National Employment Lawyers Association

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Director
Division of Regulations, Legislation, and Interpretation
Wage and Hour Division
United States Department of Labor
Room S-3502
200 Constitution Avenue, NW
Washington, DC 20210

Re: National Employment Lawyers Association's Comments Regarding RIN 1235-AA39 – Defining and Delimiting the Exemptions for Executive, Administrative, Professional, Outside Sales, and Computer Employees

Dear Ms. DeBisschop:

This letter provides the Department of Labor (DOL) with the collective comments of more than 1,500 members of the National Employment Lawyers Association (NELA) and its 69 affiliates concerning the proposed changes to the regulations applicable to executive, administrative, and professional employees ("the EAP exemption") under the Fair Labor Standards Act (FLSA).

NELA is the largest professional membership organization in the country comprised of lawyers who represent employees in labor, employment, wage and hour, and civil rights disputes. Our mission is to advance worker's rights and serve lawyers who advocate for equality and justice in the American workplace. NELA and its 69 circuit, state, and local affiliates have a membership of over 4,000 attorneys who are committed to working on behalf of those who have faced illegal treatment in the workplace in both the public and private sector, including employer violations of federal wage and hour laws. NELA has filed numerous amicus curiae briefs before the United States Supreme Court and other federal appellate courts regarding the proper interpretation of federal civil rights and worker protection laws and comments regularly on relevant proposed rules. NELA is committed to advocating for a narrow interpretation of exemptions under the FLSA. These comments were drafted by members of NELA's Wage and Hour Committee who have been involved in wage and hour litigation for decades and are intimately familiar with the current regulations.

While NELA agrees with the Department's proposal to increase the threshold salary level to qualify for the EAP exemption, and to automatically update the applicable salary level on an annual basis (to ensure that qualifying salaries will not soon become outdated), NELA advocates for a larger monetary increase to the required salary level. NELA also offers suggestions for

additional changes that should be made to the pertinent regulations in order to preserve Congress' intent that the EAP exemption be strictly limited to "bona fide" executives, administrators, and professionals. NELA appreciates this opportunity to provide these comments.

I. INCREASE TO SALARY THRESHOLD AND AUTOMATIC COST OF LIVING ADJUSTMENT.

Although NELA supports a proposed increase to the salary threshold, the amount of the increase must be larger to effectively protect workers whose rights are central to the purposes of the FLSA. A more substantial increase to the salary threshold is also critical to restore the salary threshold to prior economic values and to meaningfully reflect the salaries of the "bona fide" executives, administrators, and professionals whom Congress intended to exclude from the FLSA's protections.

A. The Standard Salary Threshold Is The "Most Effective" Check On The Validity Of White Collar Exemption Claims.

In passing the FLSA, Congress sought to remedy "labor conditions detrimental to the maintenance of the minimum standard of living necessary for health, efficiency, and general well-being of workers." 29 U.S.C. § 202. The core elements of its solution were guarantees of a minimum wage and overtime compensation for hours worked over 40 per week. *See* 29 U.S.C. §§ 206-07. "The legislative history of the overtime compensation provisions of the FLSA reveal a threefold purpose underlying them: (1) to prevent workers who, perhaps out of desperation, are willing to work abnormally long hours from taking jobs away from workers who prefer shorter hours, including union members; (2) to spread available work among a larger number of workers and thereby reduce unemployment; and (3) to compensate overtime workers for the increased risk of workplace accidents they might face from exhaustion or overexertion." *Parker v. NutriSystem, Inc.*, 620 F.3d 274, 279 (3d Cir. 2010).

At the center of the Department's NPRM is the EAP exemption, which covers those "employed in a bona fide executive, administrative, or professional capacity." 29 U.S.C. § 213(a)(1). Congress did not define these terms in the statute itself, but instead charged the Department with "defining[ing] and delimit[ing]" which employees fall under this provision. *Id.* From the outset, the Department's regulations construed the exemption as intended only for a limited set of employees at the top of the economic ladder who did not need protection because they were not subject to the low wages and long hours that FLSA remedies.

The reach of the EAP exemption is limited. Section 13(a)(1) was not intended to exclude all or even most white-collar workers from the FLSA's protections. The Department's 1940 Stein Report wholly rejected the premise "that all salaried white-collar workers enjoy satisfactory working conditions." *See "Executive, Administrative, and Professional . . . Outside Salesman Redefined: Report and Recommendations of the Presiding Officer at Hearings Preliminary to Redefinition*," (Washington: U.S. Govt. Print. Off., 1940) (hereinafter "Stein Report") at p.8. It presented evidence that despite their "white collar" titles and salaries, these

employees encountered labor conditions that, the Report found, were often "detrimental to health, efficiency, and general well-being." *Id.* Unlike true executives, these "white collar" workers often were deserving of overtime compensation, either based on their low salary and/or job duties. An assistant manager who works 60 hours a week for a salary of $40,000 per year is plainly in this category.

From the inception of the FLSA, the Department expressed concern that employers would improperly classify their employees in certain administrative, executive, or professional job positions to avoid paying them the overtime compensation they deserved. In 1938, in its first regulations on the EAP exemption, the Department introduced the minimum salary threshold in response to this concern. *See* 3 FR 2518. Below the minimum salary threshold, an employee is entitled to FLSA protections regardless of his or her title or job duties. Over the nearly eight decades that the Department has construed the EAP exemption, it has always viewed the exemption as triggered not only by an employee's job duties, but also on the amount of an employee's salaried wages. Compensation for bona fide executives, administrators, and professionals takes the form, for example, of "wages well above the minimum" and privileges making up for the lack of overtime pay, such as "authority over others, opportunity for advancement, paid vacation and sick leave, and security of tenure." *See* Report of the Minimum Wage Study Commission, vol. 4, (Washington: U.S. Govt. Print. Off., 1981) (hereinafter "1981 MWSC Report") at p.243. Managerial titles and salaried status by themselves do not remove the need for the FLSA's protections unless *also* accompanied by considerably higher compensation and privileges.

