further, are:

- (1) the increase to the "salary level" required to qualify for some of the Sec. 13(a)(1) exemptions; and,
- (2) the requirement that to qualify for exemption as an "executive," an employee must "*have the authority to hire or fire other employees or have particular weight given to suggestions and recommendations as to the hiring, firing, advancement, promotion or any other change of status of other employees.*"¹³

¹¹ As well as in many instances where the Department purports not to have made substantive changes.

¹² Preamble p. 22125.

¹³ In this regard, the Department also claims that its final rule "*is more protective for police officers, fire fighters, paramedics, emergency medical technicians, and other first responders*" (Preamble p. 22192), but the basis for this claim is somewhat confusing. The Preamble goes on to say that, "*The Department has no intention of departing from ... established case law*" (Preamble

At the same time, the Department effectively concedes that protections are weakened - and the scope of exemptions broadened - in all other cases. This concession is not made explicitly, but can be discerned from the Regulatory Impact Analysis accompanying the final rule.¹⁴

In our view, only one of the two changes that the Department claims strengthen workers' overtime protection has any substantive impact - the very long overdue change in the qualifying "salary level" test.

p. 22195) finding that such employees do not qualify for the executive, administrative, or professional exemptions. Thus, the Department seems to be saying that its final rule merely reflects current law, and is therefore not really "more protective" of these categories of employees, except perhaps in those court jurisdictions that have decided differently. The Preamble continues, "*Moreover, some police officers ... [etc.] treated as exempt executives under the current regulations may be entitled to overtime under the final rule because of the additional requirement in the standard duties test ... that an exempt executive must have the authority to 'hire or fire' [etc., as per (2) above] ... Therefore, the Department concludes that the executive duties tests for police officers ... [etc.] in the final rule is [sic] more stringent than the current short tests and some such workers may actually gain overtime protection. However, this number is too small to estimate quantitatively...*" (Preamble p. 22195, emphasis added). If we understand its rationale correctly, the Department seems to be saying that its final rule "is more protective for ... first responders" solely due to the change in the duties tests for the executive exemption [as per (2) above], and not on any other basis.

¹⁴ In analyzing the effect of its changes to the criteria for the various exemptions, the Department states that it "*has concluded that the standard duties test for administrative employees [as one example] in the final rule is as protective as the current short test. Therefore, the Department has determined that very few, if any, workers will lose their right to overtime as a result of updating the current short test with the final standard duties test. However, this number is too small to estimate quantitatively given the data limitations...*" (emphasis added). Essentially the same language is used in discussing the administrative, learned and creative professional, and outside sales exemptions. (With respect to employees in computer-related occupations, the Department says it, "*concludes that it is unlikely that any additional employees will lose overtime protection*" as a result of its changes in the final rule.)

It should be noted, however, that - despite the foregoing - the Department also claims that, "*On the whole, employees [earning between \$23,660 and \$100,000 per year] will gain overtime protection because some revisions are more protective than the existing short duties tests. However, this number is too small to estimate quantitatively*" (emphasis added). (Preamble p. 22192) We cannot see how this could be the case, as we demonstrate below.

Moreover, what is unsaid is that if the Department had not discarded the essential regulatory structure of the existing rules (eliminating the "long" test concept and very substantially diluting the existing "short" test criteria for higher paid employees), a very large number of employees would have had their right to overtime restored by any updating of the rule's salary level. Only a fraction of the employees who have become exempt only through the erosion of the salary level over the past 30 years will be returned to nonexempt status through the new rules.

Salary Level Test

In its final rule, the Department raises the minimum weekly salary level required for exemption (where this requirement applies¹⁵) to \$455 per week, or \$23,660 per year.¹⁶ This is a \$300 per week increase from the current minimum salary requirement of \$155 per week established nearly 30 years ago for those employees subject to the "long" (more stringent) duties tests. As some commenters point out, this amount is well below the level which would have resulted from simply adjusting for inflation.¹⁷

Nonetheless, the Department contends that the methodology and criteria it used to decide upon this amount (\$455 per week) to qualify for exemption are at least roughly comparable to those used by the Department in the past.¹⁸ While some commenters dispute the Department's contention that *"its methodology is consistent with the regulatory history and ... is a reasonable approach to updating the salary level test"*, we have chosen not to examine this question. We note, however, the methodology's (historical and) inherent "lowest common denominator" approach¹⁹ and the Department's decision to avoid providing *"some mechanism for regular*

¹⁵ The "salary level" test does not apply to teachers, doctors, lawyers, and outside sales employees. For the first time, this rule also removes the "salary level" requirement for employee-owners with at least a 20 percent ownership stake in the business.

¹⁶ It should be noted that about two-fifths (42 percent) of all wage and salary workers (excluding the self-employed) in the U.S. earn less than \$455 per week; 55 percent earn between \$455 and \$1,923 per week (or \$23,660 to \$100,000 per year); and, 3 percent earn more than \$100,000 per year. Source: CPS Outgoing Rotation Group.

¹⁷ See Preamble pp. 22165 and 22167. The inflation-adjusted amount for employees subject to the "long" (more stringent) duties tests in the current rule, according to commenters, would be \$530 (or \$580 for the professional exemption) per week, but the Department has largely abandoned the "long" test concept in its final rule. Thus, as the Department seems to concede, the comparable inflation-adjusted amount for employees subject to the "short" (more lenient) duties test - which are generally the tests carried forward in the final rule - would be \$855 per week, or nearly \$45,000 per year, an amount nearly twice as high as that adopted by the Department (\$455 per week).

It is also worth noting that the value of the minimum wage has also been severely eroded by inflation over the last two decades.

¹⁸ See Preamble pp. 22165 - 22171.

¹⁹ As the Department states, *"A minimum salary level of \$455 per week represents the lowest 10.2 percent of likely exempt employees in the lower-wage retail industry; the lowest 8.2 percent of likely exempt employees in the South; and the lowest 6.7 percent of all likely exempt employees."* This amount *"also represents the lowest 20 percent of salaried employees [that is, as the Department uses the term, those not reported to be paid hourly] in the retail industry; the lowest 20.2 percent of salaried employees in the South; and the lowest 16.8 percent of all salaried employees"* in the U.S. (Preamble p. 22171)

review or updates [of the salary level test] at a fixed interval, such as every five years."²⁰

We believe strongly that adjusting the salary level test through this rulemaking provides no legitimate basis for weakening other existing eligibility criteria, which is just what the Department has done. This adjustment in the salary test level only begins to restore overtime protection that has been lost to inflation through the Department's own dereliction over nearly three decades. This accomplishment - while extremely important and beneficial - simply cannot warrant or in any way justify the weakening of other eligibility criteria as, indeed, the Department has done throughout the final rule.

Regulatory Structure and Generally Applicable Criteria for Exemption

We have already mentioned in passing the structural differences between the existing rule and the new rule replacing it. To clarify the significance of the technical and sometimes arcane differences which lead us to our conclusions that workers' interests have not been appropriately served, we first here set forth a non-technical overview of the rules which have been in effect until now, so that the differences brought in with the new system can be appreciated.

The old rules provide that one would recognize an exempt employee by finding three marks: (1) a certain kind of duties; (2) a certain level of pay; and, (3) a certain method of being paid.²¹ The method of payment is a relative constant: exempt employees are paid "on a salary basis."²² Thus hourly-paid employees are quickly eliminated from consideration as possibly exempt.

²⁰ The Department states that it "intends in the future to update salary levels on a more regular basis, as it did prior to 1975, and believes that a 29-year delay is unlikely to reoccur" in the future. Without some greater understanding of the basis for this Departmental optimism, we are - at best - highly skeptical of whether such confidence and belief can be justified.

²¹ Here is how the Department explains these three tests in its Preamble: "The existing Part 541 regulations generally require each of three tests to be met for the exemption to apply: (1) The employee must be paid a predetermined and fixed salary that is not subject to reductions because of variations in the quality or quantity of work performed (the 'salary basis test'); (2) the amount of salary paid must meet minimum specified amounts (the 'salary level test'); and (3) the employee's job duties must primarily involve executive, administrative or professional duties as defined by the regulations (the 'duties tests')." (p. 22124)

²² Some professional employees can also qualify for exemption if paid on a "fee" basis. For convenience, these two different methods - salary basis and fee basis - are together denominated "salary basis" in this discussion.

As to the other two requirements, they were looked at as interacting. Originally there was a single "salary level" (compensation amount) test²³ and a single duties test, the predecessor of the current "long" (more stringent) duties test. The name "long" test came into use after 1949, when the Department added a much more lenient "short" duties test for employees who were paid what the Department considered "a lot of money."²⁴ For such employees, it thought, the examination of their duties could be quite lenient. For most employees a relatively exacting test of duties, as set forth in the "long" duties tests, was retained so that the nonexempt in this compensation range would not be deprived of the overtime pay to which they were entitled.

The new rules leave the overall three-mark structure in place, but - even while retaining much of the language of the old rules - they significantly change each piece of the structure.²⁵

Under the new rules, the changes in the tests of payment "on a salary basis" may seem among the least momentous, but they are nevertheless quite significant. The old rules and the new basically state that to be paid on a salary basis a worker must receive a guaranteed amount of compensation each week if he or she does any work during that week, regardless of the quality or quantity of the work performed, with specified exceptions. Certain deductions from the guaranteed amount are explicitly permitted and certain others explicitly prohibited. Under the old rules, disciplinary deductions for a period of less than a week (except for violations of "safety rules of major significance") defeat the exemption; they are not allowed, as inconsistent with the "salary basis" of payment. Under the new rules, disciplinary deductions for infractions of any workplace conduct rules for periods of a single day or more will be permitted so long as they are made pursuant to a written policy applicable to all employees. The guaranteed weekly salary will,

²³ And those employees paid less than the "salary level" threshold amount also could be quickly eliminated from consideration as possibly exempt.

