EMPLOYMENT, LABOR & WORKFORCE MANAGEMENT

EPSTEIN BECKER GREEN

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The Ground Continues to Shift in Wage and Hour Law

A year ago, employers across the country prepared for the implementation of a new overtime rule that would dramatically increase the salary threshold for white-collar exemptions, on the understanding that the new rule would soon go into effect "unless something dramatic happens," a phrase we and others used repeatedly.

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And, of course, something dramatic did happen—a preliminary injunction, followed by a lengthy appeal, which itself took more left turns following the U.S. presidential election than a driver in a NASCAR race. The effect was to put employers in a constant holding pattern as they were left to speculate whether and when the rule would ever go into effect.

The current status of the overtime rule is but one of several prominent issues to reckon with as wage and hour issues, investigations, and litigation remain as prevalent as they have ever been.

The articles in this edition of *Take 5* include the following:

1. The Status of the Department of Labor's 2016 Overtime Rule

By Paul DeCamp and Jonathan M. Brenner

It appears that the Obama-era white-collar overtime rules may soon be off the books, barring further surprises from the federal courts. In their place, employers can expect a new regulation implementing a salary threshold for the executive, administrative, and professional exemptions under the Fair Labor Standards Act ("FLSA") somewhere in the neighborhood of $33,000 per year.

The 2016 Final Rule

In May 2016, the U.S. Department of Labor ("DOL" or "Department") published its "Final Rule" that, among other things, would have:

- more than doubled the minimum salary for these exemptions from $455/week ($23,660/year) to $913/week ($47,476/year);
- increased the total annual compensation required for the highly compensated variant of these exemptions from $100,000 to $134,004; and
- automatically adjusted these levels every three years.

By the DOL's own estimate, the Final Rule would have immediately rendered 4.2 million previously exempt employees eligible for overtime pay if their employers took no action.

Court Challenges

Twenty-one states and dozens of private business associations filed two separate lawsuits challenging the Final Rule. The state plaintiffs sought a preliminary injunction, while the business associations pursued summary judgment.

Just nine days ahead of the December 1, 2016, effective date of the regulations, Judge Amos Mazzant of the U.S. District Court for the Eastern District of Texas issued a nationwide preliminary injunction barring the DOL from "implementing and enforcing" the key provisions of the Final Rule. The ruling suggested that the Department lacks the authority to require any salary threshold for the exemptions.

The DOL appealed to the U.S. Court of Appeals for the Fifth Circuit, initially taking the position in its opening brief that the Final Rule is valid in all respects. After the change of administrations, the Department filed its reply brief, expressly disavowing the salary level set in the Final Rule, but asking the Fifth Circuit to confirm the DOL's authority under the FLSA to require *some* salary threshold.

The Fifth Circuit scheduled oral argument for October 3, 2017.

Meanwhile . . .

In June 2017, a Chipotle employee filed a private class action in federal court in New Jersey alleging that the company failed to comply with the Final Rule. The theory in the complaint is that because "the Eastern District of Texas did not stay the effective date of the rule or otherwise prevent the Rule from going into effect . . . . the Rule went into effect on December 1, 2016."

In July 2017, the DOL issued a Request for Information ("RFI") seeking public input on a variety of topics relating to what the appropriate salary threshold(s), if any, would be for the white-collar exemptions, including whether there should be variations based on such factors as employer size, census division, or state. The comment period for the RFI closed on September 25, 2017.

Summary Judgment and the DOL Withdraws Its Appeal

On August 31, 2017, Judge Mazzant issued a ruling granting the pending motion for summary judgment, concluding that (i) the Final Rule is contrary to the FLSA and (ii) the Department has the authority to implement a salary threshold, just not one this high.

Five days later, the DOL sought to drop its appeal in the Fifth Circuit in light of the district court's ruling, which the circuit court dismissed on September 6, 2017.

The DOL may appeal the summary judgment ruling. If it does, the goal would be to delay any final ruling until the Department can issue new overtime regulations, as well as maintain a friendly forum to resolve the issue presented in the *Chipotle* case, if need be.

