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Healthcare Alert

How Healthcare Employers Can Navigate the New White-Collar Overtime Rules: Further Transition Presents Opportunities

By Kristin McGurn

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. Healthcare employers - whether in the non-profit or for-profit sector - will be impacted profoundly at a time when many already have experienced seismic change to their business operations and have been forced to scrutinize whether additional dollars can be squeezed from the cost of providing care. Exempt job classifications will need to be reassessed and, in many cases, changed. This need not, however, merely lead to another major compliance audit to endure. It may instead present potential opportunities to reevaluate and improve healthcare business models. Drawing on our deep experience counseling and partnering with healthcare industry clients, we advise in this Alert how legal analysis might be paired with healthcare employers' broader business strategies to respond to the rapidly evolving, dynamic healthcare market and, specifically, to the challenges posed by the DOL's anticipated regulations.

As we detailed in *last week's Alert*, the DOL announced its plan to narrow the FLSA's most litigated overtime exemptions. The executive and administrative exemptions are among those that will be narrowed. At present, employees earning $23,660 per year ($455 per week) may not be eligible for overtime if their primary job duties involve (1) managing other employees (executive exemption); or (2) performing nonmanual work that is directly related to management or general business operations of the employer or the employer's patients, including the exercise of independent judgment and discretion with respect to matters of significance (administrative exemption). The DOL's proposed revisions would increase the annual salary requirement more than two times the current threshold to a staggering $50,440 ($970 per week) ("salary test"). Further, the new, increased salary test would be indexed to the 40th percentile of weekly earnings for full-time salaried workers nationally, meaning that it would increase in each future year as long as national income levels continue to rise.

To date, the DOL has not proposed changes to the exemptions' "duties tests." It has suggested, however, that the tests may be rendered more similar to those currently used to define who must receive overtime pay under California law. The FLSA's duties tests now focus on an employee's key value or most important duty performed for her employer. Instead of this "primary duty test," California law applies a bright line test that requires employers to pay overtime to employees who devote more than 50% of their time to nonexempt work. The DOL did not publish a proposed rule to this effect, but it has invited public comment on a series of related questions, which can be found by clicking *here*. These questions may foreshadow an extraordinary shift to a quantifiable duties test when the DOL releases its final rules.

We encourage healthcare industry members to provide comments on these questions, to encourage the DOL to fully consider, among other things, the critical role managers and back office administrators play in running a healthcare organization, whether a hospital, physician practice, nursing or long term care facility, academic medical center or other care provider, highlighting the impact of these positions on ensuring high quality patient care. To this end, Seyfarth will be collecting employer comments through a series of client roundtable discussions and other communications aimed at obtaining views from our healthcare employer community.

Even without a change to the duties tests, the impact that the salary level increase will have on the healthcare industry will be profound. The DOL projects that millions of employees in health services will be potentially impacted. Exempt employees' salaries in administration, healthcare information technology, facility managers (laundry, housekeeping, environmental and dietary), marketing, laboratory and research positions, even at large healthcare systems and not-for-profit academic medical centers, for example, can fall under $50,000. The same often is true for certain healthcare professionals, perhaps especially behavioral and mental healthcare providers, despite their advanced degrees. Addressing job codes likely to be affected, the DOL references certain healthcare diagnosing and treating practitioners, technicians and technologists, medical and health services managers, assistants and support occupations, compliance personnel, and medical records and information technology occupations. Even the highest level office administrator at physician practice groups and long term and nursing care facilities, particularly in certain geographic locations, often are set below $50,000. Evaluating the impact of the proposed salary change on these positions is now critical.

The public has a 60-day comment period to respond to the DOL's proposal. That time could be extended by 30 days, but likely not longer. Thereafter, the DOL will review the comments before issuing its final rules. We expect the final rules to be published several months later. Healthcare industry employers, therefore, have time now to develop protection against the legal risks created by the new rules. We encourage you to begin the process soon.

In this Alert, we detail not just the necessary first step—assessing exempt-classified employees to determine their status under the new rules—but also a framework for acting on the results in ways that attempt to leverage broader business objectives in an environment where a changing competitive landscape, consolidation, and specialization have caused so many in the healthcare industry to rethink the patient experience, reduce operating expenses, locate partners for collaboration across the continuum of care, and restructure operations.

