THE VOICE OF FOOD RETAIL

Feeding Families Enriching Lives

VIA ELECTRONIC SUBMISSION

May 21, 2019

The Honorable Cheryl M. Stanton
Administrator
Wage and Hour Division
United States Department of Labor
200 Constitution Avenue N.W., Rm S-3502
Washington, DC 20210

Re: RIN 1235–AA20, Notice of Proposed Rulemaking, 29 CFR Part 541, *Defining and Delimiting the Exemptions for Executive, Administrative, Professional, Outside Sales and Computer Employees*, 84 FR 10900 (March 22, 2019)

Dear Administrator Stanton:

Food Marketing Institute (FMI) proudly advocates on behalf of the food retail industry, which employs nearly 5 million workers and represents a combined annual sales volume of almost $800 billion. FMI member companies operate nearly 33,000 retail food stores and 12,000 pharmacies. FMI membership includes the entire spectrum of food retail venues; single owner grocery stores, large multi-store supermarket chains, pharmacies, online and mixed retail stores. Through programs in public affairs, food safety, research, education, health and wellness and industry relations, FMI offers resources and provides valuable benefits to almost 1,000 food retail and wholesale member companies and serves 85 international retail member companies. In addition, FMI has almost 500 associate member companies that provide products and services to the food retail industry. For more information, visit www.fmi.org and for information regarding the FMI Foundation, visit www.fmifoundation.org.

FMI submits these comments in response to the proposal of the Department of Labor ("Department"), as published in the Federal Register, 84 FR 10900, on March 22, 2019, to revise the regulations at 29 CFR. Part 541, defining and delimiting the exemptions for executive, administrative, professional, outside sales and computer employees in section 13(a)(1) of the Fair Labor Standards Act (FLSA) (2019 NPRM).

FMI generally supports the Department's proposal, including its commitment to notice-and-comment for future increases to the minimum salary and highly compensated levels, but has several suggestions for additional changes that we discuss in more detail below.

THE MINIMUM SALARY LEVEL

The Department Should Not Use Salary Data From High-Wage Jurisdictions to Set the Minimum Salary Level.

Minimum salary levels have been a part of the Department's overtime exemption regulations since 1940.[1] But, the minimum salary level has always played a narrow role: "a ready method of screening out the obviously nonexempt employees, making an analysis of the duties in such cases unnecessary."[2] When the Department departed from this principal in its most recent rulemaking,[3] the Eastern District of Texas struck down the regulations. The court found that the Department had exceeded its authority by setting the salary level so high ($913 per week, $47,476 annually) as to exclude from the exemptions millions of employees based on salary alone, although the Department admitted the employees performed exempt duties.[4] The court noted, however, that if the Department had simply updated the salary levels using the 2004 methodology, its efforts would almost certainly have been lawful.[5]

Thus, "the Department is proposing simply to update the standard salary level set in 2004 using current data. The Department believes that adherence to the 2004 final rule's methodology is reasonable and appropriate."[6] In 2004, the Department set the minimum salary level at the 20th percentile of actual salaries paid to employees in the South and the retail industry nationwide.[7]

FMI supports a return to the 2004 methodology, but the Department has departed from that methodology by changing the definition of the "South." In 2004, the Department defined the "South" to include only the eight states then included in the East South Central and West South Central Census Divisions: Kentucky, Tennessee, Alabama, Mississippi, Louisiana, Arkansas, Oklahoma and Texas. The Proposed Rule, however, uses salary data from the entire South Census Region.[8] While the South Census Region is the lowest wage *region* in the country, it includes states not considered in 2004 – including Maryland, Virginia and the District of Columbia.[9] These three jurisdictions include some of the highest average salaries in the country.[10]

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[1] *See* Defining and Delimiting the Exemptions for Executive, Administrative, Professional, Outside Sales and Computer Employees; Final Rule, 79 Fed. Reg. 22122, 22165-66 (April 23, 2004) ("2004 Final Rule") (history of the salary levels).

