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SOCIETY FOR HUMAN RESOURCE MANAGEMENT

**SUBMITTED TO
U.S. HOUSE SMALL BUSINESS COMMITTEE**

**HEARING ON
“DAMAGING REPERCUSSIONS: DOL’S OVERTIME RULE,
SMALL EMPLOYERS, AND THEIR EMPLOYEES”**

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Introduction

Chairman Chabot, Ranking Member Velazquez, my name is Christine Walters, and I am the sole-proprietor of the FiveL Company. I have nearly 30 years of combined experience in human resources administration, management, employment law practice and teaching. Previously, I worked as an in-house HR practitioner in the nonprofit sector for 12 years and subsequently served as an adjunct faculty member at the Johns Hopkins University, teaching a variety of courses in graduate, undergraduate and certification-level programs from 1999 to 2006 in human resource management topics.

I appear before you today on behalf of the Society for Human Resource Management (SHRM), of which I have been a member for 17 years. On behalf of our 285,000 members in more than 165 countries, I thank you for this opportunity to appear before the Committee to discuss how changes to the Fair Labor Standards Act (FLSA) overtime regulations impact nonprofits, small businesses, their employees and the communities they serve.

SHRM is the world's largest HR professional society, representing 285,000 members in more than 165 countries. For nearly seven decades, the Society has been the leading provider of resources serving the needs of HR professionals and advancing the practice of human resource management. SHRM has more than 575 affiliated chapters within the United States and subsidiary offices in China, India and United Arab Emirates.

For the last 13 years I have served as an independent HR and employment law consultant. Many of my clients are small businesses, including small government contractors and small nonprofits with limited flexibility in the budget. Many employers are concerned about how they will provide potential overtime expenses under the Department of Labor's (DOL's) final overtime rule.

While SHRM supports an increase to the salary threshold, an increase of more than 100 percent in the first year is too far and too fast. The rule will force many currently exempt employees to lose their exempt status and be converted to nonexempt status. In their eyes, this is perceived as a demotion, a loss of workplace or professional stature and reduced workplace flexibility to meet work/life needs.

In my testimony, I will explain DOL's final overtime regulations, discuss the specific impact on organizations like small businesses and the nonprofit sector, and express SHRM's concerns that the DOL missed a real opportunity to create a final overtime rule that works for both employees and employers.

The Fair Labor Standards Act

The FLSA has been a cornerstone of employment and labor law since 1938. The FLSA establishes minimum wage, overtime pay, record-keeping and youth employment standards affecting full-time and part-time workers in the private sector and in federal, state and local governments. The FLSA was enacted to ensure an adequate standard of living for all Americans by guaranteeing the payment of a minimum wage and overtime for hours worked in excess of 40 in a workweek.

Virtually all organizations are subject to the FLSA. A covered enterprise under the FLSA is any organization that "has employees engaged in commerce or in the production of goods for commerce, or that has employees handling, selling, or otherwise working on goods or materials that have been moved in or produced for commerce by any person; and has \$500,000 in annual gross volume of sales; or engaged in the operation of a hospital, a preschool, an elementary or secondary school, or an institution of higher education."

Additionally, at least 16 states currently have their own "white collar" or "EAP (executive, administrative, professional)" regulations, and some states have overtime laws that are more inclusive or more generous to the employee than federal law. These overlapping requirements mean that both the state and federal laws interact to determine coverage under the wage and hour laws. The myriad federal and state laws create additional complexity as employers carefully navigate employment policies in the workplace.

The FLSA also provides exemptions from both the overtime pay and minimum wage provisions of the Act. Employers and HR professionals use discretion and independent judgment to determine whether employees should be classified as exempt or nonexempt and, thus, whether they qualify for the overtime pay provisions or the minimum wage provisions of the FLSA.

In determining exempt/nonexempt status under the FLSA, employers must look at each individual employee and his or her actual activities. Classification decisions for all employees are challenging as they are based on both objective criteria (salary basis level, salary basis test) and subjective criteria (duties test). As a result, an employer acting in good faith can easily misclassify employees as exempt when they should be nonexempt.

