September 25, 2017

Submitted Electronically

Melissa Smith
Director of the Division of Regulations, Legislation, and Interpretation
Wage and Hour Division
U.S. Department of Labor
Room S-3502
200 Constitution Avenue, N.W.
Washington, D.C. 20210

Re: **Response to Department of Labor Request for Information Regarding The 2016 Revisions to the Overtime Exemptions Under the FLSA (RIN 1235-AA20)**

Dear Ms. Smith,

The Small Business Legislative Council (SBLC) appreciates this opportunity to provide comments on the 2016 Final Rule on the FLSA's overtime rules and to share its insights on the questions that the Department of Labor (the "Department") has raised.

The SBLC is an independent and permanent coalition of major national trade and professional associations whose goal is to maximize the advocacy and presence of small business on Federal legislative and regulatory policy issues, and to disseminate information on the impact of public policy on small businesses. The SBLC is the only small business association whose membership is comprised exclusively of trade and professional associations and, through its members and their members, it represents all sectors of the economy and a significant swath of the country's small businesses.

The SBLC fully supports the goal of ensuring that all Americans receive a fair living wage in exchange for their work. However, as we previously expressed at the time the 2016 revisions were proposed, we are concerned that changes to the overtime rules could have a serious negative impact on small businesses and could decrease small business growth and job creation.

Addressing the Department's Areas of Inquiry:

1. *In 2004 the Department set the standard salary level at $455 per week, which excluded from the exemption roughly the bottom 20 percent of salaried employees in the South and in the retail industry. Would updating the 2004 salary level for inflation be an appropriate basis for setting the standard salary level and, if so, what measure of inflation should be used? Alternatively, would applying the 2004 methodology to current salary data (South and retail industry) be an appropriate basis for setting the salary level? Would setting the salary level using either of these methods require changes to the standard duties test and, if so, what change(s) should be made?*

The SBLC understands that the current salary threshold is outdated and in need of updating. While it would not be easy, most small businesses could absorb a moderate increase to the salary basis for the white collar and highly compensated exemptions without having to significantly cut back on their productivity or workforce. However, too great a change would directly undermine small business growth and success and would require many small businesses to restructure and scale-back their labor force.

The white collar exemptions are some of the most, if not the most, commonly utilized exemptions to the FLSA.[1] Any changes to the qualifications for the white collar exemptions will have a notable impact on a broad range of businesses and industries. This impact would be especially felt by small businesses. Particularly in their early years, most small businesses operate on a very thin margin and have to fight for their survival.[2] However, many employees view working for a small or start-up business as an investment in their future and are willing to work at a lower salary than they might get at a large business because they believe in the buisness' potential for growth and because of the unique culture and benefits that many small businesses offer. In 2012, the Small Business Administration reported that small businesses accounted for 64% of new private-sector jobs.[3] It is clear that the success of small businesses fuels the American economy. With businesses just getting back on their feet in the wake of the recession, the Department must take great care to ensure that these new rules do not undermine small business growth and success.

The SBLC does not have a position as to the methodology that should be used to set a new salary threshold that is fair and appropriate for both businesses and employees. **However, to the extent that the Department decides to use salary data to set a single salary threshold for all regions and businesses, the Department should continue the practice of using the data from the lowest economic region (currently the South). Relying on national data to**

[1] We suspect that this is why the 2016 Final Rule focuses primarily on these exemptions.

[2] In 2012, the Small Business Administration reported that only about half of new businesses survive their first five years and only about a third of new businesses survive 10 years or more. *Frequently Asked Questions*, Small Business Administration, Office of Advocacy (September 2012), available at http://www.sba.gov/sites/default/files/FAQ_Sept_2012.pdf

[3] *Frequently Asked Questions*, Small Business Administration, Office of Advocacy (September 2012), available at http://www.sba.gov/sites/default/files/FAQ_Sept_2012.pdf

establish a new nationwide salary basis would fail to account for regional economic differences and have a particularly hard impact on small businesses in the lower economic regions.