[2] U.S. DEPT. OF LABOR, WAGE & HOUR & PUB. CONTRACTS DIV., REPORT AND RECOMMENDATIONS ON PROPOSED REVISION OF PART 541 REGULATIONS at 8 (1949) ("Weiss ReporT"). *See also* U.S. DEPT. OF LABOR, WAGE & HOUR & PUB. CONTRACTS DIV., REPORT AND RECOMMENDATIONS ON PROPOSED REVISION OF PART 541 REGULATIONS AT 2-3 (1958) ("Kantor Report"); 2004 Final Rule at 22165.

[3] Defining and Delimiting the Exemptions for Executive, Administrative, Professional, Outside Sales and Computer Employees, Final Rule, 81 FR 32391, 32450-51 (May 23, 2016) ("2016 Final Rule").

[4] *Nevada v. U.S. Dep't of Labor*, 275 F. Supp. 3d 795, 805–808 (E.D. Tex. 2017).

[5] *See id.* at 807 n.6.

[6] Notice of Proposed Rulemaking, 29 CFR Part 541, *Defining and Delimiting the Exemptions for Executive,* Administrative, *Professional, Outside Sales and Computer Employees*, 84 Fed. Reg. 10900, 10909 (March 22, 2019) ("Proposed Rule").

[7] *Id.* at 10906.

[8] Proposed Rule at 10925.

[9] The South Census Region includes three Census divisions: the South Atlantic Division, the East South Central Division, and the West South Central Division. *Id.* at 10931. The South Atlantic Division is comprised of Delaware, District of Columbia, Florida, Georgia, Maryland, North Carolina, South Carolina, Virginia and West

To set the minimum salary level for exemption, the Department should apply the actual 2004 methodology to the 2017 data, as it claims to do – that is, setting the minimum salary level at the 20th percentile of salaries actually paid to employees in the states of Kentucky, Tennessee, Alabama, Mississippi, Louisiana, Arkansas, Oklahoma and Texas, and the retail industry nationwide. Salary data from Maryland, Virginia and the District of Columbia should be excluded.[11]

The Department Should Allow All Nondiscretionary Bonuses, Commissions, and Other Incentive Payments to Count Towards the Minimum Salary Level.

In its Proposed Rule, the Department proposes to allow employers to use commissions, bonuses, and other nondiscretionary incentive payments to satisfy up to 10% of the minimum salary level requirement.[12] FMI supports allowing such credits in general, as it recognizes that nondiscretionary incentive payments now make up a large part of compensation packages for many exempt employees.[13] Incentive payments also encourage positive behaviors by linking the employee's compensation to the business's success.[14] The Department correctly recognizes that giving employers the flexibility to structure compensation packages this way is both good for business and consistent with the FLSA's goals.[15] We also applaud the Department for allowing employers to use bonuses and incentive payments paid annually or less frequently, rather than only quarterly as in the 2016 Final Rule.[16]

FMI objects to the Department's 10% cap, however. The Department borrowed that cap from the 2016 Final Rule,[17] which itself failed to explain how the Department settled on 10%.[18] It reasoned that some cap was necessary to ensure that exempt employees continued to receive a fixed annual salary,[19] but nowhere did it explain how it came up with the 10% figure.[20] The number is inconsistent with real compensation plans, many of which now pay exempt employees far more

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Virginia. The East South Central Division is comprised of Alabama, Kentucky, Mississippi and Tennessee. The West South Central Division is comprised of Arkansas, Louisiana, Oklahoma and Texas. *Census Regions and Divisions with State FIPS Codes*, U.S. CENSUS BUREAU, https://www2.census.gov/geo/docs/maps-data/maps/reg_div.txt (last visited May 20, 2019).

[10] *See 2017 Median Household Income in the United States*, U.S. CENSUS BUREAU, https://www.census.gov/library/visualizations/2018/comm/acs-income-map.html (showing median household incomes in Virginia, Maryland, and the District of Columbia in the highest category).

[11] According to the U.S. Chamber of Commerce, applying the actual 2004 methodology results in a minimum salary level of $615 per week (equivalent to $31,980 per year).

[12] Proposed Rule at 10912.

[13] *See* 2016 Final Rule at 32424 (recounting feedback from employers and industry groups that as many as 93% used some form of bonus or incentive-payment plan).