The wild card is the lawsuit against Chipotle. Although the case seems unlikely to gain traction, it is possible that the district court or the Third Circuit could breathe new life into the Final Rule through that litigation.

Takeaways

Employers that made changes in anticipation of the implementation of the 2016 Final Rule will probably find that their best path forward is to maintain that practice, not least because of the employee relations concerns with changing classifications or pay.

Employers that did not change their practices, or that initially changed practices but then reverted to their prior state after the preliminary injunction, may take some additional encouragement from recent developments, despite the fluidity and continued uncertainty surrounding the Final Rule.

Of course, employers will want to look out for the DOL's next overtime rule, which is likely coming in the next several months. Based on Secretary of Labor Alexander Acosta's testimony during his confirmation hearing, the expectation is that the next salary threshold will be "around $33,000," though the Department may elect to go in a different direction based on the comments received in response to the RFI.

2. Recent Developments Regarding Tip Pooling

By Jeffrey H. Ruzal and Brian W. Steinbach

May employers maintain full control over the distribution of customers' tips to employees?

Until recently, the DOL has unequivocally said that they may not. However, the DOL's regulation restricting tip pooling and distribution is apparently on the chopping block. And, to further complicate matters, a circuit split on this issue may result in review by the U.S. Supreme Court.

Background—The Tip Credit, *Cumbie,* and the DOL Regulation

Under the FLSA, as well as many state wage and hour laws, an employer may pay tip-earning employees a reduced, subminimum hourly wage as long as they receive sufficient tips that, when combined with the subminimum wage, meet or exceed the prevailing minimum wage. In addition to tips that employees receive directly, the FLSA allows an employer to claim the credit for tips distributed from a tip pool in which participation is limited to employees who customarily and regularly receive tips, such as servers and bartenders in the restaurant industry. Participation in a tip pool by non-tip-earning employees, such as cooks and dishwashers, invalidates its use for the tip credit.

More controversial, however, is that the DOL expanded its regulation of tip pools, maintaining that it may do so regardless of whether an employer takes a tip credit against the wages of employees participating in a tip pool. The controversy stems from the fact that the courts did not initially interpret the rules regulating tip pooling to apply to employers that *did not* take a tip credit against employees' wages.

Thus, in *Cumbie v. Woody Woo, Inc.*, 596 F.3d 577 (9th Cir. 2010), the Ninth Circuit held that the FLSA did not bar an employer from distributing pooled tips to "back of the house" employees where the employer did not take a tip credit against its employees' wages. In response to the *Woody Woo* decision, the DOL issued a regulation explicitly barring distribution to non-tipped employees even when a tip credit is not taken.[1]

Judicial Response to the DOL Regulation and Likely Supreme Court Review

Challenges to the DOL regulation initially succeeded in two federal district court cases: *Oregon Restaurant*[2] and *Wynn Las Vegas*.[3]

However, in a consolidated decision on appeal,[4] the Ninth Circuit—which previously decided *Cumbie*—upheld the DOL's regulation as a proper exercise of its discretion.

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[1] 76 Fed. Reg. 18,831, 18,855 (April 5, 2011), amending 29 C.F.R. §531.52.
[2] *Oregon Rest. & Lodging v. Solis*, 948 F. Supp. 2d 1217 (D. Or. 2013).
[3] *Cesarz v. Wynn Las Vegas, LLC*, No. 2:13-cv-00109-RCJ-CWH, 2014 U.S. Dist. LEXIS 3094 (D. Nev. Jan. 10, 2014).

The Tenth Circuit disagreed, however. In *Marlow v. The New Food Guy, Inc*., 861 F.3d 1157 (10th Cir. 2017), the Tenth Circuit explicitly rejected the *Oregon Restaurant* decision, finding that (i) the FLSA does not state that tips are always the property of employees and, if the tip credit is not taken, tips may be distributed by employers at will, and (ii) the DOL was not vested with such rulemaking authority in this instance.

