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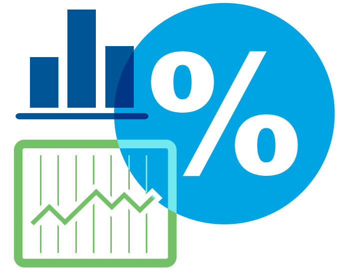

Financial Services Employment Law Alert

How Financial Services Employers Can Navigate the New White-Collar Overtime Rules

By Robert S. Whitman

The Department of Labor's proposed revisions to the Fair Labor Standards Act's overtime exemptions will impact the American workplace as much as any legal development in the past decade. Employers will need to reexamine, and in many cases change, exempt job classifications. But to view this moment merely as the time to endure a major legal audit might be to overlook a broader opportunity. Drawing upon our experience counseling and partnering with financial services clients, we discuss in this Alert how these employers might pair their legal analysis with broader business strategies in an evolving market.

As we have detailed in previous Alerts, the DOL is proposing to tighten the availability of the FLSA's most litigated overtime exemptions. Under the proposed rules, the salary requirement for exempt status (the "salary test") would more than double, from $23,660 ($455/week) to $50,440 ($970 per week). Moreover, the requirement would be indexed in perpetuity to the 40th percentile of weekly earnings for full-time salaried workers nationally, thereby automatically increasing over time. For employees to meet the "highly-compensated" exemption, the minimum salary would be $122,148, indexed to the annualized value of the 90th percentile of weekly earnings of full-time salaried workers.

In addition to raising the salary requirement, the DOL may overhaul the exemptions' duties requirements (the "duties test"). Though it did not publish a proposed rule to this effect, the DOL has invited public comment on a series of questions on this issue. Those questions, which can be found by clicking *here*, may foreshadow a major shift to a quantifiable duties analysis (e.g., requiring that managers spend a minimum percentage of time on management) when the DOL releases its final rules.

As of July 6, the public has a 60-day period to comment on the DOL's proposal. (That time could be extended by 30 days, but probably not longer.) Following this comment period, the DOL will take some time to review the comments before issuing its final rule, most likely several months later. Seyfarth will be collecting employer comments through a series of client roundtable discussions and other communications aimed at obtaining the views of the employer community.

In addition to participating in the comment process, employers should take steps to protect themselves against legal risks created by the new rules. In this Alert, we discuss not just the necessary first step of assessing exempt-classified employees to determine their status under the new rules, but also a framework for acting on the results to leverage broader business objectives in an environment where financial services firms are already subjected to unprecedented levels of competitive pressure, public scrutiny and regulatory oversight.

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Step 1: Reevaluate Exempt Positions in the Existing Operating Model.

1. Assess salary levels against the salary test and consider changes.

Assessing salary levels should be relatively straightforward. Most HRIS applications permit employers to run reports showing base salary levels across selected exempt position codes. A base salary report will allow financial services employers to determine which employees and job positions fall below the new salary requirements. For those that do, employers will have to decide whether to increase salaries to bridge the pay gap or, alternatively, to reclassify the position.

(a) bridge the pay gap

For employers that choose to bridge the gap, the result does not necessarily mean an increase in compensation costs. Because of the prevalence of bonus programs and other deferred compensation arrangements in financial services for exempt employees, employers may have the opportunity to shift dollars away from these programs in favor of higher base salaries to meet the new DOL levels. (Payment on a "salary basis," as the DOL regulations have long required, means that exempt employees must receive the same payment for any week in which work is performed, regardless of the quantity or quality. So it may not suffice for the employees to receive the new minimum amount in salary *plus* bonus; it must all come in the form of salary. That said, the DOL has created an opportunity for employers in its request for comments. More on that below.)

While deferred compensation plans present financial services employers with the opportunity to soften the blow of the heightened salary level, the entrenched nature of these programs, and the prevailing "pay for performance" ethic in financial services generally, may mean that a transition to higher salaries presents serious management and HR challenges. Employers will be wise to think through all the business ramifications of such adjustments, and not focus solely on the relatively narrow issue of legal compliance.

(b) reclassify

Financial services employers that decide to reclassify must consider how they will pay their newly nonexempt employees. The most common route will be to convert salaries into an hourly rate equivalent, with consideration given to a downward adjustment in the salary to account for possible overtime pay. A fluctuating workweek plan may make sense as well.

While the type of pay plan to pursue will vary based on factors specific to the employer and the employees it is reclassifying, the need for thoughtful communication and a change-management plan will not. Many exempt employees may view their conversion to hourly nonexempt status as a drop in prestige or a diminution of the perceived value of their work to the employer. To reduce the likelihood of rumors or fears filling any gaps in understanding, financial services employers should work with counsel to carefully plan how they communicate the changes to those affected. Such a plan should include written materials (e.g., correspondence to those affected, written directives to their supervisors about how to explain the changes, FAQs for either group), as well as a precise timeline for the staging of the changes and communications. Not only does such a plan reduce the likelihood of lawsuits by employees claiming that they should have been classified as non-exempt earlier, but it also helps allay concerns by converted employees that they are no longer as important or valued by the company.

Finally, many employers with operations in California may assume that their classifications in that state need not be revisited, given that California's overtime exemptions are already stricter than the FLSA. That assumption is incorrect. Until now, for example, a California manager earning a salary equivalent to $37,440 (*i.e.*, at least two times the state minimum wage for full-time employment) satisfied the salary level requirements of both the state and federal overtime exemptions and could, depending on her duties, be classified as exempt. Once the FLSA's salary test is finalized, however, that manager would need to be paid more or reclassified, despite the fact that she is paid a sufficient amount under California law.