²⁴ Thus the Weiss Report (June 30, 1949), p. 23, explains: *"It has been the experience of the Divisions, and this experience is supported by the evidence at the hearing, that with only minor or insignificant exceptions, persons who earn salaries of \$100 a week or more and who have as their primary duty the performance of work which is characteristic of employment in a bona fide executive, administrative or professional capacity, as the case may be, meet all of the requirements of the Administrator's basic definitions of exempt employees, including the requirements with respect to nonexempt work. The combination of monetary and qualitative requirements assures the exclusion from the provisos of persons who are not employed in bona fide executive, administrative or professional capacities."*

²⁵ Through this rule, the Department has now effectively eliminated the original concept of the "long" duties tests; applied the less stringent "short" duties tests to employees paid between \$23,660 and \$100,000 per year; and, made the duties test applicable to the highest paid employees (\$100,000 or more) much less stringent than even the old "short" duties test. Contrary to the Department's characterization of its changes to the regulatory framework, these are, indeed, fundamental and profound conceptual and structural changes.

accordingly, be subject to reduction (without effect on the exemption) for a much wider range of conduct, and potentially far more often, than before. This certainly expands the scope of the exemption, making more people exempt than under the existing rules.

Also, as discussed in greater detail in Appendix II, the changes made in the final rule regarding the "window of correction" - the rules for evaluating the effect on exempt status when deviations occur from strict compliance with the "salary basis" requirements - very significantly reduce the burden on employers to prove that the compensation paid employees is actually a "salary." One of the most significant of these changes is a narrowing of the scope of the inferences which can be drawn from proven improper deductions. The new rule restricts the conclusions to be drawn from such improper deductions to those employees who have the same supervisor as the affected employee, thus substantially increasing the burden to show that a large group of employees is paid otherwise than "on a salary basis." Similarly, the addition of a "safe harbor" (at §541.603(d)) for employers claiming to pay employees "on a salary basis" will make it substantially more difficult for employees to demonstrate that the regulations have not been complied with. The effect of these changes is to substantially reduce potential employer liabilities. The Department also reveals its intent to broaden the availability of the exemptions by its addition to the rule of a new exemption-saving concept: instead of reasserting its historic view that the burden of proving any exemption falls strictly on the employer claiming it, the new rule provides that the provisions regarding the effect of improper deductions from salary "*shall not be construed in an unduly technical manner so as to defeat the exemption*" (emphasis added).²⁶

As to the salary amount necessary for exemption (discussed above), the Department has represented that it followed a methodology similar to that employed in the past when salary level changes were effected in the rules. Assuming for the moment, for the sake of underscoring a more important point, that this contention by the Department is correct, it is essential to note that the amount used by the Department for the new "standard test" (\$455 per week, or \$23,660 per year) is comparable to the lower amount of the two used under the old rules - the amount, that is, used when the duties test to be applied is the more stringent "long" test.²⁷

The new rules, like the old, relate the degree of rigor of the examination of an employee's duties to the amount of the employee's compensation, but - as in a game of three-card monte - the trick here is keeping one's eye on positioning. The old, more robust "long" tests of duties - the tests which would have been applicable to many low- and moderately-paid employees - have virtually disappeared! Under the new rules, employees paid between \$23,660 and \$100,000 per year are judged under a test modeled on the old, less stringent "short" duties tests, the

²⁶ Sec. 541.603(e).

²⁷ Preamble p. 22123 ff.

tests used for those highly-compensated employees whose duties did not need to be examined so carefully. By this mechanism the Department can perhaps persuade a casual reader that the new test preserves duties tests similar to those previously in effect, while quite appropriately raising the amount of compensation required before an employee can be considered exempt. In fact, however, the Department's new rule expands the classes of exempt employees by applying, for the vast majority of workers, a rule matching a variant of the old "easy" duties with the new "low amount" salary. And - *presto!* - the worker finds a walnut shell with no overtime under it, and the employer is now able to qualify many more employees as exempt than the existing regulatory structure ever contemplated.

Consistent with this change in structure, the new rules also modify and weaken the test of what constitutes an employee's "primary duty." In the current rule this is at least in part an objective determination, requiring examination of all the relevant facts but taking into account the time spent by the employee at various duties and using, as a "rule of thumb," the notion that an employee typically would devote at least 50 percent of his or her working hours to the tasks deemed to be "primary." The Department asserted (but was unable to prevail in advocating) that this objective comparison of the time spent performing exempt and nonexempt work should be applied to determining the primary duty of certain assistant managers (who were paid more than \$250 per week) of Burger King establishments in the litigation of that name, and its defeats in that litigation resulted in the use of a "most important duty" test standard by other courts.

The Department now embraces the "most important duty" principle, rather than resisting it as it had previously.²⁸ It is our view that this abandonment of the objective percentage test for determining primary duty constitutes a grievous loss. On the one hand, employees allocate time among their various duties because (and to the extent that) they are doing what the employer wants and directs them to do. Thus, an assessment of how much time employees actually spend performing their various duties contributes concrete evidence about which duty is indeed "primary." On the other hand, an employer, if called upon to state which of several duties²⁹ of an employee is primary, will likely choose the one which results in the employee's exemption from the requirements of the law (thereby effectively reducing labor costs); and, of course, the courts can be expected to defer to the employer's characterization. Moreover, no disrespect intended, judges - whose job is decision-making - may well be more likely to find any decision-making an employee is

²⁸ Given its resistance to this position in the past, it is indeed ironic that the Department now states that it, "... continues to believe that this case law [citing *Burger King* and subsequent similar decisions] accurately reflects the appropriate test of exempt executive status and is a practical approach that can be realistically applied in the modern workforce, particularly in restaurant and retail settings." Preamble p. 22137 (discussion of Sec. 541.106.

²⁹ It is a truism that almost all workers actually have a variety of duties in their job, however mundane.

authorized to do to be much more important than the cooking of hamburgers or the brewing of lattes, even if 90 percent of the employee's time is spent cooking or brewing.

Those are some of the generally-applicable changes which will now govern the testing of exemption under the new rules with respect to low- and moderately-paid employees.

And what kind of a test will now be used for testing the exemption of more highly paid employees? Here a truly new standard has been devised. Under the new rule, a highly paid employee will be deemed exempt if he or she "*customarily and regularly performs any one or more of the exempt duties of an executive, administrative or professional employee.*" The Department has defined the phrase "customarily and regularly," and its definition is weak indeed: that phrase means only, according to the new regulation, with a frequency "*greater than occasional.*"³⁰ While it is impossible to forecast precisely what may emerge in the construction of this language, it may well be that regular performance of the duty for not just one afternoon a week, but one day a month or even one day a quarter, would be sufficient.³¹ Since only one exempt duty is required - say, for example, the direction of the work of two other employees - a small rearrangement of employees' duties could make virtually an entire workforce of highly paid employees exempt.

Thus difficulties would exist with respect to the highly-compensated employee exemption test even if the entire \$100,000 had to be paid "on a salary basis," as the amount for "short" test employees must be under the current rule. But the Department has added other new provisions which will make it far easier for an employer to qualify employees for exemption on the basis of the employer's own economic interests. These are the "topping up" provisions at 29 C.F.R. Sec. 541.601(b)(2)-(4). The rule first provides in Sec. 541.601(b)(1) that the \$100,000 high test amount includes "*commissions, nondiscretionary bonuses and other nondiscretionary compensation earned during [an employer-selected] 52-week period.*" Then it continues with the "topping up" provisions, which state that "*if the employee's total annual compensation does not total at least [\$100,000] by the last pay period of the 52-week period, the employer may, during the last pay period or within one month after the end of the 52-week period, make one final payment sufficient to achieve the required level*" (emphasis added). The employer will be able to make an easy year-end calculation whether, with respect to any given employee, it will be less expensive to pay the overtime owed or to add a "final

³⁰ 29 C.F.R. Sec. 541.701.

³¹ In the regulation itself the Department has added an illustrative example: "*Tasks or work performed 'customarily and regularly' includes work normally and recurrently performed every workweek; it does not include isolated or one-time tasks.*" While the portion of the quoted sentence following the semicolon limits the definitional language of the first sentence of Sec. 541.701, the portion before the semicolon does not.

payment" to reach the level of pay necessary to exempt the employee from the overtime requirement.³²

As a legal matter, one must raise the question of whether a person who performs only one exempt duty, with no threshold of substance beyond "more frequently than occasionally," can in any realistic sense be said to be a *bona fide* executive, administrative or professional employee, regardless of how highly paid he or she may be. While the number of employees who will become exempt for the first time under the "highly paid" provisions of the new rules may not be very large initially (it is estimated by the Department at no more than 107,000), it is easy to imagine (and not at all incautious to predict, despite the Department's assertions to the contrary) that virtually every "white collar" employee now earning \$100,000 or more will quickly be made exempt by the assignment of one exempt duty. It seems equally certain that the inevitable effect of (even gradual) inflation on employee compensation will lead before too long to a very substantial increase in the total number of exempt "highly paid" employees.