This divergence between the Ninth and Tenth Circuits increases the likelihood that the Supreme Court will grant pending requests for review of *Oregon Restaurant*. The issue of whether the DOL exceeded its rulemaking authority is particularly ripe and transcends just tip-pooling regulations. (As discussed by our colleagues above, the U.S. District Court for the Eastern District of Texas recently struck down as improper a DOL rule increasing the annual salary threshold requirement from $23,660 to $47,476.)

The Trump Administration's Input

Further complicating the issue, on July 20, 2017, the DOL announced its plan to rescind this controversial regulation (although to date it has not done so). The DOL also indicated that it would not enforce the regulation, suggesting that it may either decline to defend the regulation before the Supreme Court or argue that a review is not necessary because the regulation is not being enforced and will soon be rescinded.

Takeaway

Even if the DOL does not enforce the regulation, employees can still pursue private lawsuits in connection with invalid tip-pool claims and, more generally, claims concerning tip redistribution from tip pools. Accordingly, employers should continue to proceed with caution in this area and consider applicable state laws.

For example, in California, all tips must be distributed to employees, including the full value of credit card tips. And Minnesota and New Hampshire require all tips to be distributed to employees and bar mandatory tip pools.

3. Mandatory Class Action Waivers in Employment Agreements: Is a Final Answer Forthcoming?

By Frank C. Morris, Jr., and Shira M. Blank

Many employers use or have considered using arbitration agreements that both require all employment-related claims to be adjudicated in arbitration and preclude class and/or collective claims. These agreements can be invaluable tools to limit costly and time-consuming class and collective actions brought by, or on behalf of, large groups.

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[4] *Oregon Restaurant and Lodging v. Solis*, 816 F.3d 1080 (9th Cir. 2016), *pet. for reh'g en banc denied*, 843 F.3d 355, *pet. for cert. filed sub nom. Wynn Las Vegas, LLC v. Cesarz*, No. 16-163 (Aug. 1, 2016), and *sub nom. National Restaurant Assoc. v. U.S. Dept. of Labor*, No. 16-920 (Jan. 19, 2017).

In recent years, the U.S. Supreme Court has interpreted the Federal Arbitration Act, 9 U.S.C. § 1 *et seq.* ("FAA"), to enforce arbitration agreements despite objections mounted by the plaintiffs' bar and some state courts.

While the Supreme Court has upheld class action waivers in the consumer context, it is unclear whether the FAA's liberal approach to arbitration applies in the employment context. The National Labor Relations Board ("NLRB" or "Board") contends that these provisions are unlawful because the potential formation of class or collective actions contesting employment issues is a "group activity" allegedly embraced by the National Labor Relations Act's ("NLRA's") Section 7 right of employees to engage in "protected concerted" activities.

On October 2, 2017, the first day of its fall 2017 term, the Supreme Court will hear arguments in three related cases involving the legality of class action waivers in arbitration agreements for employment-related claims: *Ernst & Young LLP v. Morris*, *Epic Systems Corp. v. Lewis,* and *NLRB v. Murphy Oil USA, Inc*. In all three cases, the plaintiffs, who had previously signed arbitration agreements containing waivers, asserted collective action claims under the FLSA, as well as state law wage claims. The defendant employers moved to dismiss the collective actions and compel individual arbitration of the employees' claims. At issue in all three cases is whether arbitration agreements prohibiting class and/or collective actions are enforceable or barred by the NLRA.

The Circuit Court Split

The Fifth Circuit, in *NLRB v. Murphy Oil USA, Inc.*, 808 F.3d 1013 (5th Cir. 2015), rejected the NLRB's position and held that adjudicating a claim collectively is *not* a substantive right protected by the NLRA, and that the Board's interpretation of the NLRA impermissibly conflicts with the FAA. The Second and Eight Circuits have also held that class action waivers are enforceable.

The Seventh and Ninth Circuits, on the other hand, have adopted the Board's position that such agreements are a violation of the NLRA, in *Lewis v. Epic Systems Corp.*, 823 F.3d 1147 (7th Cir. 2016), and *Morris v. Ernst & Young, LLP*, 834 F.3d 975 (9th Cir. 2016), respectively.