The Department recognizes that the standard salary threshold is an indispensable bright-line test that gives meaning to the "bona fide" language of the EAP exemption. As the Department noted in 1940*, "[t]he final and most effective check on the validity of the claim for exemption is the payment of a salary commensurate with the importance supposedly accorded the duties in question." See* Stein Report at p.19 (emphasis added). It similarly commented in 1981 that "some employees whose duties conform to the specifications set out in the regulations may not be receiving the compensatory privileges that are considered a vital part of the character of employment exempted under this provision of the FLSA. Thus, a salary commensurate with the duties and responsibilities expected of an executive, administrative, or professional employee has traditionally been considered to be 'the single best test of the employer's good faith.'" *See* 1981 MWSC Report at p.243. If an employee is not earning this minimum threshold, then he or she clearly is not a bona fide executive. As the Minimum Wage Study Commission noted in 1981, the lower the salary threshold, the easier it is "for employers to claim the exemption for workers who would otherwise be entitled to premium pay for overtime . . . defeat[ing] the 'good faith' aspects of the test." *See* 1981 MWSC Report. This remains a problem today.

As explained below, NELA proposes that the Department adopt a current salary threshold of **$1,145 per week** based on the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region. This is the same increase to the salary threshold that the Department proposed in 2016. *See* 88 FR 62156.

B. The Standard Salary Threshold Applicable to the EAP Exemption Should Be Raised to $1,145 Per Week.

NELA strongly supports the Department's proposal to increase the standard salary threshold, but believes the amount of the increase is not large enough. Under the current proposal, too many employees whom Congress intended to protect under the maximum hour provisions of the FLSA will remain improperly exempted. For this reason, NELA recommends that the Department adopt a threshold reflecting the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region, or $1,145 per week.

As the current proposed Rule explains, "in 2016 the Department set the standard salary level at the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (the South), which produced a salary level that was at the low end of the historical range of short test salary levels." 88 Fed. Reg. 62156. "This approach restored overtime protection for employees performing substantial amounts of nonexempt work who earned between the long and short test salary levels, as they failed the new salary level test." *Id.* at 62163. NELA believes that the 40th percentile continues to represent a better measure to determine exempt status under the white-collar exemptions and should again be adopted by the Department, despite the successful legal challenge to the 2016 rule.

In May 2016, a Texas district court enjoined the 2016 rule and declared the rule invalid, in part, because the rule allegedly conferred overtime eligibility on too many employees who would otherwise be exempt. But as explained in detail by the Economic Policy Institute ("EPI"), the Texas district court "based his decision on fundamentally flawed economic logic."[1] According to EPI, there were no grounds for the Texas court to conclude that the 2016 salary threshold was so high that it displaced the role of the duties test. *Id.* The 2016 final rule contained analysis "that among white-collar workers who failed the duties test – and were thus eligible for overtime – nearly half earned above the 2016 salary level. This means that among white-collar salaried workers who were eligible for overtime as a result of their duties, nearly half had their overtime eligible status determined by the duties test alone, demonstrating that the duties test was not remotely 'displaced' by the 2016 salary threshold but was, in fact, essential. *Id*., citing 81 FR 32465.

NELA agrees with the Department's 2016 analysis, and the Department's acknowledgement in current proposed Rule, that "[s]etting the salary level at the 40th percentile of weekly earnings of fulltime salaried workers in the lowest wage Census Region would reduce the impact of a one-test system on lower paid white-collar employees who perform significant amounts of nonexempt work. This percentile is midway between the 30th and 50th percentiles and would produce a salary level ($1,145 per week) that is roughly the midpoint between the long and short test salary levels." 88 FR 62168. As the proposed Rule explains, "of the approximately 10.3 million salaried white-collar employees who earn between the long and short test salary levels, approximately 47 percent earn between the long test salary level and $1,145

[1] See, https://www.epi.org/publication/the-court-decision-invalidating-the-2016-overtime-rule-was-based-on-fundamentally-flawed-economic-logic/

and would receive overtime protection by virtue of their salary, while approximately 53 percent earn between $1,145 and the short test salary level and would have their exemption status turn on whether they meet the duties test." *Id.* The Department's articulated concerns about setting the salary threshold at the 40th percentile, as opposed to its preferred 35th percentile, are misplaced.

The reality is that the salary threshold can be set substantially higher than the salary threshold in the 2016 final rule and still easily avoid the false concerns raised by the Texas district court that invalidated the 2016 rule. See https://www.epi.org/publication/the-court-decision-invalidating-the-2016-overtime-rule-was-based-on-fundamentally-flawed-economic-logic/ for a detailed debunking of the economic analysis used by the Texas district court. As a result, the 40th percentile is still conservative by any measure.

The Department's proposed 35% salary threshold is also too low from a historical perspective. The 1958 Kantor Report characterized the salary threshold as an "index of the status that sets off the bona fide executive from the working squad-leader." *Report and Recommendations on Proposed Revisions or Regulations, Part 541, Defining the Terms "Executive," "Administrative," "Professional," "Local Retailing Capacity," [and] "Outside Salesman."* (Washington: U.S. Govt. Print. Off., 1958) ("hereinafter Kantor Report") at p.4. The proposed change would raise the salary threshold to only $1,059 per week and $55,068 per year. This will result in only 27% of the Nation's full-time salaried workers becoming overtime eligible without the need to also analyze their specific job duties to determine their exempt status. *See* 88 FR 62170. Bolder federal action is required. Under the short test salary threshold that the Ford Administration established in 1975, 62% of full-time salaried workers were eligible for overtime protection based on a salary threshold test.[2] Further, "[w]hen the Ford administration raised the salary threshold in 1975, it was 1.57 times the median wage."[3] Even the Department's own 2015 overtime rule notice of proposed rulemaking acknowledges that the FLSA's overtime salary threshold has historically ranged between the 35th to 55th percentile of weekly earnings of full-time salaried workers nationwide. 80 FR 38534.

Thus, there is ample historical precedent for raising the overtime threshold to the 40th percentile of weekly earnings in the Nation's lowest-wage Census Region and still be well within historical norms. Such a benchmark will restore the salary threshold closer to past averages, when the majority of salaried workers enjoyed overtime pay protections—and the benefits of a 40-hour workweek, and the higher compensation that comes with it.