In summary, these generally-applicable exemption tests have been eroded in virtually every respect:

- the salary basis test is loosened up;
- the new salary amount is derived from the amount previously used for lower paid exempt employees but is now coupled with the less stringent duties tests derived from those previously used for higher paid employees;
- the more stringent "long" duties tests - with their more objective, measurable criteria - have all but disappeared; and,
- the test for highly paid employees has become nothing more than a single exempt duty.

These changes alone would lead us to conclude that the new rules are significantly less protective of workers than the old rules, and that

³² Among other difficult consequences of this provision is the fact that employees potentially eligible for this exemption may not know for sure whether they are entitled to overtime or not until the last day of the thirteenth month from the beginning of the year (as defined by the employer). Furthermore, the rule does not attempt to deal with any of the issues newly raised by the Department's decision to permit deferral of the key qualifying factor for exemption until a year or more after work is done, such as the scope of the recordkeeping requirements applicable during the intervening year, including the duty to keep hours worked records for nonexempt employees (29 C.F.R. 516.3, 516.4), and the duty to make timely payment of overtime due (29 C.F.R. 778.106), etc. For example, where the employer anticipates that an otherwise-qualifying employee will earn more than \$100,000 but he or she does not, it could be very difficult for the employer to accurately reconstruct the overtime hours worked, and overtime compensation due to be paid, since a record of actual hours worked might not have been kept.

many more employees will be found exempt under this new regulatory structure. But the specific changes in the duties tests, to which we now turn, make that conclusion even clearer.

Duties Tests for EXECUTIVE Employees

There are several ways in which the final rule on the executive exemption appears to deny needed protections to workers and, in a manner wholly consistent with the other new provisions of this final rule, weaken the criteria - and broaden eligibility - for this exemption.

We are concerned first about the expanded concept of "concurrent duties"³³ and its interrelationship with the new primary duty test. Certainly we do not dispute that the concurrent duties concept has been applied by many courts, which have found that assistant managers have management as their primary duty even where they spend the vast majority of their time doing nonexempt tasks, and in disregard of the 50 percent "rule of thumb" in the existing regulations.³⁴ The Department was not constrained, however, by the decisions of the courts construing the current regulations, and could have either clarified the old regulation or promulgated a new and "improved" method for testing whether what is claimed about an employee's primary duty matches the reality of the employee's work. Furthermore, the Department (at Sec. 541.700(a)) has now defined "primary duty" as the "*principal, main, major or most important duty,*" thereby significantly downplaying the importance of the relatively more objective factor of how the employee actually spends his or her time. Thus the Department has reversed the significance of these factors. The existing regulations (at Sec. 541.103) give precedence to how much time the employee spends in exempt duties, declaring that "*[i]n the ordinary case it may be taken as a good rule of thumb that primary duty means the major part, or over 50 percent, of the employee's time,*" while the relative importance of managerial duties is just one of the other factors to consider. In the new regulations, how time is actually spent is just one of the factors to consider in determining which duties are the "*most important.*" The result of these changes together is to exempt from the minimum wage and overtime requirements a so-called "manager" who spends the vast majority of his or her time working side-by-side with hourly workers performing the same tasks, but who is passively supervising other employees in the sense that there is always the possibility that he or she may be called upon to perform some management task. While a business cannot function without management employees, to find management to be the primary duty of employees such as the one just described disregards the obvious corollary that a business cannot function without its sales and/or production personnel.

³³ In the Department's 2003 proposal, the rule on concurrent duties related only to supervisors in retail establishments. 68 FR 15586 (March 31, 2003). We believe that this is where the new concurrent duties rule is likely to have its biggest impact.

³⁴ 29 C.F.R. 541.103.

Furthermore, the Department has repeatedly stated that among the principal goals of the rulemaking are to make the rules clearer and more understandable, and to reduce litigation. In our view, the new rule's revised primary duty and concurrent duties concepts will have just the opposite effect. The "long" duties test's 20/40 percent tolerance on nonexempt work that the Department has abandoned is unequivocally an objective test.³⁵ The primary duty test - especially with its new emphasis on "most important duty" - on the other hand, is inherently subjective.³⁶ Whether an individual who has any management duty at all has management as his or her primary duty is entirely "in the eye of the beholder." This determination is peculiarly one where the courts will likely defer to the employer's characterization of the job. This is yet another area where the Department has broadened the exemption in its final rule.

Nor does the new regulation provide any real basis for distinguishing between the assistant manager who is exempt because his or her primary duty is management, and the working foreman who is not exempt because the employee's primary duty is working as an electrician. This invites employers and courts to find virtually every employee with any management or supervisory responsibilities to be an exempt executive. In our view this possibility is not obviated by the provisions in Sec. 541.3 of the final rule regarding "*non-management production-line employees and non-management employees in maintenance, construction and similar occupations.*" This begs the question. If such employees are simultaneously supervising and performing production work, a court might well find their primary duty to be management.

The Department has increased the likelihood that workers performing concurrent duties will be found to be exempt executives by making two other important changes in the regulation regarding criteria for determining "primary duty." As discussed above, rather than strengthen or modify the 50 percent "rule of thumb," the Department has eliminated it.³⁷ Furthermore, the Department - without discussion - has eliminated

³⁵ The Department suggests in the Preamble that decisions such as *Donovan v. Burger King Corp.*, 672 F.2d 221, 226 (1st Cir. 1982), which recognize that managers may simultaneously carry out exempt and nonexempt duties, undercut its ability to utilize a limitation on the amount of nonexempt work that can be performed. To the contrary, the concept of concurrent duties in *Burger King* is applied only to "short" test managers earning more than \$250 per week. In ruling on assistant managers earning less than \$250 per week, the court explicitly rejected application of the concurrent duties test with respect to the "long" test tolerance on the amount of nonexempt work that can be performed. See also *Donovan v. Burger King*, 675 F.2d 516, 519 (2nd Cir. 1982).

³⁶ Thus the Second Circuit compared the "mechanical" long test to the "judgmental" short test. *Donovan v. Burger King*, 675 F.2d 516, 520 (2nd Cir. 1982).

³⁷ But, the Department has retained the provision in the existing regulations - relating to the reverse scenario - that workers who spend more than 50 percent of their time in exempt duties are generally exempt. We agree with the Department that the existing regulation does not automatically find all

one of the most important standards in the current regulations for determining the relative importance of managerial duties: "*the frequency with which the employee exercises discretionary powers.*"³⁸ "Discretion" - though retained in some of the other exemptions - is no longer even a consideration in the determination of primary duty for the executive exemption.

The Department has substantially aggravated these problems by apparently eliminating a key element in the description of what it means to be engaged in "management" of an enterprise or a "department or subdivision" thereof. The existing regulations (at Sec. 541.104) require that a manager be "*in charge of and have as his primary duty the management of a recognized unit which has a continuing function*" (emphasis added).³⁹ The new regulations, on the other hand, might very well permit several executives to be working in one department at the same time, performing the same or different management duties, as long as they each supervise at least two employees.⁴⁰ At a minimum this change will likely engender litigation and, if the courts conclude that the regulation no longer requires that an executive be in charge of a department or subdivision, would significantly broaden eligibility for this exemption.

The new regulation (at Sec. 541.102) exempting employees who own at least 20 percent of the enterprise is in reality a new exemption. The new regulation exempts all such employees provided that they are actively engaged in management. The existing regulation (Sec. 541.114), however, only exempts such owners from the percentage limitations on nonexempt work, which limitations are not even in the new regulations. The existing regulation thus continues to apply the other regulatory tests, including the "short" test requirements, which the new rule does not. Yet again, the eligibility criteria are weakened and eligibility for the exemption consequently broadened.

employees who spend less than 50 percent of their time in exempt duties to be nonexempt, and some courts have disregarded the "rule of thumb," but we continue to believe - as the Department has argued in the past - that it is a useful criterion that the Department could have retained or clarified.

³⁸ 29 C.F.R. Sec. 541.103.

³⁹ See also Wage-Hour opinions dated June 14, 2000 (BNA Wage-Hour Manual 99:8317); March 27, 1986 (BNA Wage-Hour Manual 99:5096); May 21, 1971 (BNA Wage-Hour Manual 99:1068). The requirement that the manager be "in charge" is also implicit in the existing regulatory requirement that the manager have as his or her primary duty "the management" of the enterprise, department or subdivision. 29 C.F.R. 541.100(a)(2). The new regulation provides that the primary duty must be "management." Although this is a subtle distinction, one can imagine that it might be the subject of much litigation.

⁴⁰ It is possible that this is an error or oversight, since paragraphs (b) and (c) of Sec. 541.103 refer to employees who are "in charge" of a subdivision, but nowhere does the regulation state that the manager must be "in charge" to be exempt.

Finally, the Department contends that it has actually narrowed the application of this exemption by adding an additional criterion to the former "short" test for the exemption - the requirement that the manager, to be exempt, also have the authority to hire or fire employees, or make suggestions/recommendations that are given particular weight regarding *"the hiring, firing, advancement, promotion or any other change of status of other employees."*⁴¹ Unsurprisingly, the Department anticipates that this change/addition will have *"a minimal impact on employers."*⁴² Indeed it would be quite extraordinary for anyone to really supervise employees who does not both make recommendations regarding any change in their status, and have such recommendations given heed.