In *Lewis*, the Seventh Circuit declined to enforce a clause that precluded employees from seeking any class, collective, or representative remedies in wage and hour disputes. The court found that the clause was unenforceable because it required employees to stipulate away their NLRA Section 7 rights. Moreover, the court found that the clause was unenforceable under the FAA. Because the court viewed the clause as unlawful under Section 7 of the NLRA, it was therefore an illegal provision and met the criteria of the FAA's saving clause for non-enforcement.

A few months later, the Ninth Circuit in *Morris* also held that the NLRA precludes agreements requiring employees to waive concerted legal claims regarding wages, hours, and terms or conditions of employment.

What Will the Supreme Court Do?

As noted, the Supreme Court has demonstrated a preference for arbitration in recent years. The confirmation of Justice Neil Gorsuch may also favor the enforcement of class action waivers in arbitration agreements. Justice Gorsuch's past arbitration rulings demonstrate that he favors the FAA's liberal approach to enforcement of arbitration agreements and sees the FAA as establishing substantive federal law favoring arbitration that preempts conflicting state law doctrines. Moreover, past decisions show a reluctance to defer to administrative agency interpretations and skepticism of aggressive agency action. He has already expressed the view that the NLRB should have a more limited scope of authority. Accordingly, Justice Gorsuch may, in the case of a split, cast the deciding vote, and there is reason to believe that the Court will again find in favor of the legality of class action waivers.

While we cannot definitively predict the Supreme Court's decision, we can be sure that the decision will greatly impact employers and employees alike, and that it will provide much-needed clarity on this key issue.

Takeaways

Once the Supreme Court issues its ruling, employers should (i) promptly review their existing mandatory arbitration and class waiver agreements and (ii) consider adopting them (if not already in use) if the Court rejects the NLRB's arguments.

4. "Time Rounding": The Next Wave of Class and Collective Actions

By Michael S. Kun and Kevin Sullivan

The history of wage and hour class and collective actions has followed a fairly distinct path. First came claims alleging that employees had been misclassified as exempt under the FLSA and/or state law. Next came claims alleging employees had not been paid for all time worked or, in state actions, that employees had not received required meal and rest periods.

Many have wondered what the next wave of class actions might be. That question appears to have been answered—time-rounding claims.

Why, one might ask, *would plaintiffs bring claims regarding time rounding when the law is clear that time rounding is lawful?*

The answer is not as straightforward as one might suspect.

It is true, of course, that regulations and court decisions have confirmed that employers may use evenhanded time-rounding policies—that is, policies that round employees' time either up or down to the nearest five-, six-, or 15-minute increment are lawful on their face.[5]

But what about *in practice*? Is the impact of time rounding evenhanded as it is actually applied to employees?

And that is the basis of the time-rounding claims brought by employees, which appear to be the beginning of the next wave of class and collective actions.

In these cases, plaintiffs typically allege that while time-rounding policies may be neutral on their face, they are not neutral in practice. Specifically, plaintiffs argue that their time and payroll records reveal that they and other employees are regularly disadvantaged by time rounding to the financial benefit of their employers—and that the total amounts underpaid to all employees are enormous.

In connection with that argument, plaintiffs also often argue that time-rounding policies must be read in connection with their employers' other policies, such as attendance and tardiness policies. They argue that if employees face discipline for being late to work, or for being late returning from a meal period, it is more likely that employees will arrive at work early or return to work early—meaning that time rounding is more likely to disadvantage employees.

On first glance, these theories appear to be supported by logic. On second glance, however, they may fall apart. While it is true that an employee might be more likely to report to work early than late because of the employer's attendance policy, time rounding could still *benefit* the employee.

For example, if an employer has a policy by which employees' punch times are rounded to the nearest 15 minutes, an employee who shows up three minutes early to avoid discipline will be disadvantaged. But an employee who reports to work eight minutes early will have his or her time rounded to the nearest 15 minutes such that he or she would actually *gain* seven minutes. And even the employee who reports to work seven minutes or less early such that the start time is rounded up could still benefit from time rounding depending on when he or she leaves work at the end of the day. For instance, while an employee who reports to work three minutes early might lose three minutes of time to time rounding at the start of the day, if he or she left work eight minutes late, he or she would *gain* more time at the end of the day such that the total impact of rounding *benefited* him or her for that day.