C. The Salary Threshold Applicable to the HCE Exemption Should Be Raised to $172,796.

The Department implemented the HCE exemption in 2004. *See generally* 69 FR 22121. As the Department observed, "[t]he HCE test's primary purpose . . . is to serve as a streamlined alternative for *very highly* compensated employees because a *very high* level of

[2] See, https://www.epi.org/publication/whats-at-stake-in-the-states-if-the-2016-federal-raise-to-the-overtime-pay-threshold-is-not-preserved/.
[3] See, https://www.epi.org/publication/ib381-update-overtime-pay-rules/.

compensation is a strong indicator of an employee's exempt status, thus eliminating the need for a detailed duties analysis." 88 FR 62175 (citing 69 FR 22173-74) (emphasis supplied). Consistent with this purpose, the Department sought to create an annual compensation level that would strictly limit the exemption to those employees "***at the very top of [the] economic ladder***." 69 FR 22174 (emphasis supplied). Establishing a "very high" compensation level was necessary to, *inter alia*, "avoid the unintended exemption of large numbers of employees – such as secretaries in New York City or Los Angeles – who clearly are outside the scope of the exemptions and are entitled to the FLSA's minimum wage and overtime pay protections." 69 FR 22174; *see also id.* (HCE annual compensation level set to ensure that, for "virtually every salaried 'white collar' employee," employer would be required to satisfy *all* of EAP exemption's "duties" requirements in order to classify employee as overtime-exempt).

In 2016, the Department increased the HCE exemption's annual compensation requirement from $100,000 to $134,004. *See* 81 FR 32550. This new requirement coincided with the earnings of the 90th percentile of full-time salaried employees nationwide. *See* 88 FR 62176.

With respect to the current proposed rule, the Department asserts that it "considered setting the HCE threshold at the 90th percentile, like in its 2016 rule," but ultimately declined due to "concern[] that the resulting compensation level ($172,796) could unduly restrict the use of the HCE exemption for employers in lower-wage regions and industries." 88 FR 62176.

NELA disagrees with the Department's refusal to adopt the 90th percentile threshold of $172,796 in the current proposed rule. As indicated in Table 28 of the current Notice, utilization of the $172,796 threshold (rather than the proposed $143,988 threshold) will ensure that an *additional* 46,000 salaried employees are entitled to overtime wages *unless* they satisfy *all* of the EAP exemption's duties requirements. *See* 88 FR 62218.

The Department contends that the proposed $143,988 threshold "would be sufficient to guard against the unintended exemption of workers who are not bona fide executive, administrative, or professional employees." 88 FR 62176. But, if this is so, employers should have little trouble satisfying a robust duties test for those employees whose annual compensation falls between $143,988 and $172,796.

Simply put, NELA fails to understand why the Department would prevent approximately 46,000 salaried employees from enjoying the relatively modest protection of requiring their employers to satisfy a robust duties test before classifying them as overtime-exempt.

Moreover, as the Supreme Court recently observed in an opinion addressing the HCE exemption, the FLSA's overtime mandate was enacted to, *inter alia*, "increase overall employment by incentivizing employers to widen their "distribution of available work." *Helix Energy Solutions Group, Inc. v. Hewitt*, 143 S. Ct. 677, 682 (2023). This public policy is especially important with respect to those "highly compensated" positions that lower-paid salaried workers strive to obtain. Make no mistake: an overly-permissive HCE exemption will

result in fewer "highly compensated" jobs available for workers aspiring to climb the economic ladder to benefit themselves and their families.

In sum, the HCE compensation requirement must truly reflect what it means to be a *highly compensated* employee in today's economy. In drawing this line, the Department should follow the methodology utilized in 2016 and implement a $172,796 threshold.

D. Both Salary Thresholds Should Be Indexed.

NELA endorses the proposal to index both the standard and HCE compensation levels. Indexing is necessary to preserve the real value of both salary measures, which are prone to substantial diminution over time.

Between 1938 and 1975, the Department increased the salary level every five to nine years. 80 FR 38526. Following the 1975 rulemaking, however, 29 years passed before the salary level was again raised. *Id*. In the 2004 Final Rule, the Department expressed a commitment to updating the salary levels ''on a more regular basis,'' particularly when ''wage survey data and other policy concerns support such a change.'' 69 FR 22171. Of course, this did not happen at a tremendous cost in real dollars to working people. Absent an automatic updating mechanism allowing for regular and more predictable updates to the earnings thresholds, the real value of any fixed threshold simply erodes over time. For example, under the Department's 1975 regulations, the real value of the short test salary threshold of $250, as of June 2023, is approximately $1,452.90 per week, or $75,550.80 per year. *See*, https://www.bls.gov/data/inflation_calculator.htm. Hard-working Americans entitled to overtime compensation should not suffer the economic consequences of the political paralysis and administrative delay that prevents more frequent and necessary updates to the salary threshold test.

Fortunately, there is a fix to this problem, and it is contained in the Department's indexing proposal. Automatically adjusting the salary thresholds will ensure that that workers whose employment requires them to work overtime hours will benefit from thresholds that keep pace with inflation, no longer subjecting workers to figures devised nearly three decades earlier (as occurred between the 1975 and 2004 updates). Many states already index their minimum wage laws. As of July 1, 2023, the minimum wage is indexed for cost of living in 19 states and Washington, D.C., showing that indexing is a practical alternative to the current scheme. https://www.epi.org/minimum-wage-tracker/ (last visited Oct. 9, 2023).[4] Indexing saves administrative resources by ensuring that the Department does not expend considerable time, money, and energy to calculate new thresholds each time it updates based on economic change. With indexing, the Department can simply and effectively comply now *and* in future years with its duty to properly delimit the EAP exemption.

[4] Alaska, Arizona, Colorado, Connecticut, Florida, Maine, Minnesota, Missouri, Montana, Nebraska, Nevada, New Jersey, New York, Ohio, Oregon, South Dakota, Vermont, Virginia, Washington, and Washington D.C.