FLSA Overtime Regulations

Regulations governing the FLSA have been revised by the Executive Branch numerous times. Since the FLSA's passage in 1938, the salary threshold has been updated seven times, most recently in 2004. In 2004, the DOL attempted to simplify the overtime regulations for employers and employees by consolidating the long and short duties tests into a single "standard" test and raised the salary threshold. Specifically, under the current regulations, an individual must satisfy three criteria to qualify as a salaried worker exempt from federal overtime pay requirements: first, he or she must be paid a guaranteed minimum salary of \$455 per week (\$23,660 annually); second the employee must be paid on a salary basis (that is, the guaranteed minimum salary cannot be reduced with a few, limited exceptions); and third, his or her "primary duty" must be consistent with those common to executive, professional or administrative positions as detailed in section 541 of the FLSA overtime regulations or one of the other statutorily defined exemptions. Employees who meet these criteria are considered exempt from the overtime requirements of the FLSA.

On March 13, 2014, President Barack Obama directed the DOL to "modernize and streamline" the FLSA overtime regulations. On June 30, 2015, the DOL announced proposed changes to the section 541 FLSA regulations governing overtime determination and coverage. Then, on May 18, 2016, the DOL released its final regulations making changes to the overtime exemptions. Key provisions of DOL's final overtime rule include:

- Increasing the salary threshold by more than 100 percent to \$913 per week, or \$47,476 per year. While this level is slightly lower than the threshold in the proposed rule, it still encompasses many employees who are currently classified as exempt.
- Increasing the total annual compensation level for the "highly compensated employee" ("HCE") to be exempt from the overtime pay requirements to the 90th percentile of full-time salaried workers nationally, or \$134,004 a year.
- Including automatic salary threshold increases every three years to maintain the salary threshold level at the 40th percentile in the lowest-wage census regions. Based on current projections, the salary threshold is expected to rise to more than \$51,000 per year, with its first update on January 1, 2020.

- Requiring an effective date of December 1, 2016.

During the rulemaking process, SHRM was a strong voice for the workplace, supporting an update to the salary threshold using the same guidelines DOL has used in past salary threshold updates. As indicated above, DOL set the salary threshold, under which employees are eligible for overtime, at the 40th percentile of the lowest-wage census district — twice as high as it has been measured in the past. In addition, the final rule includes an automatic increase to the threshold at the 40th percentile, increasing the salary threshold every three years, starting in January 2020. In that year, DOL estimates the new 40th percentile will be \$51,168 — a number that is likely to grow with each automatic adjustment. The doubling of the salary threshold presents unique challenges to nonprofits where salaries tend to be lower, and to small business, including government contractors.

Overtime Regulations' Impact on Nonprofit Sector

Most nonprofit enterprises and their employees are covered under the FLSA because coverage under the law may be triggered either by individual coverage or enterprise coverage. According to a 2004 DOL opinion letter, there is no exclusion in the FLSA for private nonprofit organizations. Employees of nonprofit organizations are individually covered under the FLSA if, in the performance of their duties, they are engaged in interstate commerce or in the production of goods or materials for interstate commerce. In determining whether employees are engaged in interstate commerce for purposes of the FLSA, “the purpose of the Act was to extend federal control in this field throughout the farthest reaches of the channels of interstate commerce.” (*Walling v. Jacksonville Paper Co.*, 317 U.S. 564, 567 (1943)). In other words, if nonprofit employees are involved in fundraising, taking credit card numbers, receiving out-of-state checks or making out-of-state telephone calls, they could be deemed as utilizing the channels of interstate commerce.

As a result of the overtime rule, many nonprofit organizations and small businesses across the country will see an impact on employees, services provided, and the organization at large. The details of these concerns are below.