Duties Tests for ADMINISTRATIVE Employees

The final regulations on the duties tests for administrative employees make what appear to us to be the most far-reaching changes of any of the revisions made, notwithstanding the fact that the final rule at Sec. 541.200 retains the key elements of the existing rule. The primary duty of an administrative employee must be *"the performance of office or non-manual work directly related to the management or general business operations of the employer or the employer's customers,"*⁴³ and must include *"the exercise of discretion and independent judgment with respect to matters of significance."*⁴⁴ As we will discuss, however, the regulations explicating these provisions significantly weaken the requirements for the exemption.

⁴¹ 29 C.F.R. 541.100(a)(4), 541.105.

⁴² Preamble p. 22131.

⁴³ This language is broader than the existing regulations, at 29 C.F.R. 541.2(a)(1), which require the primary duty to be directly related to *"management policies or general business operations"* (emphasis added). The substantive effect of this change is unclear, but we believe it likely broadens the exemption. (See, e.g., the Department's opinion dated November 19, 2002 (BNA WHM 99:8399), in which the Department emphasized the administrative assistant's lack of involvement in management policy in finding the employee to be nonexempt.)

The final regulations also use new terminology (at Sec. 541.201(a)) to define what is work directly related to management or general business operations. The existing regulations describe such work as work *"relating to the administrative operations of a business"* (29 C.F.R. 541.205(a)), which they further describe as "servicing" a business. The final regulations instead describe such work as *"work directly related to assisting with the running or servicing of the business."* The regulation contains a useful list of examples of such work, but contains no discussion of the reason for, or implications of, its change in terminology. It is conceivable that *"work related to assisting with the running . . . of a business"* could be broadly defined to include work previously considered "production" work. Rather than a clear, objective test, such new terminology will undoubtedly be the subject of litigation.

⁴⁴ As we discuss below, "matters of significance" is carried over from the existing regulations at Sec. 541.207(a).

First, the final rule significantly broadens the exemption by gutting the "production versus staff" dichotomy that has been the linchpin of Labor Department enforcement. The existing rules explain in pertinent part at Sec. 541.205(a):

The phrase "directly related to management policies or general business operations of his employer or his employer's customers" describes those types of activities relating to the administrative operations of a business as distinguished from "production" or, in a retail or service establishment, "sales" work.

As the Preamble to the final rule explains, the new regulations intentionally reduce the emphasis on the "production versus staff" dichotomy⁴⁵ that is critical to an understanding of what is "work directly related to management policies or general business operations" in the current regulations. Rather than make the production versus staff dichotomy a part of the test, or part of the description of management or general business operations, the new regulations (at Sec. 541.201(a)) simply contrast exempt work to nonexempt work on a manufacturing production line or selling a product in a retail or service establishment. The concept is otherwise absent. Thus, the new regulations do not include the staff versus line distinction in old Sec. 541.201(a)(2) (describing types of administrative employees) or the contrast of exempt employees to "run-of-the-mine positions in any ordinary business," referenced in Sec. 541.205(c)(2).

Although borderline work is always difficult with any test, it has been our experience that the essential distinction between the "staff" functions of a business and the "production" or "line" functions - *i.e.*, making, selling or performing the basic goods or services that the company exists to produce and market - has proven to be a useful, relatively objective, and reasonably reliable test to administer.⁴⁶ As

⁴⁵ Preamble p. 22140-41. In this regard, the Preamble to the final rule says, "We do not believe that it is appropriate to eliminate the [production versus staff dichotomy] entirely from the administrative exemption, but neither do we believe that the dichotomy has ever been or should be a dispositive test for exemption" (emphasis added). The Preamble then goes on, without any apparent irony, to quote approvingly the 1949 Weiss Report, on which the Department relies for many purposes, which explicitly states that "*this exemption is intended to be limited to those employees whose duties relate 'to the administrative as distinguished from the "production" operations of a business.' Thus, it relates to employees whose work involves servicing the business itself - employees who 'can be described as staff rather than line employees, or as functional rather than departmental heads.'*"

⁴⁶ Though this distinction has been in the regulations from the beginning, for a period of years prior to 1988 the Department of Labor in its interpretations of the administrative exemption did not emphasize the staff versus production dichotomy. But - to the best of our collective knowledge and belief - it has consistently applied the distinction in the years since then in its administration and enforcement of the Act. See, *e.g.*, Wage and Hour opinions dated February 1, 1988 (BNA WHM 99:5203); March 16, 1992 (BNA WHM 99:5265); September 12, 1997 (BNA WHM 99: 8096); April 18, 2001 (BNA WHM 99:8360). See

the Second Circuit stated in *Reich v. State of New York* (3 F.3d 581, 588 (2nd Cir. 1993), cert. denied, 510 U.S. 1163 (1994)), "the analogy has repeatedly proven useful to courts in a variety of non-manufacturing settings."

Secondly, the final rule eliminates the requirement in the existing regulations (at Sec. 541.205(a)) that an exempt employee perform "work of substantial importance to the management or operation of the business." This requirement helped ensure that the worker's primary duty was in fact characteristic of an exempt administrative employee. The Department contends that this requirement is duplicative and confusing, since the new rule retains the existing language (at Sec. 541.207(a)) that requires the worker to exercise discretion and independent judgment with regard to "matters of significance." However, the Department acknowledges that under the new rule, the work need only "include" such exercise of judgment and discretion.⁴⁷ Thus it seems clear that work of substantial importance/significance is a smaller component of the required work of an administrative employee under the new regulations than was true under the old rules. Therefore, this change in the rule can only serve to expand the pool of employees to whom the exemption could be applied.

Finally, the examples given of administrative employees potentially eviscerate the standards of the rule. We recognize that some, not all, courts have held that employees such as insurance claims adjusters and employees in the financial services industry are exempt administrative employees. We also recognize that the existing regulations (at Sec. 541.205(c)(5)) suggest that claims adjusters are often exempt. Departmental staff have long recognized the tension and apparent inconsistency between this provision of the regulations and the standards for the administrative exemption. It is our view that both claims

also, *Martin v. Cooper Elec. Supply Co.*, 940 F.2d 896 (3rd Cir. 1991); *Reich v. State of New York*, 3 F.3d 581 (2nd Cir. 1993), cert. denied, 510 U.S. 1163 (1994); *Reich v. John Alden Life Ins. Co.*, 126 F.3d 1 (1st Cir. 1997); *Reich v. Chicago Title Insurance Co.*, 853 F. Supp. 1325 (D. Kan. 1994).

We recognize that the Department, in its recent opinion letter on insurance claims adjusters, cited the distinction between production work and work related to management policies and general business operations, but then ignored this dichotomy in finding that claims adjusters were exempt. (November 19, 2002 (BNA WHM 99:8396)) This may have been a results-driven opinion, possibly affected by the concurrent process of drafting the proposed rule. The Department relied on the dichotomy again in its more recent opinion letter on application of the exemption to administrative assistants. (February 14, 2003 (BNA WHM:8399))

⁴⁷ In contrast, the current "long" test - which the Department has decided not to utilize - requires that an exempt employee "customarily and regularly" exercise discretion and independent judgment (29 C.F.R. 541.2(b)). As discussed above, the Department has defined "customarily and regularly" in Sec. 541.701 of the final rules as "a frequency that must be greater than occasional but which, of course, may be less than constant." The regulation further provides that work performed every week is customary and regular. Since the Department emphasizes in the Preamble that "includes" is a lesser standard than "customarily and regularly," it may be that an administrative employee need not exercise discretion and independent judgment even as often as every workweek.

adjusters and financial services employees are ordinarily (though not in every case) performing work that constitutes the core business of their employer - and are not doing work related to assisting with the running or servicing of the business, and should, therefore, not be exempt.⁴⁸ Although one can view an insurance company as in the business of developing and selling insurance policies, it is also true that the customer who purchases the company's insurance is not primarily buying the policy, but rather the package of obligations and services which the company commits to provide when the circumstances arise, most importantly the essential services of claims processing and payment. To the customer, it is the claims processing and payment undertakings that are the company's stock in trade; it could not stay in business without the provision of these services. Similarly, many employees in the financial services industry today are providing services to customers, not servicing the business of their employer. By including these examples, with duties that are not at all akin to the list of exempt functions contained in new Sec. 541.201(b) in the regulations, the Department has opened the door wide to exempting other classifications of employees who have never been considered entitled to this exemption.

The team leader provision in new Sec. 541.203(c) is an entirely new regulatory concept that is also fraught with ambiguity. This provision is not based on case law, but is purportedly an attempt to reflect modern workplace practices. In the Department's 2003 proposed rule, the team leader discussion (at Sec. 541.203(b)(3)) only served as an example of work of "substantial importance" - a concept that has been deleted from the rule except as it pertains to the exercise of discretion. The final rule more broadly states that a team leader assigned to complete major projects generally meets the duties requirements, without explicit consideration of whether the team leader performs projects related to the management or general business operations of the employer. The fact that the examples concern such projects does not mean that it is necessarily so. Furthermore, the regulations do not address the very real possibility that team leaders may be working on a number of different short- or long-term projects, simultaneously or in succession, some of which would be major and directly related to the performance of management or general business operations and some of which would not. Evaluating the team leader's primary duty in that instance will be very difficult at best. Would the employee, for example, move in and out of exempt status from one week to the next?⁴⁹ How this provision will

⁴⁸ We agree that in some instances claims adjusters and employees in the financial services industry are engaged in work directly related to the management or general business operations of their customers. In such instances, the employees would be exempt if they otherwise meet the tests of the regulations.