[14] *See id.* (recounting comments from employers that bonus payments give managers a "sense of ownership" in the enterprise's success).

[15] *See id.* (recognizing that nondiscretionary incentive payments "have become associated with EAP skills, such as the exercise of independent judgment and management skills").

[16] Proposed Rule at 10912.

[17] *See* Proposed Rule at 10912 (citing 2016 Final Rule).

[18] *See* 2016 Final Rule at 32425–26.

[19] *Id.* at 32426.

[20] *See id.*

than 10% of their total compensation through incentive payments. In fact, some exempt employees receive as much from those payments as they do from traditional salary.[21]

Employees need no "protection" from incentive-based compensation, and there is no reason for the Department to create disincentives for this type of compensation. They receive the same guaranteed minimum compensation either way – the proposed credit must come from "non-discretionary" incentives, after all; the only difference is that incentive payments encourage success-oriented behavior.[22] The Department itself has recognized that incentive payments increasingly correlate with exempt duties.[23] Large incentive payments therefore are consistent with an employee satisfying the duties tests.[24] This is precisely the sort of short-hand inquiry the salary level was designed to answer.[25] So allowing a higher cap will in fact strengthen the minimum-salary test and help it better serve its original—and only proper—function.

The Department Should Provide a Longer Period for Make-Up Payments and a Safe Harbor for the Nondiscretionary Incentive Payments.

FMI also is concerned that minor or unintentional errors by employers attempting to implement the incentive pay credit could lead to the loss of the exemption and trigger an entirely new class of collective action litigation. The Department proposes to allow employers to cover any shortfall in an employee's annual incentive pay by paying employees a one-time "make-up" payment.[26] The proposal requires, however, that employers make this payment within one pay period after the end of the year.[27]

This window is far too short and inexplicably inconsistent with the window of correction under the highly compensated test.[28] Many businesses are unlikely to catch small mathematical errors within a single pay period.[29] The Department should instead adopt the same one-month time period allowed for make-up payments under the highly compensated employee test, which states:

> If an employee's total annual compensation does not total at least the minimum amount established in paragraph (a) of this section by the last pay period of the 52-week period, the employer may, during the last pay period *or within one*

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[21] *See id.* at 32424 (recounting feedback from employers).

[22] *See* 2016 Final Rule at 32424 (quoting employer comments suggesting that incentive payments link the employee's compensation and the business's success); Sanghee Park & Michael C. Sturman, *The Relative Effects of Merit Pay, Bonuses, and Long-Term Incentives on Future Job Performance*, No. CRI 2009-009 (Cornell Univ. IRL Sch. 2009) (reporting on the different effects different compensation schemes produce and noting that in "general, research has found that pay-for-performance plans do help achieve desired results").

[23] *See* 2016 Final Rule, *supra* note 1, at 10912 (stating that "such payments have become associated with EAP duties, such as the exercise of independent judgment and management skills").

[24] *See id.*; 2016 Final Rule, *supra* note 1, at 32426 (recognizing that bonuses and other incentive payments had become "sufficiently correlated with exempt status").

[25] *See* KANTOR Report, *supra* note 7, at 2–3.

[26] Proposed Rule at 10912–13.

[27] *See id.*

[28] *Cf.* 2004 Final Rule at 22175 (recounting feedback from commenters that it "takes some time after the close of the year to compute the amounts of any commissions or bonuses that are due, such as those based on total sales or profits").

[29] *See id.* ("The Department recognizes that an employer may need some time after the close of the year to make calculations and determine the amount of any catch-up payment that is due.").

> *month after* the end of the 52-week period, make one final payment sufficient to achieve the required level.[30]

The Department rejected a one-month window of correction in 2016 because, at the time, its proposal contemplated that employers could only credit incentives paid quarterly or less frequently.[31] But now, with its proposal to allow employers to credit non-discretionary incentives paid annually, the Department's reason for rejecting a one-month window is no longer relevant.