Impact on Employees. In response to the final rule and an increase in the salary threshold, many nonprofits will be forced to reclassify employees from exempt to nonexempt status, resulting in the possible implementation of a “cap” on overtime work, increasing labor costs if an employee does work overtime, limiting career opportunities and reducing the opportunity for some flexible workplace arrangements.

First, consider the expected reduction in workplace flexibility presented by the final rule. Today many employers provide exempt employees with workplace flexibility, such as the ability to leave work early during the week for a parent teacher conference or telecommuting. Exempt employee compensation is based on the understanding that an employee’s work schedule regularly exceeds 40 hours per week for a full-time employee. Therefore, when the exempt employee is converted to nonexempt status, the flexibility that is enjoyed by many professional employees will be removed.

For example, employees classified as nonexempt are paid for every hour worked and are often required to use paid leave for any partial or full day absence. If the employee has no paid leave remaining, then the absence from work may be without pay (dependent upon state or local law). While it has been suggested that this rule will not diminish workplace flexibility, it is clear newly nonexempt employees will have fewer options to manage work/life needs than they did as an exempt employee.

Furthermore, while some employees will welcome the opportunity for additional overtime pay, many others will perceive the change as a demotion from the salaried, professional status desired by so many in the workplace. It has been suggested that employers can avoid this “demoted” feeling by reclassifying

employees to salaried, nonexempt status. Under this classification, while a salary is paid each work week, the employer is still obligated to pay overtime for all hours worked over 40 in a work-week. Thus, this salary basis of payment still requires an administratively challenging retrospective review every pay period to calculate overtime pay owed, if any, for any hours worked over 40 in a prior work-week. Furthermore, a salaried nonexempt employee must still “punch the clock” to ensure all time is being accurately monitored. Based on my experience, 100 percent of the few clients who have tried this practice, quickly reverted to traditional, hourly pay because of this administrative burden.

Impact on Services Provided. As difficult as the impact may be on the private sector, the rule will drastically impact the budget and operations of nonprofits, as well as colleges and universities, health care providers, small businesses and local governments. These employers may be unable to absorb such costs without adverse impact to employee relations or fiscal operations. As a result, many nonprofits will be forced to tightly monitor hours worked, resulting in less flexibility in how programs and services are structured. As a consultant to a variety of small businesses and nonprofits, please consider the following examples:

One of my clients provides rehabilitation services to a disadvantaged population, of which 85 percent of their clients meet the current poverty threshold. Unlike other employers, this organization cannot transfer increased costs to their lower-income consumers. They face unattractive alternatives - cut expenses which could include labor costs, by abolishing one or more positions or push the duties that are currently performed in excess of 40 hours per week onto a colleague who will remain exempt.

Another nonprofit service provider client, whose reimbursement rates are set by at least two administrative agencies, indicated that as expenses increase, the organization has no ability to raise funding. By recent estimates, 104 out of 520 or approximately 20 percent of their workforce will be impacted by the new overtime rule meaning the organization must decide how to pay the extra overtime expenses or cut critical services.

Similarly, an academic institution has estimated that 75 of 500 or approximately 15 percent of their exempt employees will be impacted by the new rule. They are currently analyzing job duties and responsibilities for coaches and admissions counselors to assess, compare and contrast their options to see if these positions will satisfy other statutory exemptions.

In summary, small businesses, particularly those who are government contractors as well as nonprofits, have limited ability to raise additional funds or rely upon increases from public funding sources to compensate for an influx of overtime expenditures. Public funding is essential and it creates unique constraints. Complying with this rule will not be as simple as adjusting the price of goods sold to cover increased staffing costs for nonprofits. Furthermore, the automatic escalator every three years will create significant costs for nonprofits and small businesses in the years to come.

Mr. Chairman, as you are aware, Congress, the media, and public interest groups have all scrutinized the amount of an organization’s budget that is dedicated to overhead costs, including salaries. Generally, many nonprofit organizations try to limit administrative costs in the budget and direct the majority of funding to services and activities aligned with the organization’s mission.