⁴⁹ Neither the regulations nor the Preamble addresses the conceptual difficulty arising out of the fact that many team leader assignments are, by definition, of temporary duration. In the examples given in the rules, this appears to be the case. While it may be contemplated that an employee's exempt status would vary from week to week, the effect of overlapping or concurrent team leader assignments and similar variations is not explained. This new concept will likely become a source of confusion and litigation.

operate in practice can only be imagined, but one can surmise that employers will seek to apply this provision to large numbers of employees to whom the exemption was never intended to apply.

Thus, there are several aspects of the final rule relating to the administrative exemption that have the potential to substantially increase the numbers of employees who will be found to be exempt administrative employees. Although the proof is in the implementation, both by the Department and by the courts, we are confident that the Department has promulgated a rule that will engender many new questions and litigation, and will undoubtedly remove overtime protections for large numbers of currently nonexempt employees.

Duties Tests for PROFESSIONAL Employees

With its revised criteria to qualify for exemption as a professional employee, particularly as a "learned professional," the Department repeats the pattern of articulating standards that appear to be grounded in and resemble those in current law. However, having articulated the criteria, the Department then goes on to ignore, bend or even violate its own standards in declaring that certain occupations meet the criteria to qualify for this exemption, thereby even further expanding its scope, in what must be seen as a blatant (if incoherent) effort to achieve particular results serving certain special interests.

The Department states that *"only occupations that customarily require an advanced specialized degree are considered professional fields under the final rule."*⁵⁰ It is apparently on this basis that the Department contends that its *"final professional test is as protective as the existing short duties test under which most employees are tested for exemption today."*

But it is simply not ... as the Department goes on to admit.

For example, while admitting that, *"In the past, the Department has taken the position that athletic trainers are not exempt learned professionals"* it goes on to find - based on *"information submitted by commenters"* - that, *"athletic trainers are nationally certified and that a specialized academic degree is a standard prerequisite for entry into the field."*

⁵⁰ Preamble p. 22149. This statement accurately reflects most aspects of the duties test for exemption as a "learned professional" under current law though it does not include that the *"knowledge ... of advanced type ... must be ... in a field of science or learning."*

The term "advanced" degree does not here necessarily refer to what most would think of as an "advanced degree" - i.e., a post-Bachelor's degree like a Master's, doctorate, law degree, or medical degree. Rather, the Department uses this term (as, in some cases, it has in the past - e.g., nursing degree at the Bachelor's level) in the context of its affirming recitation of the separate elements of the "learned professional" duties test as explained in 1940 - in this case referring to *"knowledge ... of an advanced type ... [which] generally speaking ... cannot be attained at the high school level."*

That "specialized academic degree" is "a Bachelor's degree in a curriculum accredited by the Commission on Accreditation of Allied Health Education Programs," which accredits curricula in "specialized fields such as athletic training, health, physical education or exercise training..." Therefore, the Department concludes that certified "athletic trainers ... would qualify as exempt learned professionals."⁵¹ There appears to be no other, independent evidentiary basis for the Department's finding that attainment of an advanced specialized degree is "customarily required" for entry into this occupation (or the others referenced) - as opposed to certification. Rather, in this instance (again, based in part on a court case interpreting the "old," current regulation contrary to the Department's own position) the Department seems to be implying that qualification for the learned professional exemption derives from certification by some entity (here, the Board of Certification of the National Athletic Trainers Association Inc.) while bypassing any effort to independently verify "commenters'" assertions regarding the question of whether an "advanced specialized degree" is "customarily required" for entry into the occupation.⁵²

In a somewhat similar departure, the Department acknowledges that "In the past [in fact, as recently as 2000], the Department has taken the position that licensed funeral directors and embalmers are not exempt learned professionals." But, based on information that "licensed funeral directors or embalmers in 16 states must complete at least the equivalent of four years of post-secondary education" the Department declares that this "... is sufficient ... to meet the educational requirements for the learned professional exemption." Based on licensure requirements in less than one-third of the States, this seems much less than conformity with the statement that only "occupations that customarily require an advanced specialized degree are considered professional fields under the final rule."⁵³ While the Department limits its award of exempt status to those

⁵¹ See discussion at Preamble p. 22155. The Department does not go on to state explicitly that the other identified, certified occupations - i.e., some "health" workers, physical education instructors (other than physical education teachers), and exercise trainers - are, on the same basis, exempt learned professionals. But it is hard to imagine how the Department's stated rationale would not equally - and, in our view, absurdly - apply to them as well.

⁵² It should here be noted that the Department's final rule provisions relating to athletic trainers, funeral directors and embalmers (discussed below) were not included in its proposed rule, but the proposal did invite comment on occupations "the exempt status of which has been the subject of confusion and litigation including but not limited to pilots, athletic trainers, funeral directors, insurance salespersons, loan officers, stock brokers, hotel sales and catering managers, and dietary managers in retirement homes" and went on to alert the public that "The Department anticipates that the final rule will include additional provisions on the application of the exemptions to such borderline occupations, but requires more information about the particular job duties and responsibilities generally found in such occupations."

⁵³ Preamble pp. 22155 - 22156. Here, yet again, the Department cites and adopts court cases contrary to its long-standing position.

"Licensed funeral directors and embalmers who are licensed by and working in" the States that do require a four-year degree for licensure, it simply ignores the clear evidence in its own record that - in fact - no advanced, specialized degree is customarily required for entry into employment in either profession. It appears that under the new rule some people doing a given job in a given place with a given educational background will be exempt, while others with exactly the same education and doing exactly the same job, but who are located in a different State, are not exempt, based entirely on the State's licensure requirements. Can this be a rational delimitation of exempt professional work, or is it a distortion leading to a desired result?⁵⁴ And this seems, too, to represent a fundamental - but unstated - shift from making such determinations based on the customary requirements for entry into an occupation to the specific qualifications of certain individual employees in the occupation, also evidenced in the following discussion. This conceptual conflict adds new ambiguity to the regulatory structure and, of course, the effect in litigation cannot be predicted.

In another instance, though obviously wary that employers in the restaurant industry will be inclined to drive a truck through the stated boundaries of its new rules, the Department declares in its final rule that, "*Chefs, such as executive chefs and sous chefs, who have attained a four-year specialized academic degree in a culinary arts program, generally meet the duties requirements for the learned professional exemption.*"⁵⁵ Once again there is no evidentiary showing that such an "advanced specialized degree" is a customary, even common, requirement for entry into the profession, and there is not even the "fig leaf" of a licensure or certification requirement.

Continuing to demonstrate that its final rule relating to this exemption is overtly not "*as protective*" as it claims, the Department's attention to the learned professional exemption duties tests caps off these

⁵⁴ In recent years considerable consolidation has occurred in the Nation's funeral industry, with family-owned and operated funeral parlors being bought up in large numbers by large companies. One effect has been that formerly-exempt business owners (the family member owner-operators) are transformed into nonexempt employees of the large corporations. The funeral industry has, consequently, lobbied hard but unsuccessfully for many years - in both the executive and legislative branches - to get the law changed to declare these employees to be exempt "professionals." The industry obtains at least partial success through this final rule.

⁵⁵ Preamble p. 22154. In addition, "[T]he Department concludes that to the extent a chef has a primary duty of work requiring invention, imagination, originality or talent, such as that involved in regularly creating or designing unique dishes and menu items, such chef may be considered an exempt creative professional..." [emphasis added] though "[t]he Department intends that the creative professional exemption extend only to truly 'original' chefs, such as those who work at five-star or gourmet establishments, whose primary duty requires 'invention, imagination, originality, or talent.'" Preamble p. 22154. Does this clarify anything?

substantial deviations from the articulated criteria with another new provision described in the Preamble⁵⁶:

... [S]ection 541.301(f) recognizes that the areas in which the professional exemption may be available are expanding. [This new section thus ...] provides: "Accrediting and certifying organizations similar to those listed in [referenced] subsections ... also may be created in the future. Such organizations may develop similar specialized curriculums and certification programs which, if a standard requirement for a particular occupation [emphasis added], may indicate that the occupation has acquired the characteristics of a learned profession." This new language is adopted to ensure that final subsections [referenced] ... do not become outdated if the accrediting and certifying organizations change or if new organizations are created. ... Neither the identity of the certifying organization nor the mere fact that certification is required is determinative, if certification does not involve a prolonged course of specialized intellectual instruction.

While the language "may indicate" evidences some caution, the condition that such curricula and certification be "a *standard requirement for a particular occupation*" has been completely ignored with regard to the preceding "professional" occupations, and the Department makes no effort to indicate that future curricula or certification requirements or institutions must be at least as stringent as those it has bent its own criteria to accommodate.

The Department's final rule does change the duties test for teachers by eliminating the requirement that they exercise discretion in the performance of their job.⁵⁷ The implications of this change are unclear to us (as we expect most teachers would, by the nature of their challenging work, often exercise considerable discretion), but the effect of this change in the duties test - if any - could only be to broaden eligibility for exemption.

It should also be noted that the Department states that its final rule does not change the duties tests in current law with respect to some occupations that it has deemed do qualify as exempt learned professionals - including pharmacists, registered nurses, certified medical technologists or physician assistants, certified public accountants, and dental hygienists.⁵⁸

⁵⁶ See p. 22157.

⁵⁷ See Sec. 541.3(a)(3) and (b) of the existing rule, Sec. 541.303(a) of the new rule.