2. Analyze current duties under the FLSA duties test and consider changes.

Assuming that the salary level changes do not foreclose continued exempt status, financial services employers should consider partnering with their legal and human resources departments to audit selected jobs in anticipation of possible changes to the duties test under various exemptions. Acting now will put employers in a better position to respond when the final regulations are announced.

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In so doing, be sure to carefully examine duties both in design and in practice. Job descriptions, training materials, performance evaluation material, and the like are not dispositive of exempt status, but do reflect what the employer expects employees to do, how it trains them to do those things, and how it monitors performance against expectations. Just as important is the practical consideration of what duties employees are actually performing. Are they performing the duties reflected in the supporting documentation? How much time are they spending on those duties? What additional duties are they performing, how much time are they spending on them, and do those duties impact the analysis under the duties test?

The process of evaluating duties will not be a one-size-fits-all endeavor. For some, we might recommend a careful approach limited to interviews with a sampling of the employees' supervisors, and even their supervisors' supervisors. For others, the better course might be a campaign to speak to as many employees as possible. Or the solution may be something of a hybrid. Factors that will impact the decision include, for example, the number of employees in the position, the depth of the employer's current understanding of the position, and, of course, the employer's resources and risk tolerance.

For positions the employer determines can pass muster under the new salary and duties tests, care should be taken to document the review, the results, and the rationale. Should there be litigation regarding the decision—and we expect there will be, just as when the regulations were last modified in 2004—the employer will have evidence of its efforts to comply with the law, beyond the mere, "I remember we did something like…" Even if a judge or jury someday determines that the conclusion was wrong, the assessment and analysis could establish the basis for a "good faith" defense, which, in a large collective action, could mean a savings of millions of dollars in liquidated damages or an additional year of liability.

Of course, many positions that are currently classified as exempt might not survive a reconfigured duties test under the new exemption. Indeed, in a section of the DOL proposal that financial services employers might find especially ominous, it seeks comments on whether there are specific occupations for which it should provide additional examples in the regulatory language. For such employers, this may immediately bring to mind the example in the current regulations (at 29 C.F.R. § 541.203(b)):

> Employees in the financial services industry generally meet the duties requirements for the administrative exemption if their duties include work such as collecting and analyzing information regarding the customer's income, assets, investments or debts; determining which financial products best meet the customer's needs and financial circumstances; advising the customer regarding the advantages and disadvantages of different financial products; and marketing, servicing or promoting the employer's financial products. However, an employee whose primary duty is selling financial products does not qualify for the administrative exemption.

It remains to be seen, of course, whether the DOL will retain, modify or eliminate this language in the new regulations. If either of the latter two scenarios occurs, then financial services employers will have to rethink their exempt customer service positions effectively from scratch, without the security of this regulatory safe harbor.

The fate of Mortgage Loan Officers is another open question. In 2010, the DOL issued an Administrator's Interpretation conclud¬ing that they do not qualify for the administrative exemption. The Supreme Court earlier this year upheld the agency's action, but solely as a matter of administrative law, and did not address the merits of its position. It is possible that the DOL will seek to incorporate its interpretation into the final regulations as a way to better secure the non-exempt status of these employees under future administrations.

Step 2: In Deciding to Reclassify, Consider Changes to Compensation and Training.

Beyond answering and acting on the most obvious question—do we need to reclassify?—financial services employers should take the opportunity to pause and consider current and future business objectives. Any changes to exempt-classified positions will impact business operations, and the solution of simply converting exempt employees to hourly nonexempt status may be tempting as the easiest solution. But the range of possible solutions is limited only by the bounds of creative

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thinking (and, of course, the law), and spans from changing duties to bolster the exemption, to converting employees to salaried nonexempt rather than hourly exempt, to changing the management structure and labor model altogether (e.g., eliminating a manager, combining manager roles, etc.).

By approaching this task creatively, employers may be able to build a more holistic plan that both accounts for the new FLSA requirements and fosters the overall long-term business strategy. Below are some examples of the kinds of planned operational changes that might be leveraged alongside efforts to meet the new FLSA requirements:

- *Revisions to training programs* – Some firms consider trainees for exempt positions as themselves exempt. Given the higher salary minimums and possible changes to the duties requirements, this approach may be subject to challenge going forward. Employers should reevaluate the design of their training programs to ensure that any exempt classification of trainees can pass muster.

- *Revisions to commission plans* – As noted above, the current regulations state that "an employee whose primary duty is selling financial products does not qualify for the administrative exemption." This does not rule out applicability of the so-called "7(i)" exemption (codified at 29 U.S.C. § 207(i)), which generally applies for employees of retail sales or service establishments who earn at least half of their pay in the form of commissions.

- *Revisions to bonus plans* – In its request for comments, the DOL asks whether (and how) nondiscretionary bonuses might be used to satisfy the standard salary level under the revamped regulations. While the bonus plans at most financial services employers incorporate substantial discretion (precisely to prevent them from being considered "wages" or otherwise guaranteed), this may be an opportune moment to reconsider that approach for certain groups of employees in the event that a nondiscretionary bonus could help put them above the new salary thresholds.

Conclusion

The impact of the new FLSA regulations on the financial services industry will be significant. Employers should act now. As many continue to evolve their business models to meet an ever-evolving competitive landscape, these changes present an opportunity to incorporate legal solutions into business strategies. In building legal mitigation into the core strategy, financial services employers can reduce business disruption of these regulatory changes.

Please contact your Seyfarth attorney or any member of our Exemption Task Force (listed below) to discuss these legal changes and what your company can do now to prepare to comply with the new regulations.

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