Regardless of what methodology is used, what is very clear is that the more than 100% increase to the salary threshold for the white collar exemption set forth in the 2016 Final Rule is vastly too high and would be crippling for small businesses and inconsistent with the historical purpose of the salary basis. It is the SBLC's belief that no increase to the salary thresholds for the white collar and highly compensated exemptions (whether nationally or by region as discussed below) should exceed fifty percent (*i.e.* the white collar salary threshold should not be increased more than $682.50 per week). An increase of at or near 50% would only be appropriate and manageable for small businesses if, as discussed below, all non-discretionary bonuses and commissions can be counted towards meeting that threshold.

Additionally, if the salary thresholds are increased, such increases should be phased in over a period of no less than five years. As the Department is well aware, prior to the 2016 Final Rule, which has still not gone into effect, the salary bases for the white collar and highly compensated exemptions had not been increased since 2004. As such, a change to these bases is not something that employers have been budgeting or planning for in the ordinary course of business. Employers will need time to determine how to accommodate the additional costs that will result from such an increase and how to manage their workforces to ensure compliance. A phase in period of no less than five years would allow employers time to assess how many overtime hours employees who are currently classified as exempt would be working if they are re-classified as non-exempt and to make salary adjustments and related business decisions with care and planning.

Finally, in response to the Department's inquiry regarding the duties tests, the SBLC urges the Department not to make any changes to the duties tests as doing so would destabilize the entire business community and be particularly harmful for small businesses.

It has taken years, and volumes of case law and administrative decisions, for employers to understand, and become comfortable with, the application of the duties tests and how the tests apply to their employees. Any increase in the salary bases will be challenging enough for small businesses. If this were accompanied by a change to the duties tests it could be crippling. Any change to the duties tests will require each and every employer to expend the time and resources to understand the changes and to audit their own workforces to ensure that any exempt employees are still exempt under the modified test. This would have to be done without the wealth of resources and case law that has developed to assist employers in understanding and apply the existing duties test.

Changes to the duties test would pose a particular challenge for small businesses that often do not have the resources to engage attorneys or other professionals to provide them with advice on such issues. Thus, these small businesses would be faced with difficult choices of allocating funds away from employee salaries or other business needs to pay a professional to assist them or risking a costly misclassification. The vast compliance and professional costs to

businesses that would result from a change in the duties would undermine economic growth and be directly inconsistent with the Department's goal of increasing employee pay. If an increase in the salary bases is accompanied by a change in the duties test, employers will have no choice but to expend funds for compliance costs rather than increasing salaries.

2. *Should the regulations contain multiple standard salary levels? If so, how should these levels be set: by size of employer, census region, census division, state, metropolitan statistical area, or some other method? For example, should the regulations set multiple salary levels using a percentage based adjustment like that used by the federal government in the General Schedule Locality Areas to adjust for the varying cost-of-living across different parts of the United States? What would the impact of multiple standard salary levels be on particular regions or industries, and on employers with locations in more than one state?*

The DOL itself has recognized that the historical purpose of the salary bases for the exemptions is "screening out the obviously nonexempt employees."[4] The salary basis works in concert with the duties tests for each exemption. Setting a salary basis which, in many industries and regions, would capture only the highest paid small business employees is not consistent with the purpose of the salary basis and would result in excluding employees who, under the duties test, would clearly qualify for exempt status.

The SBLC does not have a position on whether the Department should establish a single nationwide basis or different regional bases. However, the SBLC recognizes that, as noted in the Department's question, the federal government itself relies on geographic variation to set the compensation level for its own employees and that the Department may look to setting different geographical bases as a means of tackling the concern raised above that certain regions may be harder hit by a uniform national increase to the salary basis.

If the Department decides to use different salary bases by region, the SBLC urges the Department to do so under the following parameters:

- As discussed earlier, the increase to the existing salary threshold in any region, including the highest paid region(s), should not exceed, at a maximum, fifty percent. In setting salary thresholds, the Department should be mindful of the fact that, even in the regions with the highest averages, those averages are commonly inflated by the economies of the large cities like New York, Washington, D.C. and San Francisco, while other parts of the region differ considerably with respect to wages and costs of living, which commonly go hand in hand. Any regional salary bases must be set so that they are appropriate and manageable for all employers in that region, not just the urban employers.