⁵⁸ However, the Department does not discuss how its loosening of the "salary basis" test, discussed above, may have the practical effect of converting employees in these occupations from nonexempt to exempt as their employers adjust their compensation systems in a manner allowed by the new rule. This outcome is likely because, in the past, many employees in these occupations were nonexempt - and, thus, entitled to overtime premium pay - based not on their

Duties Tests for OUTSIDE SALES Employees

The employees at issue in the outside sales exemption are unlike the employees considered elsewhere in this rule. In many cases they are the blue collar workers whom the Act was especially intended to protect. Notwithstanding, the final regulations make a dramatic substantive change that will likely remove minimum wage⁵⁹ and overtime protection for large numbers of employees.

The existing regulations prohibit an exempt outside sales employee from spending more than 20 percent of his or her hours worked in any workweek on nonexempt work.⁶⁰ Unlike the other exemptions, there is no salary level requirement for outside sales employees and, therefore, there is no "long" or "short" test; all exempt employees are subject to the 20 percent limitation. In the guise of conforming to the principle it has applied to the executive, administrative and professional exemptions of using only a "primary duty" test, the Department (in Sec. 541.500(a)(1) of the final rule) eliminates the more objective time tolerance test and substitutes a more subjective primary duty test.⁶¹

This change alone has the potential to dramatically increase the number of employees subject to this exemption. First, instead of denying the exemption to any employee who spends more than 20 percent of his or her time on nonexempt work, the general regulation on "primary duty" (at Sec. 541.700) - applicable to this exemption just as it is to the others - provides that any employee who spends 50 percent or more of his/her time on exempt work is generally exempt. Moreover, the regulation provides

(otherwise qualifying) duties, but on the fact that they were not paid "on a salary basis" under the current, more stringent rules.

Further, the Department also reaffirms its long-standing position that certain occupations do not meet the duties test for the "learned professional" exemption, including licensed practical nurses, cooks, pilots, engineering technicians, and beauticians - generally because "*none of these occupations require specialized academic training at the level intended by the regulation.*" Preamble p. 22150.

⁵⁹ The Part 541 regulations are commonly referred to as the "white collar" exemption from the Act's overtime requirements. In fact, as noted at the outset of this paper, they also exempt employees from the minimum wage. Although this is rarely an issue for executive, administrative, and professional employees, it can be a very real consideration for outside sales employees, who have no salary protection in the regulations.

⁶⁰ 29 C.F.R. 541.5, 541.507. For this purpose, work that is "*incidental to and in conjunction with the employee's own outside sales or solicitations*" is not regarded as nonexempt work.

⁶¹ Structurally, the primary duty test takes the place of the "for the purpose of" standard in the regulation. Compare, existing Sec. 541.3, to new Sec. 541.500. It is not clear if there is a substantive distinction.

further that an employee might be exempt even if the employee spends less than 50 percent of his/her time on exempt duties.⁶²

Thus, pursuant to Sec. 541.700(a), the determinative test becomes not the objective test of the amount of time spent on exempt and nonexempt work, but rather the subjective test of the employee's most important duty.⁶³ This is likely to be particularly problematic when considering the exempt status of drivers who sell. The exempt status of these workers has always been a difficult question, requiring consideration of both the employee's primary (or chief) duty, and the amount of time spent in nonexempt work.⁶⁴ Yet the new regulation (at Sec. 541.504(b)), unlike the general regulation on "primary duty" (at Sec. 541.700(b)), completely eliminates time as a factor in determining the exempt status of such driver-sales employees, thereby substantially increasing the likelihood that these workers will be found to be exempt.

The final regulations also appear to open the door to the exemption of employees performing services in the homes or businesses of their customers, such as plumbers and electricians. Existing Sec. 541.501(d) extends the exemption to employees who sell or take orders for service performed for the customer "*by someone other than the person taking the order.*" At the same time, existing Sec. 541.501(e) expressly states that the exemption does not extend to employees such as service persons, even if they may be said to sell the service they are performing, since selling the service is incidental to the service performed. In marked contrast, new Sec. 541.501(d) changes the whole emphasis, extending the exemption to employees who take orders for a service whether the service is performed by that employee or someone else. The additional discussion of the nonexempt status of service persons is deleted. Although the Department, in the Preamble,⁶⁵ states that the removal of this language was not intended to be a substantive change, it declined to reinstate the language, thereby creating, at a minimum, new ambiguity. Courts may well find that the effect of these two modifications to the rule is to extend the exemption to service persons who take orders for service in the customer's home.

The sum of these changes - clearly intentional in the case of the elimination of the time limitation on nonexempt duties - is sure to

⁶² We are at a loss to understand how the Department can contend that "*few, if any, employees would lose overtime protection*" as a result of its revisions to this exemption category (Preamble p. 22195).

⁶³ The inappropriateness of this test for outside sales employees is demonstrated by the fact that two of the generally-applicable factors used in determining primary duty seem completely inapposite - the employee's relative freedom from direct supervision and the relationship between the employee's wages and the wages of other employees performing the same kind of nonexempt work.

⁶⁴ 29 C.F.R. 541.505(a).

⁶⁵ See p. 22161.

increase greatly the number of workers who will be considered exempt as outside sales employees.

Duties Tests for Employees in COMPUTER-RELATED Occupations

The principal difference between the old and the new rules for exemption of highly skilled employees in computer-related occupations relates to the exercise of discretion and judgment. As explained in the Preamble to the new final rules, the regulatory scheme under the old regulations provides two distinct methods for such an employee to be exempt: (1) meeting the tests of the 1996 statutory provision codified at Sec. 13(a)(17), which enacted most but not all of the substance of the Department of Labor's 1992 rule; or (2) meeting the requirements of the 1992 rule itself. Under the old rules an exemption under Sec. 13(a)(17) means being paid hourly at a higher level (\$27.63 per hour) but with no requirement relating to the exercise of discretion; qualification under Sec. 13(a)(1), as promulgated in 1992 (to implement the 1990 legislation relating to computer personnel), requires payment "on a salary basis" at the required salary level, but also has the separate requirement that the work require the consistent exercise of discretion and judgment in its performance. This discretion requirement has been eliminated in the new rule, on the stated ground that it was not included by Congress in adopting Sec. 13(a)(17), and that, in the Department's opinion "*two different definitions for computer employees exempt under sections 13(a)(1) and 13(a)(17) of the FLSA would be inappropriate given that Congress recently spoke directly on this issue...*" Despite this judgment, however, the Department does continue to provide exemption for computer employees under both Sec. 13(a)(1) and Sec. 13(a)(17), with the difference that an employee may in the future qualify for exemption under Sec. 13(a)(1) without meeting the "*consistent exercise of discretion and judgment in the performance of the work*" test. Without doubt some employees who would not have met the requirements for exemption under the old rule will meet the new, less stringent requirements.

In addition, the new rules eliminate the entire statement in the existing regulations that the exemption:

*"... applies only to highly-skilled employees who have achieved a level of proficiency in the theoretical and practical application of a body of highly-specialized knowledge in computer systems analysis, programming, and software engineering, and does not include trainees or employees in entry level positions learning to become proficient in such areas or to employees in these computer-related occupations who have not attained a level of skill and expertise which allows them to work independently and generally without close supervision. The level of expertise and skill required to qualify for this exemption is generally attained through combinations of education and experience in the field"*⁶⁶ (emphasis added).

⁶⁶ See 29 C.F.R. 541.303.

It seems clear that the omission of this language will create new ambiguity and, with respect to the underscored language, is likely to expand eligibility for the exemption to include employees who, because they work with skill and proficiency but with relatively more supervision and less independence than those now exempt, are now considered not to be exempt.

It is on the basis of the foregoing discussion that we have concluded, as stated previously, that in every instance (with the sole possible exception of the "salary level" test) where the Department has made substantive changes to the existing rules it has weakened the regulatory criteria for, and thereby expanded the reach and scope of, the Sec. 13(a)(1) exemptions.

The Department's Stated Goals

We also considered whether the final rule actually achieves the Department's own stated goals to "*simplify, clarify and better organize the regulations ... Rather than broadening the exemptions, the final rule will enhance understanding of the boundaries and demarcations of the exemptions Congress created.*"⁶⁷

The Department contends that such simplification, clarification, and reorganization - its pervasive euphemism is "streamlining" - will serve to better reflect the realities of the modern workplace, promote greater understanding of rights and responsibilities by both employers and workers, promote higher levels of compliance and better enforcement, and substantially reduce future litigation. Certainly these are laudable goals and generally desirable results to be achieved. But, as we have tried to show in the above discussion, the proposition that the Department is not "broadening the exemptions" is not - in our view - substantively correct and warrants little attention except for its propaganda value. We have, therefore, also considered whether the Department's final rule is likely to achieve its other intended outcomes.

Reorganize: We agree that the Department has reorganized the structure of the current regulation in what can be a useful and ultimately beneficial way, by combining and integrating the formerly separate legislative and interpretive rules on the same subject. This reorganization will no doubt benefit the regulated community - both employers and employees - in facilitating accessibility to and identification of the exemption criteria because they are now delineated in one set of rules. A corresponding effect which must be noted, however, is that the entire rule is now a legislative rather than an interpretive rule. This will substantially extend the range of matters to which greater judicial deference will be given, and this extension, as we have pointed out in our comments on the substance of the changes, may

⁶⁷ See Preamble p. 22125. In her testimony before the House of Representatives Committee on Education and the Workforce on April 28, Labor Secretary Chao said, "we have designed new regulations that are clear, straightforward and fair."

not be entirely constructive, especially in those instances where examples seem to contradict substantive exemption criteria. The full impact of these changes will be seen only years from now.