Moreover, indexing based on fixed earnings percentiles is most consistent with the Department's express explanations for the proposed salary thresholds. The NPRM sets the thresholds at the 35th and 85th percentiles of full-time salaried workers. If the appropriate salary threshold for *today* is based on the percentage of the full-time salaried workforce earning below the threshold, then it follows logically that this would be the basis for the most appropriate salary threshold at *future* points in time. Although NELA contends that these chosen percentiles should both be higher, we maintain that, whatever percentiles the Department ultimately adopts, indexing these figures to fixed earnings percentiles is the fairest way to maintain consistency in workers' FLSA eligibility in light of inevitable economic change. It is also likely to be many years—even decades, given historical trends—before the Department decides to adjust fixed salary thresholds again. In light of these well-established facts, indexing represents the only simple and accurate means of preserving the real value of both the standard and HCE thresholds over time. Nor should the Department be concerned that the 2016 Rule utilizing the 90th percentile compensation amount was invalidated in *Nevada v. U.S. Dept. of Labor*, 275 F. Supp. 3d 795 (E.D. Tx. 2017). There is no indication that the outcome of that forum-shopped litigation would have been different had the Department adopted a more modest compensation threshold. *See id.* Moreover, another district court has correctly held that the Department acts well within its authority in setting the HCE threshold amounts. *See Mayfield v. U.S. Dept. of Labor*, 2023 WL 6168251, 2023 U.S. Dist. LEXIS 168054 (W.D. Tx. Sept. 20, 2023).

II. WHILE NELA IS IN OVERALL AGREEMENT WITH THE DEPARTMENT'S PROPOSAL TO INCREASE AND INDEX THE SALARY LEVEL TEST, THE DEPARTMENT SHOULD FURTHER STRENGTHEN THE "DUTIES TESTS" FOR THE EAP EXEMPTIONS.

The low salary level adopted by the Department in 2004 has *increased* litigation of EAP exemption disputes. That is because with the salary level test set so low, employers continued to designate low-wage employees as exempt executives or exempt administrative employees where their salary levels could not otherwise support any reasonable finding that these low wage workers were "bona fide" executives or administrators. With a salary level test restored to its historical moorings, there should be fewer disputes over purported executives or administrators who are earning poverty level wages. NELA's proposed salary level test should obviate unnecessary litigation over the duties tests. This will conserve the Department's enforcement resources and reduce the workload of our federal court system.

However, NELA submits that the duties tests can and should be strengthened to better carry out the fundamental policies and legislative purposes underlying the FLSA.

A. Employees Must Spend At Least Fifty Percent of Their Time Performing Exempt Work to Qualify for Exemption.

Courts have mistakenly found that employees who spend only a small portion of their work time on exempt duties may nonetheless have exempt work as their primary duty. *See*, *e.g.*, *In re Family Dollar FLSA Litig*., 637 F.3d 508 (4th Cir. 2011) (store managers who spent up to 99% of time performing non-exempt tasks could still be exempt); *Soehnle v. Hess Corp.*, 399

F.Appx. 749 (3d Cir. 2010) (gas station manager exempt notwithstanding she spent 85% of her time on non-managerial duties); *Baldwin v. TrailerInns, Inc.*, 266 F.3d 1104, 1113-4 (9th Cir. 2001) (exempt but "vast majority of their work week spent on manual labor"); *Sappington v. Styleline Furniture*, 2007 WL 3355838 (N.D. Miss. Nov. 8, 2007) (exempt but worked 75% of time on non-exempt tasks). The regulations should be revised to prevent this injustice. NELA believes the intent of the regulations, as embodied by the rule of thumb test that the primary duty is the work an employee does the majority of their time, should not allow an employee who spends less than 50% of their work time on exempt duties to be found as having exempt work as the primary duty.

NELA supports the adoption of California's 50% quantitative model for all of the EAP exemptions. California's 50% quantitative model has been used successfully in that state for many years. Practitioners have found this standard to be protective of the restrictive nature of exemptions from the general rule of overtime for workers. A 50% rule would achieve greater consistency and predictability for the EAP exemptions and is easier for employers and courts to apply.

Unlike a qualitative test, the 50% standard can be objectively measured. Once the work duties of a position are categorized as exempt or non-exempt, an employer need only track the amount of time each type of duty is performed for a representative period. This does not require an expensive time-motion study or employee-by-employee analysis. Once an employer conducts the initial job analysis, it does not need to do so again unless there is a significant change in the job duties of the position.

The 50% standard ensures the exemptions apply only to those who are truly performing exempt work. The white collar classifications are exemptions to the general rule that workers should be paid overtime. As such, the standards should be rigorous. A 50% rule would require that those who are called "managers" truly spend their time managing. It would prevent an employer from taking advantage of an employee by giving her a slightly higher salary, but tasking her with primarily non-exempt duties and requiring HER to work 60 to 80 hours a week without overtime. This is unfortunately routine for many workers NELA practitioners represent.

The bright-line rule NELA proposes would also decrease the amount of litigation and litigation cost. A rule that is simple to apply would result in greater compliance and the areas of argument between employees and employers would be smaller under such a regime. Moreover, the bright-line test minimizes uncertainty over the "primary duty" of an employee's job.

B. The Department Should Eliminate The "Concurrent" Duties Regulation for Executive Employees Because It Results in Misclassification of Employees Who Perform Primarily Non-Exempt Work and Is Inconsistent With the FLSA.

The concurrent duties regulation set forth in 29 C.F.R. 541.106 has resulted in the overbroad application of the white collar exemptions. Employees have been determined to be exempt who spend the majority of their time on non-exempt duties—working alongside non-

exempt workers—based on the illusion that they are simultaneously managing while they perform non-exempt tasks. *See Family Dollar, Soehnle*, *Baldwin*, and *Sappington*, above. The Department should do away with the regulation and clarify that, to be a bona fide executive, an employee must ***actually*** perform management duties. An employee cannot be managing while "serving customers, cooking food, stocking shelves and cleaning the establishment," as the regulation presupposes. This is fantasy. These manual labor tasks do not permit an employee to be performing the types of management duties set forth in 29 C.F.R. 541.102, such as "interviewing, selecting, and training of employees; [or] setting and adjusting their rates of pay and hours of work."