[4] Defining and Delineating the Exemption for Executive, Administrative, Professional, Outside Sales, and Computer Employees; Final Rule, 69 Fed. Reg. 22,122, 22,165 (April 23, 2004) ("The Department has long recognized that the salary paid to an employee is the 'best single test' of exempt status . . . which has 'simplified enforcement by providing a ready method of screening out the obviously nonexempt employees'").

- To mitigate costs and issues for such employers, the Department should also create simple and clear rules that allow employers to easily determine which of the regional bases applies to which employees – particularly for those employees who work in multiple regions or who telecommute from one region for an employer based in another region.

While again, the SBLC is not taking a position on whether the Department should establish a single national salary basis or multiple salary bases, the SBLC would certainly not object to a lower salary basis being set for the country's smallest businesses. As noted earlier, the benefits, and potential, that employees see from working for a small or start-up business don't always correspond to a high salary. Structuring the salary bases to recognize that, even for the most senior level employees, salaries at new and small businesses tend to start out low and increase markedly over time as the business grows and thrives, will help encourage small business growth and success.

3. *Should the Department set different standard salary levels for the executive, administrative and professional exemptions as it did prior to 2004 and, if so, should there be a lower salary for executive and administrative employees as was done from 1963 until the 2004 rulemaking? What would the impact be on employers and employees?*

The Department should maintain a single salary bases for the executive, administrative and professional exemptions. The reason for this is simple – to make the rules as fair and easy for employers to apply as possible.

Under the existing duties tests, which, as articulated above, the SBLC urges the Department to leave in place, employees commonly qualify for multiple exemptions. Take, for example, a managing attorney at law firm who could qualify for both the executive and professional exemptions, or a director of human resources who might qualify for both the executive and administrative exemptions. **If the Department establishes different salary bases for the different white collar exemptions while maintaining the current duties tests, the Department will also need to establish rules for how to handle employees that qualify for more than one exemption.**

Simply establishing a rule that the higher of the salary bases applies might seem like the easy answer to this concern but it is not that simple. Under the current system, when employers apply the duties tests the big question they are looking for is whether the employee qualifies for <u>any</u> of the exemptions. As discussed above, this type of analysis is nuanced and employers rely a great deal on case law and guidance from the Department and other sources. It is very common for employers to identify that an employee squarely fits within one of three above mentioned exemptions and is borderline for another of exemptions. In such a case, because the salary bases for the executive, administrative and professional exemptions are the same, the employer can classify the employee as exempt on the basis of the exemption that they clearly qualify for, without having to delve into any further analysis on the borderline exemption. However, if different salary bases are set for the executive, administrative and professional exemptions, such an employer will be required to make a determination about whether the employee, in fact, qualifies for the borderline exemption to determine the appropriate salary

basis. **This will place a greater administrative burden on the employer. Moreover, it will bring back an added level of risk and liability to the classification process – as employers would then need to worry about being sued, not simply for mishandling the exempt/non-exempt distinction, but also for potential errors in determining which exemptions and related salary bases apply.**

The decision in the 2004 regulations to create a single salary basis for the executive, administrative and professional exemptions, was a meaningful step towards creating greater simplification in the rules and making them easier for businesses to apply and should not be undone.

4. *In the 2016 Final Rule the Department discussed in detail the pre-2004 long and short test salary levels. To be an effective measure for determining exemption status, should the standard salary level be set within the historical range of the short test salary level, at the long test salary level, between the short and long test salary levels, or should it be based on some other methodology? Would a standard salary level based on each of these methodologies work effectively with the standard duties test or would changes to the duties test be needed?*

In the 2016 Final Rule, the Department set the salary basis for the white collar exemptions at the "40th percentile of weekly earnings of full-time salaried workers in the lowest wage Census Region (currently the South), because it was at the low end of the historical range of short test salary ratios."[5] As discussed herein, that salary basis was far too high.

As detailed above, the SBLC opposes any changes to the duties tests, including any return to a long/short test system. Accordingly, rather than getting caught up on the historical ranges of the long and short test, which are no longer in use, the Department should focus instead on the current salary bases and the type of increase that would be manageable for businesses and fair for employees.