The Department's proposal also fails to address the consequences of shortfalls. This silence allows an interpretation that an employer whose bonuses fall even a penny short could lose the exemption for the *entire prior year* – and thus owe many thousands in overtime pay to employees who have not been tracking their hours worked (as all thought they were exempt).

In 2004, the Department recognized the importance of preventing such disproportionate penalties when it revised section 541.603 regarding the effect of improper deductions from salary. That section provides that employers shall lose the exemption only "if the facts demonstrate that the employer did not intend to pay employees on a salary basis."[32] Employers do not lose the exemption due to "isolated or inadvertent" improper deductions.[33] The Department provided a safe harbor against losing the exemption in 541.603(d) for employers who adopted and clearly communicated a policy that prohibits improper deductions and includes a complaint mechanism if the employer "reimburses employees for any improper deductions and makes a good faith commitment to comply in the future."

FMI requests that the Department take a similar approach to the incentive pay credit by revising the proposed language to provide that the exemption is not lost if the facts demonstrate that the employer did not intend to pay employees less than the required minimum salary or if the shortfalls are small, isolated or inadvertent. In addition, the Department should adopt a safe harbor for shortfalls similar to the safe harbor in 541.603(d) for salary basis violations.

The Highly Compensated Test

The Department has recognized some type of short-form duties test for well-compensated employees since the 1940s,[34] although it was not until 2004 that the Department adopted the highly compensated exemption in its current form.[35] At that time, the Department explained that the exemption is not intended to exclude employees from overtime pay merely because they are well paid. Instead, the Department recognized that a high salary strongly correlates with exempt

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[30] 29 CFR § 541.601(b)(2) (emphasis added).
[31] The Department rejected a one-month window of correction in 2016 because, at the time, its proposal contemplated that employers could only credit incentives paid quarterly or less frequently. *See* 2016 Final Rule, supra note 1, at 32427. But now, the Department proposes to allow employers to pay the incentives annually. The reason for rejecting a one-month window has therefore fallen away.
[32] 29 CFR § 541.603(a).
[33] 29 CFR § 541.603(c).
[34] *See* U.S. Dept. of Labor, Wage & Hour & Pub. Contracts Div., Report and Recommendations on Proposed Revision of Regulations, Part 541 (1949) at 22–23 (discussing "special provisos" for "high salaried" exempt employees).
[35] 2004 Final Rule at 22174.

duties; thus, it is therefore appropriate to apply a streamlined duties test to an employee who earns a large salary.[36]

The Department's current proposal ignores this principle. If the purpose of the highly compensated test is to provide a short-hand for identifying highly valued employees (and therefore employees likely to perform exempt duties), then the test should be available to any employer. However, by setting the highly compensated level at $147,414, the Department puts the highly compensated level out of reach for employers in many regions and industries. For example, in 29 states, fewer than ten percent of all *households* earn $150,000 per year.[37] Given that households increasingly consist of multiple earners, even fewer employees than that will qualify as highly compensated under the Department's proposal. Thus, the HCE test will become available as a practical matter only in certain states—predominately those on the coasts and with large urban population centers.[38] Whether an employee qualifies for exemption under the highly compensated test will depend more on where the employee works than the employees' job duties.

The Department can solve this problem by relying on the same data set used to determine the minimum salary level for exemption. To set the new highly compensated salary level, the Department used national data instead of a data set limited to salaries in southern states and the retail industry.[39] That choice inflated the final number and clashed with the Department's traditional approach to setting salaries levels at the lower end of the relevant range. This has been true even for tests applicable only to well-compensated employees.[40] For example, when setting salary levels for early forms of the "short test," the Department relied on salary data from low-wage regions and industry groups.[41] It did so in part to avoid penalizing employers in these regions and industries.[42]

The Department should set the highly compensated test at the 90th percentile of a data set including all salaried employees, regardless of salary level, in the retail industry nationwide and the eight southern states (Kentucky, Tennessee, Alabama, Mississippi, Louisiana, Arkansas, Oklahoma and Texas) – and, as discussed below, without any inflationary projections.[43]

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[36] *Id.*

[37] *See* Jeff Desjardins, How Many People make More than $150,000 in Every U.S. State, Business Insider (Nov. 7, 2017) (compiling figures from U.S. Census Bureau).