Impact on Organizations. The compliance costs to business will be significant. In fact, the Office of Advocacy of the U.S. Small Business Administration noted the increasing salary level would add “significant” paperwork burdens on small entities, “particularly businesses in low wage regions and in industries that operate with low profit margins.” The administrative burden will be disproportionately experienced by small businesses and nonprofits that often have one person performing the role of office manager, payroll administrator and HR generalist to ensure compliance.

To suggest that organizations will incur compliance challenges as a result of this rule is an understatement. For many small employers compliance will be intensive and ongoing, in not just the calculations but in tracking down employees. Sometimes employees will forget to fill in a beginning or ending time or to time out from an unpaid meal period. In addition, formerly exempt employees who were not required to monitor their time before the rule, will now need to be fully trained on the employer's tracking requirements.

Increasing the number of employees whose individual working hours must be recorded, reviewed, calculated for straight time and overtime, and submitted for payroll processing is no small task. However, the task for many employers does not stop after navigating the new overtime law. Complex state and local laws must also be navigated by employers who are reclassifying employees, leading to additional administrative time for compliance. Employers must consider:

- Pay Frequency — Some state and local jurisdictions require that nonexempt employees be paid at least twice each month or more frequently. Since more employees will now be classified as nonexempt this will increase payroll costs for employers who pay their exempt employees monthly or less frequently than required by state law for nonexempt employees;
- Pay Day — Some state laws require that nonexempt employees be paid the day before a holiday when the holiday falls on a work day. Employers will now need to ensure that this rule is applied to even more employees who will be reclassified as a result of the rule and adjust their payroll schedules accordingly;
- Pay Deduction — Exempt employees converted to nonexempt will need to understand that they may now be subject to deductions from their pay for lost/damaged company property, the use of sick and vacation leave for less than a day, as well as for tuition reimbursement followed by a separation from employment for a certain period of time;
- Overtime Limits — Some states restrict the amount of overtime that may be required to be worked by nonexempt employees and they have daily overtime requirements as well. Employers will need to plan their staffing needs accordingly since employees who are currently exempt and are converted to nonexempt may no longer be required to work as needed;
- Predictive Scheduling — An increasing number of states and localities are considering or enacting legislation that requires work schedules for nonexempt employees be posted a certain period of time, such as two weeks in advance, and if the work schedule is reduced or modified the employer must pay the employee for all or a portion of the cancelled or modified shift. Employers will need to anticipate these added costs when market, economic, weather and other factors impact staffing and scheduling;
- On Call Pay — Exempt employees converted to nonexempt will now need to be paid for certain on-call hours where such hours constitute "time worked" even if the employee is not actually called to work. This is common in the health care industry such as health care clinics that serve at-risk populations;
- Travel pay — This is time that exempt employees may not currently count as time worked but that may need to be counted as time worked as a nonexempt employee. This can greatly impact educational institutions whose admissions counselors travel to college fairs;
- Waiting Time — Similar to but different from on-call pay, employers will need to ensure that qualifying waiting time is included in projections for time worked for employees who are exempt

today and converted to nonexempt, e.g., where the employee is engaged to wait rather than waiting to be engaged; and

- **Electronic Devices** — The DOL’s regulatory agenda indicates it will publish a Request for Information (RFI) seeking feedback from employers and employees about how time is recorded and paid for hours worked using electronic devices during non-traditional work hours such as evenings and weekends.

As outlined above, the reclassification of many employees will result in numerous considerations that must be carefully navigated by the employer, adding tremendous compliance time for smaller employers and nonprofits with an HR department of one.

SHRM’s Reaction to the Final Overtime Regulations

After receiving over 270,000 comments to its proposed overtime rule, the Administration failed to make any substantive changes to the main elements in the final rule. Although DOL responded to some of our comments, SHRM is disappointed in the dramatic increase in the salary under which employees are eligible for overtime and the automatic increases in the salary level. Unfortunately, DOL missed a real opportunity in finalizing the overtime rule.