5. *Does the standard salary level set in the 2016 Final Rule work effectively with the standard duties test or, instead, does it in effect eclipse the role of the duties test in determining exemption status? At what salary level does the duties test no longer fulfill its historical role in determining exempt status?*

The salary bases provided for in the 2016 Final Rule did not work effectively with the duties tests. Particularly in the context of small businesses and businesses in lower wage regions, the high salary requirements set by the 2016 Final Rule would have prevented a number of high level administrative employees, such as human resources and accounting managers or and executive employees, such as store or department managers, who unquestionably satisfy the duties tests from being classified as exempt.

The SBLC is not convinced that there is a magic number at which the salary level will not eclipse the duties test. However, there are steps – like allowing all non-discretionary

[5] U.S. Department of Labor, Final Rule: Overtime; Questions and Answers, available at https://www.dol.gov/whd/overtime/final2016/faq.htm.

compensation to be counted towards the salary bases – that the Department could take to help get the rules closer to that magic balancing point.

6. *To what extent did employers, in anticipation of the 2016 Final Rule's effective date on December 1, 2016, increase salaries of exempt employees in order to retain their exempt status, decrease newly non-exempt employees' hours or change their implicit hourly rates so that the total amount paid would remain the same, convert worker pay from salaries to hourly wages, or make changes to workplace policies either to limit employee flexibility to work after normal work hours or to track work performed during those times? Where these or other changes occurred, what has been the impact (both economic and non-economic) on the workplace for employers and employees? Did small businesses or other small entities encounter any unique challenges in preparing for the 2016 Final Rule's effective date? Did employers make any additional changes, such as reverting salaries of exempt employees to their prior (pre-rule) levels, after the preliminary injunction was issued?*

Because of the costs and challenges posted by the 2016 Final Rule's high salary thresholds, many of the small businesses that had identified employees who would no longer qualify as exempt, were waiting until the effective date of the Final Rule to roll out any changes and were still contemplating what changes to make when the preliminary injunction was issued.

The most significant problem these businesses were grappling with was with respect to employees whose salaries were significantly below the new threshold, i.e. those employees whose salaries the business couldn't afford to increase enough to keep them exempt. Because exempt employees typically are not required to track their hours, many employers with these types of employees had very little sense of how many hours these employees regularly worked over the course of a year. This created a twofold problem. On one hand, businesses were struggling to determine what hourly rate to pay these newly-non-exempt employees because there was very little sense of how much overtime the employee would be working. As such, businesses were setting hourly rates based on rough estimates of expected overtime hours. To account for potential inaccuracies in the estimates and avoid unbudgeted overtime costs, many businesses were preparing to cap the amount of overtime that these newly-non-exempt employees would be permitted to work. This in turn created the concern that, with such restrictions on their hours, these employees might not be able to complete all their job duties or perform at the same level they had when their hours had been unrestricted. **This quandary that employers were facing is the very reason why the SBLC is advocating that the salary level for the white collar exemptions not be increased nearly as much as it was in the 2016 Final Rules and that any increase be phased in to allow employers to either slowly increase employees' salaries or to begin to track their hours and find the appropriate pay rate for them as a non-exempt employee.**

7. *Would a test for exemption that relies solely on the duties performed by the employee without regard to the amount of salary paid by the employer be preferable to the current standard test? If so, what elements would be necessary in a duties-only test and would examination of the amount of non-exempt work performed be required?*

The salary threshold, when appropriately set, sets a floor for the exemptions and prevents gross abuses of the system and the employees in it, by ensuring that, regardless of an employee's position, they are getting some level of fair compensation. Moreover, it often serves as a helpful guide for employers in classifying the more borderline employees. If the salary requirement was eliminated entirely, the duties test would almost certainly need to be modified to maintain even the pre-2016 Final Rule status quo. For the reasons stated above, the SBLC opposes any changes to the duties test. Moreover, if the salary threshold were to be eliminated, the response would likely be to further narrow the duties tests, which already prevents most mid-level employees from being exempt. The harm created for businesses, big and small, by a narrowing of the duties test would far outweigh the benefit of an elimination of a reasonably set salary threshold. **Because of the almost guaranteed impact on either the duties test or on the labor system as a whole, either of which would be jarring in the current ever-tenuous economy, the salary threshold should be set responsibly but not be eliminated.**

8. *Does the salary level set in the 2016 Final Rule exclude from exemption particular occupations that have traditionally been covered by the exemption and, if so, what are those occupations? Do employees in those occupations perform more than 20 percent or 40 percent non-exempt work per week?*

The SBLC has not identified any specific occupations that would be more heavily hit than others by the new salary bases set forth in 2016 Final Rule. However, as discussed above, the 2016 Final Rule's salary level would have caused a number of high level employees whose duties were comprised of almost exclusively exempt-type work to no longer qualify as exempt.

