SULLIVAN & CROMWELL LLP

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Nevada v. *U.S. Department of Labor*: Federal Court Invalidates 2016 Overtime Regulations

After Preliminarily Enjoining U.S. Department of Labor's Overtime Exemption Regulations, Federal Judge Issues Permanent Injunction

SUMMARY

On August 31, 2017, the United States District Court for the Eastern District of Texas issued a ruling holding that the U.S. Department of Labor's 2016 overtime exemption regulations were unlawful. The court previously preliminarily enjoined the regulations from coming into effect. As noted in our prior Client Alert, the 2016 regulations provided that employees could not qualify for the white-collar exemption to the minimum-wage and overtime requirements of the Fair Labor Standards Act ("FLSA"), regardless of their duties, unless they earned more than $47,476 per year. This ruling makes the prior preliminary injunction permanent. The district court held that the Department exceeded its statutory authorization because Congress intended for the white-collar exemption to apply based on employees' job duties. The court reasoned that although the Department has the authority to implement a salary-level test for overtime exemption eligibility, the 2016 regulations raised the salary level too high, thereby impermissibly supplanting an analysis of an employee's job duties.

The decision significantly decreases the risk to employers who chose not to comply with the 2016 overtime regulations in reliance on the preliminary injunction. In light of the decision, earlier today the Department asked the Fifth Circuit to dismiss its prior appeal of the preliminary injunction. The Department had challenged the district court's preliminary injunction ruling to the extent it held that the Department may not use a salary-level test in its white-collar exemption regulations. But in its August 31 decision, the district court clarified that the Department may use a salary-level test so long as it does not supplant a duties test. It bears mention that the ruling does not affect state overtime laws, which were not affected by the August 31 decision.

BACKGROUND

Section 213(a)(1) of the FLSA exempts from minimum-wage and overtime requirements "any employee employed in a bona fide executive, administrative, or professional capacity,"[1] which is commonly referred to as the "white-collar" exemption. The FLSA authorizes the Secretary of Labor to define and delimit the terms of the exemption.[2] Since the 1940s, the U.S. Department of Labor (the "Department") has included a "salary-level test" as part of its regulations, which requires an employee to be paid at least the minimum-salary level established by the regulations to qualify for the exemption.[3] The salary-level requirements have been updated seven times.[4]

On May 18, 2016, the Department issued new regulations governing the white-collar exemption. Under prior regulations, an employee had to earn more than $23,660 per year to qualify for the white-collar exemption. The 2016 regulations, among other things, raised the salary level to $47,476 annually for a full-year worker, and provided a mechanism to adjust the salary thresholds for overtime-exempt employees every three years.[5] The regulations were scheduled to take effect on December 1, 2016, and were estimated to reclassify about 4.2 million workers as non-exempt.[6]

On September 20, 2016, more than 50 business coalitions (the "Business Plaintiffs") and 21 states each filed suit in the Eastern District of Texas challenging the Department's regulations.[7] They argued that the Department's salary-level test violated the text of the FLSA, the automatic-updating mechanism violated the Administrative Procedure Act, and the regulations violated the Constitution by requiring states to pay their employees overtime.[8] The Business Plaintiffs and states each sought an injunction preventing implementation and enforcement of the regulations, and the district court consolidated both actions.[9]

On November 22, 2016, shortly before the regulations were scheduled to take effect, Judge Amos Mazzant (who was appointed by President Barack Obama) preliminarily enjoined the Department from "implementing and enforcing" its overtime regulations "on a nationwide basis."[10] The Department filed an expedited appeal, which is currently pending before the Fifth Circuit. The Business Plaintiffs moved for summary judgment, which the states joined, and Judge Mazzant declined to stay the district proceedings during the pendency of the appeal.[11]

AUGUST 31 DECISION

On August 31, Judge Mazzant granted the Business Plaintiffs' motion for summary judgment, holding that the Department's 2016 overtime regulations are "invalid."[12] The court determined that the Business Plaintiffs had standing to challenge the Department's regulations because "their members would incur significant payroll, accounting, and legal costs to comply."[13] And the Business Plaintiffs' challenge to "the automatic updating mechanism is ripe for review" because "[t]he facts of this case have sufficiently developed to address the legality of the Department's Final Rule."[14]

Turning to the merits, the court concluded that "[t]he Department has exceeded its authority and gone too far" with its 2016 overtime exemption regulations.[15] "Congress defines the ["white collar"] exemption with regard to duties," but the 2016 regulations "more than double[] the previously minimum salary level," which "makes overtime status depend predominantly on a minimum salary level, thereby supplanting an analysis of an employee's job duties."[16] "[T]he Department does not have the authority to use a salary-level test that will effectively eliminate the duties test as prescribed by Section 213(a)(1)."[17]

In a footnote, the court offered the caveat that its "opinion is not making any assessments regarding the general lawfulness of the salary-level test or the Department's authority to implement such a test."[18] Rather, it merely found the salary levels set in the Department's 2016 regulations to be invalid. The court "suggested it would be permissible if the Department adjusted the 2004 salary level for inflation."[19]

IMPLICATIONS

The August 31 decision effectively makes the district court's preliminary injunction permanent, which significantly decreases the business and legal risks to employers who decided not to comply with the Department's 2016 regulations in reliance on the preliminary injunction. The decision also resolves the main issue currently pending before the Fifth Circuit, and the Department has therefore moved to dismiss its appeal of the district court's decision, further decreasing risk to employers.