But whether this new regulation will serve to accomplish the Department's other stated objectives - to better reflect the realities of the modern workplace, promote greater understanding of rights and responsibilities by both employers and workers, promote higher levels of compliance and better enforcement, and substantially reduce future litigation - certainly depends much more on the extent to which the Department has, in fact, been able to simplify and clarify the exemption criteria so that both employers and employees are more confident that they clearly understand who does and does not qualify for exemption, with the real-world operational effect that employers will misclassify fewer employees as exempt who do not qualify.

Simplify: The Department has indeed simplified the exemption criteria in its final rule. Unfortunately, in our view, it has done so largely by eliminating exemption criteria in the current rule, and thereby it has effectively broadened the exemptions. For example, the Department has eliminated discretion - an important indicator of exempt status - as a factor for determining the exempt status of employees in computer-related occupations, as a factor considered in examining the "primary duty," and as a factor in the exemption of teachers as learned professionals. The Department has also chosen to eliminate important, objective criteria for exemption that give valuable weight to how one actually spends one's time at work, including the standards for the portion of time spent in exempt duties (the old 50 percent "rule of thumb") or in nonexempt duties (the former 20 [and 40] percent "tolerances" in the "long" test, and the 20 percent tolerance for outside sales employees). Instead of finding ways to retain or modify such straightforward and measurable tests, the Department has eliminated them from the new rule.

Clarify: The Department has also simplified and in a way "clarified" the rule by declaring entire occupational categories that do not meet the regulatory tests (some of which it previously held did not qualify for exemption) as now qualifying. This, of course, might serve to prevent some future litigation by employees in these occupations simply because their entitlement to overtime pay has been taken away by the Department.⁶⁸ It is our view that the net effect of these declarations, however, will be to greatly increase litigation because they are so clearly inconsistent with the regulatory criteria. Employers will argue - and courts may well agree - that other occupations that do not meet the regulatory criteria should likewise be exempt.

Furthermore, by eliminating or greatly reducing the emphasis on several existing requirements and introducing new terms and concepts as the basis to qualify for exemption, it is our view that, in fundamentally important ways, the Department's final rule is significantly less clear than the

⁶⁸ Though, of course, some employees newly losing nonexempt status, and overtime pay, may be inclined to litigate the question of whether the Department has abused its discretion and exceeded its authority in this rulemaking.

current rules. For example, the Department has decreased the emphasis on the staff-production dichotomy in the administrative exemption without putting any other meaningful standard in its place. The requirement that an executive be "in charge" seems to have been eliminated from the executive exemption (though still mentioned in examples). In dropping the requirement that an exempt administrative employee perform work of substantial importance to the management or operation of the business, and including the requirement that the work include the exercise of discretion on "matters of significance," the Department has added new ambiguity to the duties requirements for administrative employees. The new definition of "primary duty," the key to the determination of exempt status, is merely a collection of loose synonyms that largely depend upon the employer's characterization of the employee's duties and confide the decision entirely to the subjective judgment of the decision-maker. The circumstances in which employers may take improper deductions from pay without losing the benefit of the exemption have been redefined and expanded, making further litigation virtually certain. All of these changes constitute an open invitation to dispute, with the almost certain result that the Department's stated goals will be frustrated.

In other words, to the extent that the Department's new exemption eligibility rules may achieve some of its stated goals, they do so only where, and because, they go so far in eliminating or reducing existing exemption criteria and declaring new occupational categories to qualify for exemption. At the same time, the murkier and less stringent standards now embodied in the final rule can only have the countervailing effect of encouraging employers to push the boundaries of the new standards. That is because it is - and always will be - in their fundamental economic interests to do so in order to reduce labor costs by avoiding overtime pay. The Department's new rules give them great license and latitude to do so - with the predictable effect that misclassifications will multiply, workers will be less able to discern or show that they are improperly treated as exempt (and wrongfully denied overtime pay), and litigation will proliferate over a host of different issues than under the current rules. Of course, we will all have to wait to see whose expectations of future results prove more prescient.

In conclusion, based on our review of the final rule and the foregoing discussion, we believe that the Department has systematically and effectively weakened virtually all of these exemptions, and thus substantially broadened the class of employees who will be exempt, without substantially clarifying the rules for exemption; and, that the highly desirable results the Department expresses its hope to achieve will prove elusive, at great cost to U.S. workers and their families.

Appendix I

If we correctly understand the Department's own estimates, from the final rule's economic impact analysis:

- There are about 135 million people in the entire U.S workforce.
- 15 million - about 11 percent of the workforce - are not covered by the FLSA, principally the self-employed.
- 3 million workers are employed in "occupations specifically exempted from the FLSA's overtime provisions,"⁶⁹ such as most farm workers, and another 1.5 million Federal employees are not subject to the Department's regulations (but rather to rules promulgated by the Office of Personnel Management) - together comprising another 3 percent of the entire workforce.
- Consequently, about 115 million workers (85 percent of the total U.S. workforce) are - according to "the Department's best estimate" - covered by the Act's overtime provisions.
- About 43 million of these workers - 37 percent of the covered workforce (and about one-third of the total workforce) - are employed in what the Department refers to as "blue collar" occupations that are, based on the job titles, unlikely to qualify for exemption under Sec. 13(a)(1).
- There are more than 7.5 million employed in occupations that (again based on the job titles) make them highly likely to be minimum wage/overtime exempt under Sec. 13(a)(1) as "learned professionals" (teachers, doctors, lawyers, judges, etc.) or "outside sales" employees.
- This leaves more than 64 million workers - nearly three-fifths (56 percent) of the covered workforce (and, with the previous 7.5 million likely exempt, a total of nearly 72 million, more than one-half [53 percent] of the entire U.S. workforce) - who work in occupations that *might* qualify for exemption under Sec. 13(a)(1).⁷⁰

The Department estimates that more than 19 million (of the estimated 31 million "white collar workers who earn \$155 or more per week" - about two-thirds of the total) are exempt under the current rules implementing

⁶⁹ See Table 3-1, Preamble p. 22197. Presumably these employees are overtime exempt under various provisions of Sec. 13(b) of the Act, but, of course, this number does not include any who might be exempt under Sec. 13(a)(1).

⁷⁰ See Preamble at p. 22201. These occupations are, as with the other statistics cited, based on job title alone. The Department reports that about half of these workers are hourly paid and half paid other than hourly (which - for convenience - it calls "salaried").

Sec. 13(a)(1). So - in aggregate - the new rule could conceivably extend exempt status to as many as 53 million more workers ($64.4 + 7.5 - 19.4 = 52.5$), or about 40 percent of the total U.S. workforce.⁷¹ But it is impossible to predict - even by the Department - to what extent changes in compensation practices will actually be experienced by these workers under the Department's final regulations.

⁷¹ Of course, some of those in the currently exempt count could also experience a change in exempt status.

Appendix II - The "Salary Basis" Test's "Window of Correction"

Because payment of compensation "on a salary basis" is one of the listed indispensable conditions for the vast majority⁷² of workers who might be exempt under Sec. 13(a)(1) of the Act, the question whether this test is met has been and could be determinative in many cases. Under both the old and new rules there are provisions for resolving doubts about whether the salary basis requirements have been met, but the new rules take a much less stringent view of what is "enough" for the employer to show that this requirement has been met, and, we believe, very substantially reduce the possibility of proving that a typical hourly pay plan fairly applied to a typical hourly-paid employee fails to meet the salary basis test. In other words, the limitations placed on the inferences to be drawn from deductions inconsistent with the salary basis of compensation make the continued inclusion of the salary basis requirement largely meaningless.

Under both versions of the rules⁷³ the question of possible "correction" arises when an employer claims that an employee or a group of employees is paid "on a salary basis," but the records show that there are circumstances where deductions have been made that are not consistent with salary basis payment.

A provision of the current "window of correction" rule provides that, "[W]here a deduction not permitted by these interpretations is inadvertent, or is made for reasons other than lack of work, the exemption will not be considered to have been lost if the employer reimburses the employee for the deductions and promises to comply in the future."⁷⁴ It has long been recognized that the language of this provision is ill-designed to serve its intended purpose, since the use of the word "or" implies grammatically that a deduction for any reason whatever other than "lack of work" can be corrected without penalty. In the last 50 years, few deductions have been made for "lack of work." In the contemporary workplace, deductions are made either because an employee doesn't work; or for disciplinary reasons; or, most commonly, because the employer gave little or no attention to the requirements of payment "on a salary basis" and/or thought the deductions made did not defeat the salary basis requirements. A very common situation is that deductions are made from the compensation of employees because the

⁷² Professional employees may be exempt if paid on a "fee" basis; and doctors, lawyers, teachers, and outside sales employees have no payment basis requirement.

⁷³ 29 C.F.R. Sec. 541.118(a)(6) (current rule); 29 C.F.R. Sec. 541.603 (new final rule).