[38] *Id.* (reporting that the states with the highest percentage of households earning over $150,000 were California, Connecticut, Massachusetts, Maryland, and New Jersey).

[39] 2019 Proposed Rule at 10913.

[40] *See* U.S. Dept. of Labor, Wage & Hour & Pub. Contracts Div., Report and Recommendations on Proposed Revision of Regulations, Part 541 (1958) at 10 (using same lower-wage baseline to calculate salary levels for ordinary exempt employees and "high salaried" employees).

[41] *Id.*

[42] *See* 2004 Final Rule at 22166 (reviewing regulatory history and noting that Department has always used lower-wage regions because the salary level will apply uniformly across the country).

[43] According to comments filed by the U.S. Chamber of Commerce, applying this methodology would result in a highly compensated level of around $122,000 per year.

INFLATIONARY PROJECTIONS

In the Proposed Rule, the Department proposes to inflate both the minimum salary and highly compensated levels to account for expected growth between now and 2020, when it expects the new level to take effect.[44] The Department explained that it thought this inflation was necessary to avoid relying on two-year-old data.[45]

This proposal is inconsistent with historical practice. Except on one occasion, the Department has relied on the most recent available data on actual salaries.[46] The only exemption was in 1975 when the Department found that using an inflationary measure to increase salaries levels was justified due to unusually high inflation at the time. Between March 1970 and February 1974, the Consumer Price Index increased by 23.67 percent.[47] The Department stated that using inflation was "necessary because present economic conditions have substantially impaired the current salary tests as effective guidelines for determining [] exempt status."[48] But the increases based on inflation were "interim rates" only, pending completion of a study by the Bureau of Labor Statistics of actual salaries.[49] Using an inflationary measure, moreover, was not "to be considered a precedent."[50] It should be apparent that inflationary conditions in 1975 bear no resemblance to today. The 12-month percentage increase to the Consumer Price Index, as reported at www.bls.gov/cpi is only two percent.

The Department's justification for its inflationary projection is to avoid reliance on two-year-old data. But that will not be necessary as actual 2018 and 2019 salary data should be readily available before the planned date for publication of the final rule. Instead of applying speculative projections of 2017 data, the Department should base its determinations on actual available for 2018 and 2019 data. Data for all of 2018 and through March 2019 is already published and available. Data through June 2019 will be available to Department analysts by mid-July, providing ample time to update the analysis to reflect the latest available data by January 2020 without resort to speculative projections.

FUTURE INCREASES

FMI agrees with the Department that "the need to update the part 541 earnings thresholds on a regular basis is clear."[51] Although those updates have sometimes come slowly, as the Department concluded in 2004, it does not have authority to increase the minimum salary and highly

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[44] Proposed Rule at 10917 (inflating figures using compound annual growth rate).
[45] *See id.*
[46] *See* 2004 Final Rule, *supra* note 2, at 22165 (surveying past adjustments an observing that each time, the Department used "actual salaries and wages paid to exempt and nonexempt employees").
[47] *See* 40 Fed. Reg. 7091 (Feb. 15, 1975).
[48] *Id.* at 7092.
[49] *Id.* at 7091-92.
[50] *Id.* at 7092.
[51] Proposed Rule at 10914.

compensated levels without notice-and-comment rulemaking as required under the Administrative Procedure Act (APA).[52]

Thus, we applaud the Department for abandoning the automatic updates adopted in the 2016 Final Rule.[53] Instead, the Department proposes to revisit the levels every four years through notice-and-comment rulemaking.[54] The APA contemplates that agencies will enact major policies through notice-and-comment rulemaking.[55] Such rulemaking gives stakeholders an opportunity to weigh in and provide the Department with information.[56] That information can make a difference. For example, in 2004, the Department responded to feedback from employee groups by raising the salary level from $425 to $455 per week.[57] The Department's 2016 automatic indexing approach, by contrast, would have made significant policy changes without any feedback from stakeholders. That is not how Congress intended the process to work.[58]