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

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

To assess whether exempt-classified positions might need to be reclassified, healthcare employers must assess both salary levels under the salary test and job duties under the duties test. Because it involves a far simpler analysis, the former is the ideal first step. If current salary levels do not meet the new minimum, and if raising them to do so is not an option, then employers need not waste time assessing duties under the potential new duties test.

- *Consider adjusting pay scales*

Assessing salary levels should be relatively straightforward. Most HRIS systems permit employers to run reports showing base salary levels across selected exempt job codes. A base salary report will allow employers to determine which employees and jobs fall below the new salary requirement. For those that do, employers must decide whether to increase salaries to bridge the gap or, alternatively, reclassify the position. As healthcare provider organizations consolidate, for-profit healthcare providers expand and develop, and technology and delivery mechanisms change within the industry, opportunities arise for consolidating, eliminating or rewarding personnel differently. Additionally, if healthcare employers are not inclined to change employees' exempt status, a new compensation review process must be implemented soon to ensure that the salaries are adjusted on a going-forward basis, consistently with the index, so they do not fall behind in subsequent years as the salary test minimum rises as anticipated. Cash-strapped providers should begin to develop a compliant multi-year strategy.

- *Consider reclassifying*

Healthcare employers that decide to reclassify must consider how they will pay their newly-nonexempt employees and how they will communicate the changes in their compensation structure. Healthcare organizations should navigate this path in conjunction with their legal department or Seyfarth lawyer. The most common route will be to convert salaries into an hourly rate equivalent, with consideration given to a downward adjustment to account for possible overtime pay.

For healthcare employers concerned that reclassification to nonexempt status will negatively affect the morale of formerly exempt employees, a fluctuating workweek plan might be considered in jurisdictions where that is permissible. One of the core requirements of fluctuating workweek is a "clear mutual understanding" between the employee and employer about the pay plan, which often presents additional benefits as a natural hurdle to class certification.

In healthcare, part-time and per diem workers have long comprised a significant percentage of the talent pool. Many healthcare employees who receive less than the new threshold requirement never work more than 40 hours per workweek. For those employees, employers merely must takes steps to ensure that they do not work overtime hours *and* are being paid at least minimum wage for each hour worked.

The type of pay plan to pursue will vary based on factors specific to the nature of healthcare employer at issue, and the employees it decides to reclassify, but the need for a thoughtful communication and change management plan applies across the board. To reduce the likelihood of misplaced rumors or fears filling any gaps in understanding, all healthcare employers should work with counsel to carefully plan how they communicate changes to affected employees. Such a plan should include written materials (e.g., correspondence to affected employees, written directives to supervisors about how to explain the changes, FAQs), and a precise timeline. Such a plan should minimize employees' concerns that their importance to the organization is being diminished, and reduce the likelihood of lawsuits by employees claiming that they should have been classified as non-exempt earlier.

Finally, many healthcare employers with operations in California may assume that their California classifications need not be revisited because California's overtime exemptions already are stricter than those of the FLSA. That assumption is incorrect. Until now, for example, a California employee earning a salary equivalent to $37,440 (i.e., at least 2 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. If the DOL's proposed salary level becomes final, that employee would need to be paid more or reclassified, even though she is sufficiently paid under California law. Healthcare employers with operations in California should consider evaluating how classification decisions have been made in that state, as a first step toward making necessary changes elsewhere.

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

Assuming that the salary level changes do not foreclose continued exempt status, healthcare employers should consider relying on their legal and human resources departments to identify and assess which exempt employees are most likely to be impacted by potential changes to the duties test. Healthcare employers who do this now will be in a better position to respond with agility when final regulations issue. Employers should take care to examine duties in design and in practice. As to the former, employers should review job descriptions, training materials, performance evaluation materials, and the like. While not dispositive of exempt status, these documents reflect what the particular healthcare employer expects its employees to do, how it trains them, and how it monitors performance against expectations.

The practical consideration is just as important: What duties are the employees actually performing? Are expected duties being performed and if so for how much time? How much time is spent on additional duties and do those duties impact the duties test analysis?