The concurrent duties regulation has enabled employers to implement staffing models and payroll budgets that simply shift non-exempt work hours onto the backs of salaried "managers". This practice hurts both the purported managers (who must work long hours without receiving any additional pay) and hourly staff (who are denied the opportunity to work additional hours).

C. The Department Should Reaffirm and Strengthen the Continued Vitality of the Administrative/Production Dichotomy in Construing the Administrative Exemption.

As the preamble to the most recent revised regulations explained in 2004, the administrative/production dichotomy is "a relevant and useful tool in appropriate cases to identify employees who should be excluded from the exemption" and is "determinative if the work falls squarely on the production side of the line." 69 FR 22122, 22141 (internal quotations and citations omitted). The "administrative versus production" dichotomy test has long been codified as 29 C.F.R. § 541.205(a) and courts have routinely applied the test to ensure that workers deserving of overtime protection are not misclassified as exempt administrators.

Analyzing that dichotomy, courts have long distinguished between "administrative" employees, who are "running the business itself or determining its overall course or policies" from the production workers engaged in the "day-to-day handling of the business affairs." *Bothell v. Phase Metrics, Inc.*, 299 F.3d 1120 (9th 2002); *see also Bratt v. County of Los Angeles*, 912 F.2d 1066, 1070 (9th Cir. 1990) *cert. denied* 498 U.S. 1086 (1991); *Dalheim v. KDFW-TV*, 918 F.2d 1220, 1231 (5th Cir. 1990) (distinguishing between "those employees whose primary duties are administering the business affairs of the enterprise" ("administrators") from those whose "primary duty is producing the commodity or commodities, whether goods or services, that the enterprise exists to produce and market" ("production workers")); *Rock v. Ray Anthony Intern., LLC,* 380 Fed.Appx. 875, 878 (11th Cir. 2010) ("[p]roduction work relates to the goods and services that the business contributes to the marketplace, whereas administration relates to running the business."); *Schaefer-LaRose v. Eli Lilly & Company*, 679 F.3d 560, 574 (7th Cir. 2012) ("[W]hen an employee is engaged in the core function of a business, his or her task is not properly categorized as administrative."); and *Fowler v. OSP Prevention Group, Inc.*, 38 F.4th 103, 110 (11th Cir. 2022) ("Production employees who perform the core function of the business are not transformed into administrative employees just because the work they do is essential to what the company sells — its 'marketplace offerings.'") (citing *Bothell*, 299 F.3d at 1127).

This distinction is increasingly important in the modern economy where more companies offer services to the public, rather than producing traditional, assembly-line goods, and courts have appropriately utilized analysis of the dichotomy in weighing the administrative exemption. *See Cotten v. HFS-USA, Inc.,* 620 F.Supp.2d 1342, 1348 (M.D. Fla. 2009) ("Application of the distinction between production and administrative duties is not limited to the traditional manufacturing context. In a service industry, production activities relate to the "primary service goal" of the entity."); *Rood v. R&R Express, Inc.*, 2022 WL 1082481, *6 (W.D. PA, April 11, 2022) ("But "[t]he concept of a 'production worker' is not limited to individuals involved in the manufacture of tangibles"…Rather, the "administrative/production dichotomy turns on whether the services or goods provided by the employee constitute the marketplace offerings of the employer, or whether they contribute to the running of the business itself.") (citations omitted); and *Davis v. J.P. Morgan Chase & Co.*, 587 F.3d 529, 535 (2d Cir. 2009) ("[W]e have drawn an important distinction between employees directly producing the good or service that is the primary output of a business and employees performing general administrative work applicable to the running of any business."). Courts should continue to use the administrative/production dichotomy, as it has been universally recognized as a useful analysis tool in a myriad of cases weighing the applicability of the administrative exemption. *See, e.g., Walsh v. Until Serv. Corp.*, 64 F.4th 1, 7 (1st Cir. 2023) (recognizing the continued utility of the administrative/production dichotomy).

In addition, the Department itself has utilized the administrative/production dichotomy in its prior FLSA Opinion Letters. *See* Opinion Letter Fair Labor Standards Act (FLSA) 2010 WL 1822423, March 24, 2010. The 2010 Opinion Letter involved mortgage loan officers and ultimately held that the administrative exemption did not apply because the duties do not relate to the "internal management" or "general business operations" of the company, for example like a company's HR department, accounting department, or research department, but rather involve the day-to-day carrying out of the employer's business, i.e. the "production side" of the business. *Id.* at *7. The 2010 Opinion Letter also cites numerous cases (some of which are cited above) discussing the dichotomy and cases applying the analysis in determining the administrative exemption. *Id.* at *3-6.[5]

The Department's continued recognition of the validity and utility of the administrative/production dichotomy in the newly promulgated regulations would buttress a well-established tool routinely used by the courts in appropriate cases to determine whether employees were truly exempt administrators. NELA urges the Department to adopt a regulation that explicitly recognizes that "administrative" employees are those who are "running the business itself [that is, the business of the employer—not the business of the employer's customer] or determining its overall course or policies" rather than production workers engaged in the "day-to-day handling of the business affairs" or whose activities relate to the "primary service goal" of the business.

[5] Many of the cited cases involve using the analysis to employees whose primary duties involve sales, a common administrative exemption issue.

D. The Fluctuating Workweek Method of Overtime Compensation Should Not Be Available to Employers Who Misclassify Salaried Employees as Overtime-Exempt.

The Department's proposed rules are presently silent as to how damages for unpaid overtime hours are to be calculated in the event employees are determined to be misclassified as exempt under the EAP exemption. Employers often assert that the appropriate method for calculating damages for a misclassified employee is the FWW method of calculating overtime compensation found in 29 C.F.R. § 778.114. Misclassified employees on the other hand argue that they are entitled to what their full rate of pay would have been absent a violation.