In July 2017, the Department published a Request for Information ("RFI") in the Federal Register seeking comments regarding the "white-collar" exemption.[20] Comments are due by September 25, 2017 and we are aware of a number of employer groups that plan on submitting comments. The RFI indicates the Department's interest in promulgating new overtime exemption regulations rather than reverting to the prior 2004 regulations or continuing to defend its enjoined 2016 regulations.

Employers should nonetheless give consideration to the possibility of undoing any implemented or announced changes in anticipation of the 2016 regulations. As an initial matter, it may be very difficult to rescind any implemented or announced salary increases from an employee-relations perspective. Employers will also need to make sure that any rollback plans comply with applicable state and local requirements. Certain states have overtime laws, some of which incorporate the FLSA, while others have adopted different salary and exemption requirements.[21] For example, as noted in our prior Client Alert, the New York State Department of Labor substantially increased the salary threshold for the executive and administrative exemptions under state law, which are not affected by the district court's injunction. Moreover, certain states have laws governing changes to pay. For example, California "requires that employers provide notice to employees of their rate(s) of pay, . . . and the basis of wage payment . . . , including any applicable rates for overtime . . . within 7 days of a change if the change is not listed on the employee's pay stub for the following pay period."[22]

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ENDNOTES

[1] 29 U.S.C. § 213(a)(1).

[2] *Nevada* v. *U.S. Dep't of Labor*, No. 16-CV-00731, at 1 (E.D. Tex. Aug. 31, 2017), ECF No. 99.

[3] *Id.* at 2.

[4] Dep't of Labor, Wage & Hour Div., Defining and Delimiting the Exemptions for Executive, Administrative, Professional, Outside Sales and Computer Employees, 81 Fed. Reg. 32,391, 32,392 (May 23, 2016).

[5] *Id.* at 32,393, 32,430.

[6] *Id.* at 32,399.

[7] *Nevada*, No. 16-CV-00731, at 3-4.

[8] Complaint at 2–4, *Nevada* v. *U.S. Dep't of Labor*, No. 16-CV-00731 (E.D. Tex. Sept. 20, 2016), ECF No. 1.

[9] *Nevada*, No. 16-CV-00731, Op. at 3-4.

[10] *Nevada* v. *U.S. Dep't of Labor*, 218 F. Supp. 3d 520, 534 (E.D. Tex. 2016).

[11] *Nevada* v. *U.S. Dep't of Labor*, 227 F. Supp. 3d 696, 697–98 (E.D. Tex. 2017).

[12] *Nevada*, No. 16-CV-00731, Op. at 18.

[13] *Id.* at 5.

[14] *Id.* at 6.

[15] *Id.* at 17.

[16] *Id.* at 15–17.

[17] *Id.* at 14.

[18] *Id.* at 13 n.5.

[19] *Id.* at 16 n.6.

[20] Dep't of Labor, Wage & Hour Div., Request for Information; Defining and Delimiting the Exemptions for Executive, Administrative, Professional, Outside Sales and Computer Employees, 82 Fed. Reg. 34,616 (July 18, 2017).

[21] Ten states and the District of Columbia expressly incorporate FLSA regulations into state law. *See* Alaska Stat. Ann. § 23.10.055(c)(1); D.C. Code Ann. § 32-1004(a)(1); 820 Ill. Comp. Stat. Ann. 105/4a(2)(E); Me. Rev. Stat. tit. 26, § 663(3)(K); Md. Code Regs. 09.12.41.01; *id.* 092.12.41.05; *id.* 09.12.41.17; 454 Mass. Code Regs. 27.03(3); Mo. Ann. Stat. § 290.505; N.J. Admin. Code. § 12:56-7.2; N.Y. Comp. Codes R. & Regs. tit. 12, § 142-2.2; N.C. Gen. Stat. Ann. § 4111.03(D)(3)(d); Ohio Rev. Code Ann. § 4111.03(D)(3)(d). Employers should be mindful that, although these provisions track federal law, states may interpret them in light of the new federal regulations, notwithstanding the preliminary injunction.

[22] State of Cal., Dep't of Indus. Relations, Wage Theft Protection Act of 2011 – Notice to Employees: Frequently Asked Questions, http://www.dir.ca.gov/dlse/FAQs-NoticeToEmployee.html.

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