There is another problem with many time-rounding claims brought by plaintiffs. Specifically, plaintiffs and their counsel often ask the courts to assume that all time that an employee is "on the clock" is compensable. However, there is valid argument that

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[5] 29 C.F.R. § 785.48(b); *Alonzo v. Maximus, Inc*., 832 F. Supp. 1122 (C.D. Cal. 2011); *Contini v. United Trophy Mtg.*, 2007 U.S. Dist. LEXIS 42510 (M.D. Fla. June 20, 2007); *Harding v. Time Warner, Inc.*, 2009 U.S. Dist. LEXIS 72852 (S.D. Cal. Aug. 18, 2019); *East v. Bullock's, Inc*., 34 F. Supp. 2d 1176 (D. Ariz. 1998).

employees are not entitled to be paid for time engaged in personal activities after they punch in at the start of the day but before they commence work.[6] For instance, an employee who arrives at work early and punches in, then sits in the break room reading a newspaper and drinking coffee for 10 minutes, arguably is not entitled to be paid for that time. And that non-compensable, pre-shift time could be the difference between whether an employer's time-rounding policy is neutral in practice or not.

Ultimately, with more and more time-rounding class actions and collective actions being filed, employers should ask themselves a critical question: Do we really want a time-rounding policy and, if so, why?

There are, of course, entirely legitimate reasons for an employer to maintain time-rounding policies. While the argument that time-rounding policies make cutting paychecks easier administratively may not be as sound as it once was given the ease with which compensation can be calculated electronically, the desire to have a healthy work environment where employees do not feel hounded to commence work immediately upon punching in is a very reasonable one. So, too, are issues dealing with the location of time clocks or lines to punch in and out.

That said, any employer that is looking to save labor costs through time rounding not only does not have a legitimate reason to maintain a policy but will have a difficult time explaining itself in litigation.

Takeaway

As time-rounding class actions become more prevalent, it will not be a surprise to see more and more employers abandon what was once considered a "best practice" simply to avoid the possibility of litigation and the risks and costs that follow. Those that stick with the policies will need to be prepared to defend them—and being able to show that employees spend a couple minutes getting coffee before commencing work could make the difference in defeating a class certification motion or in prevailing on the merits.

5. **The Department of Labor, Congress, and the Courts Wrestle with the Definition of "Employee"**

By Michael D. Thompson and James J. Sawczyn

The potential misclassification of employees as independent contractors received considerable attention from federal agencies during the Obama administration. The Wage and Hour Division of the DOL was skeptical of independent contractor status, issuing guidance that stated that "most workers are employees." The Trump administration and Republican legislators seem intent on reversing this expansive definition of "employee."

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[6] *See, e.g.*, 29 C.F.R. § 785.48(a); Cal. Department of Labor Standards Enforcement Manual § 47.2.2.

The DOL During the Obama Administration

As part of the DOL's Wage and Hour Division's initiative to combat worker misclassification under President Obama, the Division's Administrator issued Administrator's Interpretation No. 2015-1 on July 15, 2015 ("Interpretation"). The Interpretation advocated for a reading of the "economic realities test" that favored classifying most workers as employees rather than independent contractors under the FLSA.

The Interpretation pointed out that, to determine whether a worker should be classified as either an employee or an independent contractor under the FLSA, courts rely on the following six factors comprising the "economic realities test": (i) the extent to which the work performed is an integral part of the employer's business, (ii) the worker's opportunity for profit or loss, (iii) the nature and extent of the worker's investment in his or her business, (iv) whether the work performed requires special skill and initiative, (v) the permanency of the relationship, and (vi) the degree of control exercised or retained by the employer. The Interpretation advocated for interpretations of these factors that have not been universally applied by courts and would result in more workers being classified as employees rather than independent contractors.

Significantly, the Interpretation rejected courts' historical emphasis on the "control" factor, and focused instead on workers' entrepreneurial activities. Regarding the worker's opportunity for profit or loss, the Interpretation argued that this factor should focus on not only the opportunity for profit or loss but also whether the worker has the ability to make decisions and use his or her managerial skill and initiative to affect opportunity for profit or loss. As to the nature and extent of a worker's investment, the Interpretation stated that the worker's investment must be substantial when compared to the putative employer's investment for the worker to be engaged in an independent business.