However, while FMI has no objection to including the methodology for determining future increases in the regulations, we do not believe it is necessary for the Department to adopt by regulation a rigid schedule to update the levels every four years.[59] The Department already has statutory authority to engage in rulemaking to update these regulations from "time to time."[60] Setting a schedule form updating in the Part 541 regulations would therefore serve only to expose the Department to legal challenges—for example, if it failed to adopt a new salary level on schedule.[61] The Department might try to mitigate this risk by wording the regulation to retain discretion over the rulemaking process.[62] But the Department already has that discretion.[63] If the

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[52] 2004 Final Rule at 22171 ("the Department finds nothing in the legislative or regulatory history that would support indexing or automatic updates."). *See also Nevada*, 275 F. Supp. 3d at 808 (finding mechanism to automatically update levels in the 2016 Final Rule unlawful).

[53] 2016 Final Rule at 32430–31.

[54] Proposed Rule at 10918.

[55] *See* 5 U.S.C. § 553.

[56] *See, e.g., Chocolate Mfrs. Ass'n of U.S. v. Block*, 755 F.2d 1098, 1102 (4th Cir. 1985) ("The notice-and-comment procedure encourages public participation in the administrative process and educates the agency, thereby helping to ensure informed agency decisionmaking."); *Nat'l Retired Teachers Ass'n v. U. S. Postal Serv.*, 430 F. Supp. 141, 147 (D.D.C. 1977), *aff'd*, 593 F.2d 1360 (D.C. Cir. 1979) ("One of the central purposes of the notice and comment requirements is to allow public participation in the promulgation of rules which have a substantial impact on those regulated.").

[57] *See* 2004 Final Rule, *supra* note 2, at 22168 (increasing minimum salary from $425 to $455). The Department also responded to public comments by raising the highly compensated minimum salary from $65,000 to $100,000. *See id.* at 22174.

[58] *See Brown Exp., Inc. v. United States*, 607 F.2d 695, 701 (5th Cir. 1979) ("Congress realized that an agency's judgment would be only as good as the information upon which it drew. It prescribed these procedures to ensure that the broadest base of information would be provided to the agency by those most interested and perhaps best informed on the subject of the rulemaking at hand.").

[59] Proposed Rule at 10915 n.140.

[60] *See* 29 U.S.C. § 213(a)(1) (authorizing the Secretary of Labor to define the terms "executive," "administrative," and "professional"); *Auer v. Robbins*, 519 U.S. 452, 456 (1997) ("The FLSA grants the Secretary broad authority to "defin[e] and delimi[t]" the scope of the exemption for executive, administrative, and professional employees." (quoting § 213(a)(1))).

[61] *See Sierra Club v. Thomas*, 828 F.2d 783, 793 (D.C. Cir. 1987) (finding that delay in mandatory rulemaking may be a final reviewable action under the APA) ("[A]gency inaction may represent effectively final agency action that the agency has not frankly acknowledged . . . .").

[62] *See* Proposed Rule at 10915 n.140 (proposing that the Secretary could forgo rulemaking "in his or her sole discretion" for "economic or other" reasons).

regulation does nothing but retain the authority the Department already has, it serves no purpose.[64]

CONCLUSION

Once again, FMI appreciates the opportunity to submit comments in response to the Department's proposal to revise the regulations at 29 CFR. Part 541, defining and delimiting the exemptions for executive, administrative, professional, outside sales and computer employees in section 13(a)(1) of the FLSA. We look forward to our continued collaboration with the Department in the future.

If you have questions about these comments or would like additional information, please feel free to contact me at (202) 452-8444.

Sincerely,

Dana M. Graber
Regulatory Counsel

[63] *See Addison v. Holly Hill Fruit Products, Inc.*, 322 U.S. 607, 613 n.6 (1944) (finding that the Secretary of Labor has authority to define the white-collar exemptions); *Spradling v. City of Tulsa*, 95 F.3d 1492, 1495 (10th Cir. 1996) (same); *Dalheim v. KDFW–TV*, 918 F.2d 1220, 1224 (5th Cir. 1990) (same).
[64] *Cf.* Weiss Report at 9 (acknowledging that if the salary levels need adjusting, the Department can always revisit them).