In order to protect the rights of those who are misclassified, the Department should clarify that the FWW cannot be used to calculate damages when an employee is denied overtime due to misclassification. A position by the Department on this issue is appropriate as it aligns with the Departments efforts "to ensure that the FLSA's intended overtime protections are fully implemented" and that the outcome "fully reflect[s] the purpose of the exemption[s]."

NELA believes that the Department taking a position on the appropriate damage calculation is necessary to adequately protect the rights of employees. Application of the FWW in misclassification claims results in employees being denied appropriate overtime damages in multiple regions of the country. As one district court explained:

> Application of the FWW in a misclassification case gives rise to a "perverse incentive" for employers, because the employee's hourly "regular rate" decreases with each additional hour worked. In fact, the difference between the FWW method and the traditional time-and-a-half method can result in an employee being paid seventy-one percent less for overtime over a given year, and under the FWW method, the effective overtime hourly rate of an employee working sixty-one hours or more is less than the non-overtime hourly rate of an employee who worked no more than forty hours per week.

Blotzer v. L-3 Communs. Corp., 2012 U.S. Dist. LEXIS 173126, *38 (D. Ariz. Dec. 5, 2012) (citations omitted).

The FWW is often said to have origins in the U.S. Supreme Court's decision *Overnight Motor Transp. Co. v. Missel*, 316 U.S. 572 (1942), which was decided only a few years after the FLSA was enacted. In *Missel*, the plaintiff was a rate clerk for a trucking company. He had a contract with his employer to be paid a fixed weekly amount for all his hours worked which fluctuated, but was not paid overtime. The employer made an argument tantamount to that the regular rate, as a default, should be the minimum wage and therefore it had already compensated the plaintiff for any minimum and overtime wages due. The Supreme Court disagreed stating that "[i]mplication cannot mend a contract so deficient on complying with the law" … and determined that the regular rate in this situation was to be paid by dividing the plaintiff's fixed weekly amount by all his hours worked. *Id*. at 581.

In 1968 the Department issued 9 C.F.R. § 778.114 addressing the payment of overtime to salaried employees "who do not customarily work a regular schedule of hours," and indicated that it was issued in connection with two Supreme Court cases that had addressed payment of overtime to employees who had fluctuating hours from week-to-week, and who wished to receive a predictable, flat rate of pay. The Department's interpretative bulletin sets forth requirements that must be satisfied in order for an employer to utilize the FWW method of calculating overtime pay: (1) the employee's hours fluctuate from week to week, (2) the employee receives a fixed weekly salary that remains the same regardless of the number of hours worked per week; (3) the fixed salary is sufficient to provide compensation at a regular rate not less than the legal minimum wage; (4) the employee receives at least 50 percent of his regular hourly pay for all overtime hours worked; and (5) the employer and the employee have a clear mutual understanding that the fixed salary is compensation (apart from overtime premiums) for the hours worked each workweek. 9 C.F.R. § 778.114.

Thus, in order to ensure employees receive all benefits bestowed upon them by the FLSA, the Department should clarify that the FWW articulated in 29 C.F.R. § 778.114 and the approach used in *Missel* is not the appropriate method for calculating damages when an employee has been misclassified as a salaried-exempt employee pursuant to the Executive, Administrative, Professional, Outside Sales, or Computer employee exemptions.

1. Court Opinions Support Clarification That Reliance on 29 C.F.R. § 778.114 is Improper to Calculate Damages in Misclassification Cases.

Numerous courts have rejected the retroactive applicability of the FWW, as set forth in 29 C.F.R. § 778.114, to calculate damages in an FLSA misclassification cases. *See Snodgrass v. Bob Evans Farms, LLC*, 2015 U.S. Dist. LEXIS 33621(S.D. Ohio Mar. 18, 2015) (collecting cases); *Urnikis-Negro v. American Family Property Services*, 616 F.3d 665 (7th Cir. 2010) (collecting cases). In *Snodgrass*, the court explained "[t]he requirements of § 778.114 can never be satisfied in a misclassification case, however, because (1) there are no contemporaneous payments of overtime, and (2) there is no clear mutual understanding." 2015 U.S. Dist. LEXIS 33621 at *26; *see also West v. Verizon Services Corp*., 2011 U.S. Dist. LEXIS 5952, *30-31 (M.D. Fla. Jan. 21, 2011); *Russell v. Wells Fargo & Co*., 672 F.Supp.2d 1008, 1013-15 (N.D. Cal. 2009); *Scott v. OTS Inc*., 2006 U.S. Dist. LEXIS 15014, *35-40 (N.D. Ga. March 31, 2006); *Rainey v. American Forest and Paper Assoc.*, 26 F.Supp.2d, 100-01 (D.D.C. 1998). [T]he FWW methodology set forth in the DOL bulletin was never intended to be applied retroactively in a case where an employee has been misclassified as exempt." *O'Neill v. Mermaid Touring, Inc.,* 968 F.Supp.2d 572, 586 (S.D.N.Y. 2013). The reasoning for rejecting the use of a FWW in misclassification cases under both 29 C.F.R. § 778.114 and *Missel* was precisely presented by the court in *Ransom v. M. Patel Enters., Inc.,* 825 F.Supp.2d 799, 809 n.11 (W.D. Tex. 2011) (overruled by *Ransom v. M. Patel Enters*., 734 F.3d 377, 387 (5th Cir. 2013)).

> The fundamental assumption underpinning the FWW is that it is fair to use it to calculate overtime pay because the employee consented to the payment scheme. But in the context of an FLSA misclassification suit when consent is inferred from

> the employee's conduct, that conduct will always, by definition, have been based on the false assumption that he was not entitled to overtime compensation. The job will have been advertised as a salaried position. The employee, if he raised the issue, will have been told that the salary is all he will receive, regardless of how many hours he works. That is the very nature of a salaried, exempt position. When it turns out that the employer is wrong, and it is learned that the FLSA required the employer to pay the employee an overtime premium, the notion that the employee's conduct *before* he knew this is evidence that the employee somehow consented to a calculation method for the overtime pay *that no one even knew was due,* is perverse. If the FWW requires consent in some fashion, the employee's actions before he knew he was due overtime pay just cannot logically be the basis of that consent.