The DOL During the Trump Administration

On June 7, 2017, Secretary Acosta announced that the DOL was withdrawing the Interpretation. It appears that the DOL has chosen to reject the previous administration's interpretation of the "economic realities test," which disfavored the independent contractor classification. If this is true, employers may anticipate seeing (i) less of an emphasis on workers' entrepreneurial activities in DOL enforcement proceedings and (ii) a return to a focus on the degree of control exerted by the putative employer over workers.

In a move that may signal a further shift from the DOL's policies under President Obama, on September 6, 2017, President Trump announced that he was nominating Cheryl Stanton, a former shareholder at a management-side employment firm, as Administrator of the Wage and Hour Division.

Courts' Positions on Independent Contractors

Prior to its withdrawal, the Interpretation appears to have had minimal influence on how courts applied the "economic realities test" in misclassification cases. For example, in its March 2017 decision in *Hall v. DirecTV LLC*, 846 F.3d 757 (4th Cir. 2017), the Fourth Circuit reversed a district court decision dismissing the complaint in a putative FLSA collective action brought by a group of satellite television technicians. In holding that the plaintiffs' adequately alleged that they were employees of DirecTV rather than independent contractors, the Fourth Circuit made no reference to the Interpretation. The appellate court did, however, note that the district court's error was understandable "given the confused state of FLSA joint employment case law."

Congress and the Save Local Business Act

The controversy surrounding independent contractor status and joint employment was not limited to FLSA matters. For example, in *Browning-Ferris Industries of California*, the NLRB found that a business could be deemed a joint employer if it exerts "indirect control" over a contractor or reserves for itself the ability to exert such control. In response, Republican legislators have introduced the Save Local Business Act, a bill that would amend both the NLRA and the FLSA to say the following:

> A person may be considered a joint employer in relation to an employee only if such person directly, actually, and immediately, and not in a limited and routine manner, exercises significant control over the essential terms and conditions of employment (including hiring employees, discharging employees, determining individual employee rates of pay and benefits, day-to-day supervision of employees, assigning individual work schedules, positions, and tasks, and administering employee discipline).

Congress will consider the Save Local Business Act while simultaneously weighing other options. On September 6, 2017, the House Committee on Education and the Workforce held a hearing on the sharing economy and the protections that may be needed to protect the workers of companies such as Uber and Homejoy, who are typically classified as independent contractors.

Takeaway

Prior to its withdrawal, the Interpretation appears to have had minimal influence on how courts apply the "economic realities test" in misclassification cases. Likewise, the withdrawal of the Interpretation will likely have little effect on how courts apply the test. A legislative response to this confusion is a strong possibility, but for the time being, federal courts will continue to analyze whether a worker is an employee or independent contractor by applying their own versions of the "economic realities" test consistent with precedent.

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For additional information about the issues discussed above, please contact the Epstein Becker Green attorney who regularly handles your legal matters, or an author of this *Take 5:*

Shira M. Blank
New York
212-351-4694
SBlank@ebglaw.com

Jonathan M. Brenner
Los Angeles
310-557-9504
JBrenner@ebglaw.com

Paul DeCamp
Washington, DC
202-861-1819
PDeCamp@ebglaw.com

Michael S. Kun
Los Angeles
310-557-9501
MKun@ebglaw.com

Frank C. Morris, Jr.
Washington, DC
202-861-1880
FMorris@ebglaw.com

Jeffrey H. Ruzal
New York
212-351-3762
JRuzal@ebglaw.com

James J. Sawczyn
Newark
973-848-7728
JSawczyn@ebglaw.com

Brian W. Steinbach
Washington, DC
202-861-1870
BSteinbach@ebglaw.com

Kevin Sullivan
Los Angeles
310-557-9576
KSullivan@ebglaw.com

Michael D. Thompson
Newark
973-639-8282
MDThompson@ebglaw.com

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