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 supervisors. For others, speaking to employees on the units or in back office support might be the better course. 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 test and a potential time-based duties test, care should be taken to document the review, the results, and the rationale. Should there be litigation regarding the classification decision, a prepared employer will have evidence of its efforts to comply, and the employer's exemption assessment could establish the basis for a "good faith" defense even if a judge were to determine that the decision ultimately was incorrect. For a healthcare employer facing a large class action, such a defense could save millions of scarce dollars. Healthcare employers should expect such litigation, just as we experienced when the regulations were last modified about a decade ago.

Many healthcare employees currently classified as exempt might not survive a time-based duties test, depending on how the DOL reacts to comments received in response to its questions. Healthcare employers should now determine how to address the gaps, if any, between what the employees are currently doing and what they need to be doing to maintain an exemption, and consider whether the delta can be bridged by adding duties to the position at issue.

Step 2: In Deciding to Reclassify, Take Time to Identify Possible Future Operating Structures.

The most obvious question is: do we need to reclassify? But during this time of changing ventures, relationships and organizational structures in the healthcare market, take this opportunity to consider business objectives. Any changes to exempt-classified positons will impact operations. The tempting and easy solution of converting exempt employees to hourly nonexempt status may seem simplest. But the range of possible solutions expands with changing healthcare management structures and labor models.

Approaching this task creatively, we suggest that there may be ways to build a holistic plan that both accounts for the new FLSA requirements, contributes to cost reduction, and maximizes patient experience as part of overall long-term business strategy. Healthcare employers' long-term strategic plans should be viewed through the lens of these new DOL regulations. Some examples of operational changes that might be leveraged alongside efforts to meet the new requirements follow:

- If mergers or acquisitions are underway in the drive toward accountable care and integrated delivery systems, consider carefully whether certain layers of management can be eliminated post-integration.
- Likewise, if staff reductions are anticipated, consider consolidating management functions, which may lead naturally to bolstering the exempt duties of the remaining managers. Heightened exempt-duty expectations (e.g., evaluating how to achieve cost savings or better patient experience and outcomes) would both bolster exempt status and justify higher salaries.
- As retail clinics and telemedicine opportunities continue to disrupt the way patient care historically has been provided, and patients continue to demand more in-home care, evaluate opportunities to diminish the prevalence of traditional in-facility management responsibilities. At the same time, ensure that remaining managers are well-trained to manage a more dispersed population of subordinates.
- Evaluate relationships with agencies, registries and per diem providers to assess how managerial duties and the distribution of management responsibilities may be altered with key business partners.
- Grant recipients should carefully explore how researchers who are paid with grant funds may be affected by the anticipated increase in the salary threshold. Grant guidelines for salaries may be misaligned with the new thresholds, and may not leave room for increases in subsequent grant funded years. Grant terms that dictate staffing structures may constrain the recipient's ability to adjust. The affected researchers, who seek personal professional advancement through their grant work, often are uniquely self-motivated to work long hours, or are required by clinical tasks to do so, thereby posing predictable challenges should reclassification occur.

- If exempt employees are spending large amounts of time on non-exempt duties in order to meet patient needs, evaluate staffing levels of non-exempt employees and shift models to free up exempt employees to focus more effort on managerial duties.
- If formerly exempt employees will be reclassified as non-exempt, consider bonus incentives, vacation or earned time availability, and other fringe benefits, to competitively attract and retain managers who may view a non-exempt position as less prestigious or important.

With respect to bottom-line payroll spend, the good news is that converting certain job codes does not have to mean added payroll. Healthcare employers may convert to a lower hourly rate than the 40-hour per week, 2,080-hour per year salary equivalent especially if they anticipate additional overtime costs. Healthcare employers might also look at ways to take labor hours out of the facility by, for example, outsourcing certain jobs or functions to third party vendors.

Conclusion

Not-for-profit and for-profit healthcare employers will be impacted by the new FLSA regulations at a time when they are uniquely challenged by ongoing rapid change in the industry. As many continue to evolve their business model to meet an ever-evolving competitive landscape, explore opportunities to incorporate legal solutions into business strategies, thereby reducing business disruption from the regulatory changes once they become effective.

Please contact your Seyfarth attorney or any member of the Firm's 541 Amendments 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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