Ransom, 825 F. Supp. 2d. at 810.

Despite this logic, the Fifth Circuit reversed the lower court's ruling in *Ransom* relying in part upon its prior decision in *Blackmon v. Brookshire Grocery Co*., 835 F.2d 1135 (5th Cir. 1988), which relied upon 29 C.F.R. § 778.114, in determining that the FWW method is appropriate in misclassification cases to calculate overtime damages using a half-rate. Other courts including the First and Tenth Circuits in *Valerio v. Putnam Assocs*., 173 F.3d 35 39-40 (1st Cir. 1999) and *Clemonts v. Serco, Inc*., 530 F.3d 1224 (10th Cir. 2008), have similarly relied on 29 C.F.R. § 778.114 to apply the FWW method in misclassification cases. *Valerio* and *Clemonts*, however, have been criticized for failing to provide any meaningful analysis on this disputed legal issue. *See Perkins v. Southern New Eng. Tel. Co*., 2011 U.S. Dist. LEXIS 109882 (D. Conn. Sept. 27, 2011) (stating same); *Russell*, 672 F.Supp.2d at 1013-15 (distinguishing *Clements v. Serco, Inc*. and *Valerio v. Putnam Associates* as these decisions exclusively relied on non-misclassification cases for their holdings); *In re Texas EZPawn Fair Labor Stds. Act Litig*., 633 F.Supp.2d 395, 406 (W.D. Tex. 2008) (finding *Blackmon* "fundamentally flawed"); *Ader v. SimonMed Imaging Inc.*, 465 F. Supp. 3d 953, 971–72 (D. Ariz. 2020) (criticizing the approach adopted in *Clements* and *Valerio*).

Given this conflicting case law, clarification from the Department that 29 C.F.R. § 778.114 is "forward-looking" and only describes how employers and employees may structure an agreement for future compensation and cannot be applied retroactively to misclassification claims would be helpful guidance.

2. Reliance On *Missel* Is Improper To Calculate Damages In Misclassification Cases.

The U.S. Court of Appeals for the Second, Fourth, Fifth, and Seventh Circuits have relied on *Missel* and applied 29 C.F.R. § 778.114 retroactively while ignoring that no overtime compensation is typically paid to misclassified employees. *See Thomas v. Bed Bath & Beyond Inc., 961 F.3d 598 (2d Cir. 2020); Desmond v. PNGI Charles Town Gaming, LLC*, 630 F.3d 351 (4th Cir. 2011); *Urnikis-Negro v. American Family Property Services*, 616 F.3d 665 (7th Cir. 2010); *See generally Black v. Settlepou, P.C., 732 F.3d 492, 498* (5th Cir. 2013). For example,

in *Urnikis-Negro*, the court determined that while 29 C.F.R. § 778.114(a) could not be used to calculate damages in a misclassification case, because "it is not a remedial measure that specifies how damages are to be calculated when a court finds that an employer has breached its statutory obligation [to pay overtime,]" the court instead relied on *Missel*, 316 U.S. 572.

This application of *Missel* is wrong. The court in *Snodgrass* explicitly rejected the application of *Missel* to misclassification cases for four reasons. First, as the court noted, "*Missel* is not directly on point[;] *Missel* is not a misclassification case, and it does not expressly authorize the use of the FWW half-time method in a misclassification case." 2015 U.S. Dist. LEXIS 33621 at *33 (*citing Wallace v. Countrywide Home Loans,* 2013 U.S. Dist. LEXIS 69215, 2013 WL 1944458, at *7). Second, the court reasoned that reaching an agreement that the salary is intended to cover all hours worked with no mention of overtime pay, "would mean that an employer and an employee could mutually agree to depart from the standard, default FLSA arrangement of a forty-hour work week with time-and-a-half overtime, simply with an understanding that a salary is intended to cover all hours worked and with no mention at all of overtime payment." *Id.* at 34 (*quoting Wallace* 2013 U.S. Dist. LEXIS 69215 at *7). Third, the application of *Missel* to misclassification claims in which an employee was paid a fixed salary and worked varied hours would improperly result in the FWW applying to all claims. *Id.* at *35-36. Fourth, and most importantly:

> [T]o allow defendant employers to utilize *Missel* in such a way goes against the remedial purpose of the FLSA. *McCoy v. N. Slope Borough*, 2013 U.S. Dist. LEXIS 121797, *19 (D. Alaska Aug. 26, 2013) ("the FWW method should not be applied in a misclassification case, particularly in light of the FLSA's remedial purpose.") '[A]ssessing damages using the fluctuating workweek method provides a perverse incentive to employers to misclassify workers as exempt, and a windfall in damages to an employer who has been found liable for misclassifying employees under the FLSA.' *Perkins*, 2011 U.S. Dist. LEXIS 109882, 2011 WL 4460248 at *4 n. 5; see also, *Ransom*, 825 F.Supp.2d at 810 n. 11 ("The significance of the employee's lack of knowledge of nonexempt status cannot be overstated. The fundamental assumption underpinning the FWW is that it is fair to use it to calculate overtime pay because the employee consented to the payment scheme. But in the context of an FLSA misclassification suit when consent is inferred from the employee's conduct, that conduct will always, by definition, have been based on the false assumption that he was not entitled to overtime compensation.").

Id. at *36-37. The court further explained:

> Utilizing *Missel* as authority to retroactively apply the FWW method creates a lower threshold requirement for the retroactive application of the FWW method. This produces a perverse incentive to employers. For instance, an employer attempting to pay employees using the FWW method cannot avail itself of the 50% overtime calculation unless it meets all the requirements of § 778.114; but if that same employer misclassifies its employees as exempt and pays them a salary with no overtime, that employer can avail itself of the 50% overtime calculation even

> though it does not meet the requirements of § 778.114 (and that's assuming the misclassified employee finds out he is misclassified and files a law suit). In short, utilizing *Missel* as authority for retroactive application of the FWW method creates a loophole where employers can circumvent the requirements of § 778.114. This incentivizes employers to break the law and misclassify employees as exempt.