9. *The 2016 Final Rule for the first time permitted non-discretionary bonuses and incentive payments (including commissions) to satisfy up to 10 percent of the standard salary level. Is this an appropriate limit or should the regulations feature a different percentage cap? Is the amount of the standard salary level relevant in determining whether and to what extent such bonus payments should be credited?*

The SBLC would urge the Department to allow all forms of non-discretionary compensation, including non-discretionary bonuses and incentive payments, to be included in determining whether an employee is receiving the requisite salary to qualify for an exemption without any limit.

While the SBLC believes there should be no cap, if the Department is going to place a limit on the extent to which non-discretionary bonuses and incentive payments can be applied to satisfy the salary requirement, that threshold should be set to correspond with the extent to which the salary bases are being increased. In other words, the higher the salary bases are increased, the more important it will be for non-discretionary bonuses and incentive payments to count towards that requirement.

Perhaps the only part of the 2016 Final Rule that the SBLC would encourage the Department to carry forward were the rules established to allow employers to make catch-up payments to employees to bring them up to the required salary bases in the event that their non-discretionary bonuses or incentive compensation payments are less than anticipated. These rules adequately accounted for the fact that a business may not always be able to calculate in advance what an employee's non-discretionary bonus or incentive compensation will be and that the exemption should not be immediately lost if these amounts fall below what was expected.

10. *Should there be multiple total annual compensation levels for the highly compensated employee exemption? If so, how should they be set: by size of employer, census region, census division, state, metropolitan statistical area, or some other method? For example, should the regulations set multiple total annual compensation levels using a percentage based adjustment like that used by the federal government in the General Schedule Locality Areas to adjust for the varying cost-of-living across different parts of the United States? What would the impact of multiple total annual compensation levels be on particular regions or industries?*

The SBLC maintains the same position with respect to setting multiple required salary levels for the highly compensated exemption as has been set forth in response to Inquiry 2, above, with respect to setting multiple required salary levels for the white collar exemptions.

11. *Should the standard salary level and the highly compensated employee total annual compensation level be automatically updated on a periodic basis to ensure that they remain effective, in combination with their respective duties tests, at identifying exempt employees? If so, what mechanism should be used for the automatic update, should automatic updates be delayed during periods of negative economic growth, and what should the time period be between updates to reflect long term economic conditions?*

The SBLC understands the Department's desire to create a mechanism by which to ensure that the salary threshold will stay up to date without the Department having to go through the burdensome and time consuming rulemaking process.

However, if the Department decides to implement an automatic increase, like that which was included in the 2016 Final Rule, the SBLC urges the Department to do so under the following parameters:

- **The increase should be made no more frequently than every five years**. If automatic increases are made too frequently it will leave businesses in a perpetual state of uncertainty. Automatic increases every five years would achieve the goal of providing for increases to the salary bases without the need for new rulemaking, while allowing employers time to acclimate and implement each increase.

- **Employers must receive notice of the increase at least one calendar year in advance of its effectiveness**. Employers, and small businesses in particular, need time to plan and budget for any increase to the salary threshold – regardless of whether it is enacted

through new regulation or automatic increases. The 150 days advance notice of automatic increases provided for in the 2016 Final Rule is not enough time to allow employers to prepare for a new salary bases. Such a short notice window would be particularly challenging for businesses whose fiscal years don't coincide with the calendar year and who could find themselves starting out a fiscal year without knowing what the salary bases will be for the latter part of that fiscal year. Giving employers at least one year's advance notice of any automatic increase will prevent this issue and allow all employers sufficient time to plan for the change.

Conclusion

On behalf of our members, we respectfully submit these comments and look forward to working with the Department to ensure that any changes to the overtime regulations do not undermine the small business growth that fuels the American economy.

Sincerely,

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American Hort
American Moving & Storage Association
American Pet Products Association
American Road & Transportation Builders Association
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America's Small Business Development Centers
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