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States and Business Groups File Lawsuits Seeking to Block DOL's 'White Collar' Overtime Rule

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Twenty-one states, led by Texas and Nevada, have filed a lawsuit against the Department of Labor seeking a preliminary and permanent injunction declaring unlawful the DOL's Final Rule amending the overtime exemption for executive, administrative, and professional employees (the "white collar" exemptions) under the Fair Labor Standards Act.

The U.S. Chamber of Commerce, along with more than 50 other business groups, including the National Automobile Dealers Association, National Association of Manufacturers, and National Retail Federation, filed a separate lawsuit also challenging the DOL's Final Rule.

The Final Rule, scheduled to go into effect on December 1, 2016, more than doubles the salary level requirement for the standard white collar exemptions from $23,660 per year to $47,476 per year and increases the salary level for the highly compensated exemption from $100,000 per year to $134,004 per year. It also, for the first time, requires the salary levels to be adjusted automatically, every three years, to reflect increases to the average salary levels for full-time employees, instead of requiring separate rulemaking by the DOL each time an increase is sought. The Final Rule also will allow employers to satisfy the standard salary level requirement with payment of non-discretionary incentive compensation, but this form of compensation is limited to 10 percent and must be paid at least quarterly.

Both suits were filed in the U.S. District Court for the Eastern District of Texas, a jurisdiction that has been receptive to challenges made to regulatory changes proposed by the Obama Administration.

Final Rule Unconstitutional as Applied to State Governments

The lawsuit filed by the coalition of state governments challenges nearly every aspect of the Final Rule.

As it applies to state governments, the lawsuit alleges the Final Rule is unconstitutional because it permits the federal government to force states to commit their limited resources to increased labor costs, requiring state governments to shift resources from other important priorities the state would otherwise pursue. "By committing an ever-increasing amount of *State* funds to paying State employee salaries or overtime, the Federal Executive can unilaterally deplete State resources,

forcing the States to adopt or acquiesce to federal policies, instead of implementing State policies and priorities," according to the complaint.

The complaint acknowledges, however, that Congress amended the FLSA in 1974 to extend coverage to state governments, and that the U.S. Supreme Court in *Garcia v. San Antonio Metro. Transit Auth.*, 469 U.S. 528 (1985), held that extending coverage of the FLSA to state governments did not violate the Constitution (overruling its prior decision in *National League of Cities v. Usery*, 426 U.S. 833 (1976)). The complaint argues that more recent jurisprudence casts doubt on the continued validity of *Garcia* and that it should be "overruled."

Similar to complaints lodged by private businesses and non-profit organizations that have been struggling to address the increased labor costs resulting from the Final Rule, the complaint alleges the Final Rule will cause a significant increase in labor costs to state governments resulting in the elimination of essential government services and functions and the reduction of hours and pay to employees to avoid payment of overtime. The complaint estimates the Final Rule will cost Iowa $19.1 million and Arizona $10 million.

Salary Level Should Not Be Litmus Test for Determining Exempt Status

In addition to challenging the constitutionality of the Final Rule as it applies to state governments, the state-led lawsuit broadly challenges the validity of the Final Rule in ways that would apply equally to enforcement against private employers.

The lawsuit argues the Final Rule imposes a salary level requirement as a prerequisite for the white collar exemptions to apply, but the statute itself contains no salary basis or salary level requirement, instead focusing on the duties of the employees. Under the Final Rule, for example, even if an employee squarely performs the duties of an exempt employee, if the employee does not earn the requisite salary level, the exemption cannot apply. "Salary may be one factor to be considered, but it cannot be a litmus test," according to the complaint.

While the complaint correctly notes the FLSA itself does not contain a salary level requirement for the exemption to apply, the DOL added a salary level requirement in 1940. Since that time, DOL's regulations have always required a minimum salary level for the white collar exemptions to apply (except for certain positions, such as doctors, lawyers, and teachers).

A successful challenge to the salary level requirement as a prerequisite would have broad applicability and result in sweeping changes to the regulations, nullifying the Final Rule and the salary level requirement, and requiring the DOL to refocus the exemption analysis on the duties performed by the employee, not the salary they earn.

The state-led lawsuit, however, may face an upward battle on this point given Congress' broad delegation to the DOL to implement the white collar exemptions, and thousands of cases that have applied the white collar exemptions and the requirement that employees receive a minimum salary level.

Delegation of Rulemaking to DOL Unlawful

Likely anticipating the DOL's argument the salary level requirement is lawful given the broad delegation to the agency to implement the white collar exemptions, the lawsuit argues that Congress' broad delegation to DOL without any "intelligible principle by which DOL was to establish the

qualifications of the white collar exemption" is itself unconstitutional because DOL is exercising a legislative function, not a regulatory function.

Automatic Salary Level Increases Unlawful

The state lawsuit also takes aim at the Final Rule's automatic indexing or increases to the salary level every three years, arguing this portion of the Final Rule violates the FLSA's requirement that the DOL define and delimit the exemptions "from time to time" and the notice and comment requirements of the Administrative Procedures Act. The Chamber-led lawsuit joins this challenge, arguing there is no "basis to conclude that Congress authorized the Department to index the salary level," contrasting it to other statutes that expressly authorize cost-of-living increases.

This aspect of the lawsuits might have strong appeal, as the DOL itself noted in previous rulemaking in 2004 that automatic indexing was contrary to congressional intent. The DOL reversed its position on this point in the 2016 Final Rule.

Salary Level Set Too High

The Chamber lawsuit also attacks the new salary level set by the DOL, calling it arbitrary, resulting in the exclusion of too many workers who otherwise satisfy the duties requirement for the exemptions. "The Rule raises the minimum salary threshold so high that the new salary threshold is no longer a plausible proxy for the categories exempted by Congress," according to the Chamber complaint.

Salary Level and 10% Rule Arbitrary

The Chamber-led lawsuit also seeks to invalidate the Final Rule's limitation on the use of non-discretionary incentive compensation to satisfy the salary level requirement. The DOL, for the first time, is permitting employers to pay up to 10 percent of the required salary level in the form of non-discretionary compensation. But the lawsuit alleges that the provision is "so restricted by the DOL as to be meaningless" because the rule excludes non-discretionary bonus, commissions, and incentives paid less than quarterly and excludes other types of compensation, such as discretionary bonuses.

Ensuring Compliance

Owing to the December 1, 2016, effective date, the plaintiffs in both lawsuits likely will ask for expedited briefing and ruling on the motion. But given the short time before the effective date, employers should prepare for the changes to the exemption to ensure they are compliant come December 1, 2016.

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