Id. at *37-38(citations omitted).

Other courts have reached the same conclusion. *See e.g. Costello v. Home Depot USA, Inc*., 944 F.Supp.2d 199, 208 (D. Conn. 2013) ("[Defendant's] reading of *Missel* and the FLSA plainly run counter to the policy implications of that case and the statute itself. Indeed, 'assessing damages using the fluctuating workweek method provides a perverse incentive to employers to misclassify workers as exempt . . . .'"); *Zulewski v. Hershey Co*., 2013 U.S. Dist. LEXIS 23448, *15-16 (N.D. Cal. Feb. 20, 2013) ("[T]he retroactive application of the FWW method in the misclassification context does not square with *Missel*, because *Missel* requires an agreement between the parties that the fixed weekly salary was compensation for all straight time. . . such an agreement is not present in misclassification cases"); *Ader v. SimonMed Imaging Inc*., 465 F. Supp. 3d 953, 971–72 (D. Ariz. 2020) (holding there can be "no true 'understanding…'" as required by 9 C.F.R. § 778.114 "..when an employee is misclassified"); *Boyce v. Indep. Brewers United Corp*., 223 F. Supp. 3d 942, 949 (N.D. Cal. 2016) (finding the application of the FWW to misclassification cases would be contrary to the remedial purpose of the FLSA). In *Costello, Ader*, and *Boyce* the court reached the same conclusion articulated in *Snodgrass* that applying *Missel* retroactively would produce an illegal result: "an employer and an employee could mutually agree to depart from the standard, default FLSA arrangement of a forty-hour work week with time-and-a-half overtime, simply with an understanding that a salary is intended to cover all hours worked and with no mention at all of overtime payment." 944 F.Supp.2d at 207.

NELA proposes that the Department follow *Snodgrass*, *Costello*, *Zulewski*, *Ader*, and *Boyce* in rejecting the application of *Missel* to misclassification claims and issuing clarification as part of the Final Rules that the FWW cannot be used to calculate damages in a misclassification claim.

E. The Department Should Restore Its Pre-2004 Protections Against Improper Deductions.

NELA urges the Department to restore the pre-2004 safe harbor provisions to the regulations.[6] No employer should be allowed access to the "window of correction" unless the employer meets a burden of establishing that any deductions made were "inadvertent," that all deductions made were reimbursed as soon as they came to the employer's attention, and that the

[6] The Secretary's prior position that an exemption was lost if there was a "significant likelihood" of improper deductions. *Coates v. Dassault Falcon Jet Corp.*, 961 F.3d 1039, 1043, n. 3 (8th Cir. 2020); Defining & Delimiting the Exemptions, 69 Fed. Reg. at 22180.

employer has revised all of its rules, codes, policies, practices, and procedures which leave no doubt that as a practical matter the affected employee will not be subject to such deductions in the future. *See, e.g., Klem v. Cnty. of Santa Clara, California*, 208 F.3d 1085, 1092 (9th Cir. 2000) ("According to the Secretary, [the safe harbor] applies only to employers who objectively intended to pay their employees on a salaried basis in the first place." Otherwise, "[i]n the event that [] employees sued for overtime pay, []an employer simply could use the window of correction to comply retroactively with the salaried-basis requirements. According to the Secretary, such a result would render the 'salary basis' rule 'essentially meaningless' and run counter to the rule that FLSA exemptions are to be construed narrowly.").

The 2004 regulation adopted an extremely broad "safe harbor" provision, which too frequently allows an employer to make an improper deduction without losing the exemption if it is retroactively corrected upon complaint. *See*, *e.g.*, *Ellis v. J.R.'s Country Stores, Inc.*, 779 F.3d 1184, 1189 (10th Cir. 2015) (citing Section 541. 603(c)) ("the Secretary has carved out a savings provision for '[i]mproper deductions that are **either** isolated **or** inadvertent,' which allows the exemption to stand "if the employer reimburses the employees for such improper deductions.") (emphasis added); *see also Rebischke v. Tile Shop, LLC*, 229 F. Supp. 3d 840, 855 (D. Minn. 2017) (Notably, at no time did the Department suggest that intentional, improper deductions would automatically foreclose the window of correction.). These changes set out in the 2004 regulations departed from the Department's historical position and went way too far in loosening the standards applicable to protecting the salary basis.

Moreover, through the 2004 regulation, the Department seemed to limit the loss of the exempt status to work units that are making improper deductions. *See* Section 541. 603(d);[7] *Coates*, 961 F.3d at 1048. In many instances, however, improper deductions are companywide. Thus, the revised interpretations should make it clear that if there is a companywide policy or practice of making such improper deductions, then the exempt status is lost for all employees, regardless of location, classification. While this may be subsumed by the example in Section 541.603(b),[8] the example seems to have a limiting effect that could be ameliorated by adding language allowing liability on a companywide basis where the practice or policy could reasonably be construed to be companywide.

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[7] "If an employer fails to reimburse employees for any improper deductions or continues to make improper deductions after receiving employee complaints, the exemption is lost during the time period in which the improper deductions were made for employees in the same job classification working for the same managers responsible for the actual improper deductions." Section 541.603(d).

[8] "Thus, for example, if a manager at a company facility routinely docks the pay of engineers at that facility for partial-day personal absences, then all engineers at that facility whose pay could have been improperly docked by the manager would lose the exemption; engineers at other facilities or working for other managers, however, would remain exempt." Section 541.603(b).

NELA urges that the changes to the improper deduction regulations adopted in 2004 be rescinded and replaced by the Department's regulations pertaining to improper deductions that better served the purposes of the FLSA until August 23, 2004.

III. CONCLUSION.

In sum, NELA supports the proposed rule with the suggested changes to particular provisions described above. Thank you for your consideration. If you have questions or wish to discuss these matters, please contact Ashley Westby at awestby@nelahq.org or (202) 420-1123.

Sincerely yours,

Ashley Westby

Program Director

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