⁷⁴ The derivative of this provision (in the current rule at Sec. 541.118(a)(6)) appears in the new rules at Sec. 541.603(c), which provides "*Improper deductions that are either isolated or inadvertent will not result in the loss of the exemption for any employees subject to such improper deductions, if the employer reimburses the employees for such improper deductions.*"

employer has in place some system which he regards as a "salary," but which in fact is not consistent with the "salary basis" requirements previously described.⁷⁵

To assist the courts in applying the window of correction rule to the exact problems before them, the Department has, for many years, taken the position that the window of correction is not properly applied to permit the restoration of exempt status if the employer never had a policy of paying employees "on a salary basis" to begin with. The Department of Labor has expressed this view clearly in a number of cases.⁷⁶

As will be shown, the Department's new rules seem initially to express the position formerly taken by the Department, but then go on to make fundamental changes in the regulatory approach to the question addressed by the former "window of correction" language. In language apparently consistent with the Department's past position, the new regulation provides that "An employer who makes improper deductions from salary shall lose the exemption if the facts demonstrate that the employer did not intend to pay employees on a salary basis." The rule continues, "An actual practice of making improper deductions demonstrates that the employer did not intend to pay employees on a salary basis."⁷⁷ From these two sentences the rule appears straightforward to apply.

However, the picture then becomes much less clear, as the rule continues:

The factors to consider when determining whether an employer has an actual practice of making improper deductions include, but are not limited to: the number of improper deductions, particularly as compared to the number of employee infractions warranting discipline; the time period during which the employer made improper deductions; the number and geographic location of employees whose salary was improperly reduced; the number and geographic location

⁷⁵ Many employers have adopted paid leave programs which have significantly reduced the frequency of partial day deductions for partial day absences for personal reasons among both salaried and hourly employees. This development has also had the effect of making it harder to discern which employees are paid "on a salary basis" and which are not.

⁷⁶ After the decision of the Supreme Court in *Auer v. Robbins*, 519 U.S. 452 (1997), which deferred to the Secretary's view of what it means to be paid "on a salary basis," the Department of Labor filed briefs as *amicus curiae* in *Yourman v. Giuliani*, 229 F.3d 124 (2nd Cir. 2000), cert. denied, 532 U.S. 923 (2001); *Klem v. County of Santa Clara* (9th Cir. 2000); *Whetsel v. Network Property Services, LLC*, 246 F.3d 897 (7th Cir. 2001); *Takacs v. Hahn Automotive Corp.*, 246 F.3d 776 (6th Cir. 2001), cert. denied, 534 U.S. 889 (2001). In all of these cases the courts upheld or deferred to the Secretary's interpretation of the "window of correction." Other courts have held to the contrary, although no court in which the Secretary made an appearance to express a view has done so. See, e.g., *Davis v. City of Hollywood*, 120 F.3d 1178 (11th Cir. 1997); *Balgowan v. New Jersey*, 115 F.3d 214 (3rd Cir. 1997); *Moore v. Hannon Food Serv.*, 317 F.3d 489 (5th Cir. 2003), cert. denied, 2003 U.S. LEXIS 7309.

⁷⁷ Sec. 541.603(a).

of the managers responsible for taking the improper deductions; and whether the employer has a clearly communicated policy permitting or prohibiting improper deductions.

The "light" cast by the last sentence on the preceding two provisions leaves, in our view, almost total uncertainty about the result which should be reached in a given case. The various matters which are to be taken into account seem to imply that even the existence of many actual deductions, or actual deductions taken on every occasion when such deductions might have been made, might not lead to a conclusion that the employer had an "actual practice" of making such deductions. The significance of such factors as the number and geographic location of the employees whose salaries were improperly reduced, and of the managers "responsible" for taking the improper deductions, is more mysterious still.

Suppose employer A, who provides no sick leave or paid vacation time to employees, has 100 employees, whose work records present 15 occasions on which improper deductions might have been made (for example, because employees took off work for part of a day).⁷⁸ On these 15 occasions, 10 improper deductions were made and five were not made. Compare Employer A's situation to that of Employer B, a similar employer who has 10 employees whose work records present five occasions on which improper deductions might have been made and on four of those five occasions, improper deductions were made. Leaving aside questions of geographic location, managers involved, etc., are Employer A and B the same, or different? And compare both to Employer C, who has 1,000 employees whose work records reflect 100 occasions on which improper deductions might have been made and 20 occasions on which improper deductions were made. Reasonable advocates could clearly make the case that each of these three employers had an actual practice of making improper deductions; equally reasonable advocates, that none of them did.

The rule does not, in our opinion, provide anything like sufficiently clear criteria or guidance to decide whether all, or some, or none of these three employers have an "actual practice" of making improper deductions, and that is even before one attempts to factor in the relevance, if any, of the "*number and geographic location of the managers responsible*" and the existence or not of a clearly communicated policy "*permitting (sic) or prohibiting improper deductions.*"⁷⁹

The next part of the revised "window of correction" rule, although not free of ambiguity, is much clearer than the first part. Paragraph (b) has the purpose and effect of limiting the weight to be given to any

⁷⁸ A partial day's absence is an occasion which will provide evidence concerning an employer's policies of making or not making deductions not permitted under the "salary basis" rules.

⁷⁹ One might be forgiven for thinking that a clearly articulated policy permitting improper deductions would lead to the conclusion that the salary basis test was not met.

improper deductions actually made, and thus significantly limiting the scope of employer liability. Under the old rule, where improper deductions show that the compensation of some class of employees is "subject to reduction" and thus that they are not being paid "on a salary basis,"⁸⁰ the conclusion typically extends to some objectively delineated class or classes of employees to which workers (or plaintiffs) belonged. The new rule is limited both in time and in scope: *"If the facts demonstrate that the employer has an actual practice of making improper deductions, the exemption is lost [only] during the time period in which the improper deductions were made [and only] for employees in the same job classification working for the same managers responsible for the actual improper deductions."*⁸¹ It is also noteworthy that unlike the current rule (Sec. 541.118A(a)(6)), paragraphs (a) and (b) of the new rule do not even require that the employer promise to comply in the future.

To demonstrate the unsoundness of this approach it is only necessary to examine a few hypothetical cases. Suppose an employer has three sections of 20 engineers each (engineers are the example given in the regulations) all in the same job classification who are managed by managers A, B and C. If six employees in A's section have improper deductions made in January, June, August and December, and no employees in B's section or C's section have any improper deductions, and no clearly communicated policies are found, it seems to follow that the employees in A's section lose the exemption from January through December (or, perhaps, only in the four specific months when the improper deductions actually occurred). Making a small change in the hypothetical, if 40 of the engineers work in A's section and the rest in C's, the 40 in A's section would lose the exemption from January through December as above. On the other hand, if three employees in A's section have improper deductions made in January and March, and three employees in B's section have improper deductions made in June and August, perhaps the employees in A's section lose the exemption only for January through March, while those in B's section lose the exemption only in June through August. The result that all employees in the A and B sections, who, if all were in a single section would all lose the exemption from January through December, should all likewise lose the exemption from January through December in this hypothetical, is apparently not possible under the language of the regulation. Similar examples of irrational outcomes can be multiplied.

Under the current rules, a policy or practice of making deductions from the compensation of employees who are claimed to be exempt, and thus are due to be paid "on a salary basis," carries with it risk, for examination may reveal that the salary basis test has not been met and that the employees involved - generally all who are similarly situated - will be entitled to overtime for their hours worked over 40 in each week during which they were not so paid. The Department has by the new rule reduced the economic risk described by a huge amount, and thus made questionable salary deductions a much more attractive gamble. Under the new rules the

⁸⁰ 29 C.F.R. 541.118(a).

⁸¹ Sec. 541.603(b).

loss of exemption, which previously would have covered two years' work at least for similarly situated employees, now covers only "*the time period in which the improper deductions were made*" and only "*employees in the same job classification working for the same managers responsible for the improper deductions.*"⁸²

Furthermore, the final provision of the new "window of correction" regulation is the one which really makes the entire "salary basis" requirement - for all practical purposes - inoperative. This section provides that if the employer (1) has a clearly communicated policy that prohibits improper pay deductions and includes a complaint mechanism; (2) reimburses employees for any improper deductions; and (3) makes a good faith commitment to comply in the future, the employer will not lose the exemption (for any employee) unless the employer then goes on to willfully violate the policy by continuing to make improper deductions after receiving employee complaints. This section so effectively limits the risk of having to pay overtime that it seems that an employer who adopts a policy along the lines described can get away with ignoring the question of whether any deductions made are permissible or not - shifting to employees the responsibility to figure out whether their deductions are impermissible and then complain to that effect. After an employee discerns the improper payment and if he or she is courageous enough to complain, the employee receives what he or she should have received in the first place. The employer, who has enjoyed the benefit of not paying overtime throughout, need merely affirm the intention to pay employees claimed to be exempt on a salary basis in the future.

The Preamble to the new regulations tells us that it has been a burden for employers to consult counsel about the complex provisions of the exemption rules. Under this provision of the new rules, the burden has been effectively shifted to employees to consult counsel concerning these complex provisions, and, if they are not being correctly followed, to identify themselves to the employer so as to receive a reimbursement of the salary payment advertised, rather than receiving the overtime which failure to make payment "on a salary basis" is said, under the prominent provisions of the rules, to entail.

Finally, the Department reveals its intent to broaden the availability of the exemptions by its addition to the rule of a new exemption-saving concept. Instead of reasserting its historic view that the burden of proving any exemption falls strictly on the employer claiming it, the new rule provides that provisions regarding the effect of improper deductions from salary "*shall not be construed in an unduly technical manner so as to defeat the exemption*" (emphasis added).⁸³ The Department by this provision gives the benefit of a generous construction of the rule to the employer rather than the employee, in a manner that seems inconsistent with the Department's core mission.

⁸² Sec. 541.603(b).

⁸³ Sec. 541.603(e).