While SHRM supports an increase to the salary threshold, an increase of more than 100 percent to the salary threshold in the first year is too far and too fast. The drastic increase will present challenges for employers whose salaries tend to be lower, such as small employers, nonprofits, employers in certain industries and employers in lower cost-of-living areas. Of equal concern, SHRM opposes automatic increases to the salary threshold, which have been considered and rejected in the past. Automatic increases ignore economic variations of industry and location and the overall state of the economy.

The salary threshold — although slightly less than originally proposed — will mean many employees will lose the perceived professional exempt status for which they feel they have worked hard and the flexibility from rigid schedules about which they care deeply. While changes in regulations were meant to benefit employees, a change of this magnitude will do the opposite in many instances. There likely will be fewer opportunities for overtime pay as employers are forced to restructure their compensation and staffing.

Throughout the rulemaking process, SHRM cautioned that the proposed changes to expand overtime eligibility will not necessarily result in a windfall of overtime income for newly classified nonexempt employees. Employers across all sectors monitor labor costs closely and will likely cap or eliminate access to overtime work or will adjust salaries to make sure that an employee’s total wages remain the same even if that employee’s overtime hours increase.

SHRM also believes the changes to the overtime regulations will limit workplace flexibility in some instances and impact certain flexible options such as telecommuting and flextime. Workplace flexibility allows employees to meet work/life needs and benefits the employer through greater employee retention and engagement. Doubling the salary threshold will mean many employees will lose their exempt status and the workplace flexibility it affords. Employers will be forced to closely monitor hours to avoid potential lawsuits and carefully track employee time. Simply put, it is challenging to offer nonexempt employees flexible workplace arrangements because every hour over 40 must be tracked and accounted for. Even though the Administration has repeatedly stated that workplace flexibility will not be reduced, the consequences of the rule are clear — newly nonexempt employees will see diminished flexibility in the workplace.

The Partnership to Protect Workplace Opportunity (PPWO), a diverse group of associations, businesses, and other stakeholders representing employers with millions of employees across the country, has expressed similar concerns with changes to the overtime regulations. The PPWO, co-chaired by SHRM, is made up of 85 associations including private, public, and nonprofit sectors and represents nearly every industry. The Partnership continues to advocate for a regulation that is considerate of all stakeholder and economic realities facing employers and employees, and has urged Congress to support H.R. 4773, the Protecting Workplace Advancement and Opportunity Act.

Given these collective concerns with the current DOL overtime rule, SHRM appreciates the leadership of Representatives Walberg and Kline in introducing H.R. 4773, to nullify the current overtime proposal. This reasonable legislation does not prevent DOL from moving forward with changes to the overtime regulations. It simply requires DOL to perform an economic analysis of how changes to overtime regulations will impact nonprofits, small businesses, and employers in other industry sectors before issuing a new rule. DOL's own final rule recognizes that all these considerations may not have been assessed, stating: "benefits of the rulemaking were not quantified due to data limitations." The bill would also prohibit automatic increases to the salary threshold while ensuring that any proposed changes to the duties test receive proper scrutiny through the formal notice and comment process. SHRM strongly supports this legislation and recommends its swift passage.

Conclusion

In conclusion, Mr. Chairman, small businesses, nonprofits, and employers across the country, are concerned with the final overtime rule. As I noted earlier, more than doubling the salary threshold will significantly impact employers in a variety of industries, and of various sizes, their employees and the populations they serve.

It is important to note that when the overtime regulations were last updated in 2004, a majority of SHRM members reported reclassifying exempt employees to nonexempt status, resulting in lower employee morale, a sense of loss of "workplace status," and increased distrust between employers and employees. SHRM and its members are concerned that these changes to the overtime rule will have the same result.

While SHRM supports an increase to the salary threshold over time, challenges arise if the increase is too high, is implemented too quickly, or fails to consider economic, fiscal, geographic and industry differences. SHRM and its members look forward to working with Congress to improve the overtime rule in a way that works for both employers and employees.

Thank you. I welcome your questions.

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