

The Overtime Exemption for “Administrative” Employees

The Fair Labor Standards Act (the “FLSA”) is the federal law governing employers’ minimum wage and overtime obligations. Under the FLSA, eligible non-exempt employees must be paid overtime premium pay equal to time-and-one-half the employee’s regular rate of pay for all hours worked over 40 in a single workweek. However, the FLSA has several exemptions, including those commonly known as the “white collar” exemptions, for executive, administrative and professional employees.

In practice, applying the white collar exemptions can be difficult for employers, and mistakes can be costly. Due to imprecise standards, the administrative exemption in particular has proven difficult for employers to apply. Moreover, employers have the burden of proving that employees classified as exempt meet the requirements of the administrative exemption. This edition of the *Employment Law Advisor* provides explanation and guidance for employers concerning the administrative exemption so potentially costly mistakes can be avoided.

The Regulations

The FLSA itself does not define and interpret the administrative exemption, therefore employers must look to federal regulations for guidance. Under the regulations, for the administrative exemption to apply the employee must meet two tests:

- ✓ The employee must be paid a predetermined and fixed salary of at least \$455 per week that is not subject to reductions because of variations in the quality or quantity of work performed (the “salary basis test”); and
- ✓ The employee’s job duties must primarily involve administrative duties as defined by the regulations (the “duties test”).

The Salary Basis Test

As with the other white collar exemptions, the employee must regularly receive a predetermined salary that is “not subject to reductions because of variations in the

Employers often find it difficult to interpret and apply the overtime exemption for “administrative” employees. Do you want to:

- ✓ Gain a better understanding of the administrative exemption?
- ✓ Avoid misclassifying employees as exempt from overtime pay?
- ✓ Reduce the risk of employee wage hour litigation?

Read on for details and to learn more about the requirements of the administrative exemption...

quality or quantity of the work performed.” This means that employees classified as exempt must receive their full salary for any week in which they perform work. In other words, in order to maintain exempt status employers cannot deduct amounts from exempt workers’ paychecks. Exceptions to this requirement are limited; generally employers may only make deductions for full-day absences for personal reasons (not disability or illness) and violations of employer safety rules.

However, even if an employee is paid on a salary basis, this does not mean that the employee is exempt from payment of overtime premium pay. The employee must still meet the “duties test” as well.

The Duties Test

In practice, the duties test probably has caused the most difficulty for employers. For example, most employees with the title of “administrative assistant” are not exempt administrative employees. The duties test provides that an exempt administrative employee is one “whose primary duty is the performance of office or non-manual work directly related to the management or general business operations of the employer (or the employer’s customers)” and whose primary duties include the exercise of “discretion and independent judgment with respect to matters of significance.” The imprecise nature of these standards often

makes it difficult for employers to determine whether the employee qualifies for overtime pay.

“Directly Related to Management or General Business Operations”

The regulations say that “performance of work directly related to the management or general business operations of the employer (or the employer’s customers)” means that the employee must perform work related to assisting with the running or servicing of the business (or the customer’s business). The regulations provide examples of functional areas that generally are found to be directly related to management or general business operations, including: tax, finance, accounting, budgeting, auditing, insurance, quality control, purchasing, procurement, advertising, marketing, research, safety and health, personnel management, and human resources. This is simply a listing of functional areas -- not a list of specific exempt jobs. The actual work performed by the employee must be evaluated.

“Discretion and Independent Judgment”

What constitutes “discretion and independent judgment” has been the subject of a great deal of litigation. Generally, the regulations say that exercising “discretion and independent judgment” with respect to matters of significance means that the work involves the comparison and the evaluation of possible courses of conduct, and acting or making a decision after the various possibilities have been considered. The term “matters of significance” refers to the level of importance or consequences of the work performed.

Whether the employee exercises discretion and independent judgment with respect to matters of significance requires an evaluation of the facts and circumstances of each particular case. The decision must be based on the employee’s job function -- not his/her job title. Relevant factors include the employee’s:

- ✓ Authority to formulate, affect, interpret, or implement management policies or operating practices;
- ✓ Carrying out of major assignments in conducting the operations of the business;
- ✓ Performance of work that affects business operations to a substantial degree;
- ✓ Authority to commit the employer in matters that have significant financial impact;
- ✓ Authority to waive or deviate from established policies and procedures without prior approval;
- ✓ Authority to negotiate and bind the company on matters of significance;
- ✓ Involvement in planning long- or short-term business objectives;
- ✓ Investigating and resolving matters of significance on behalf of management; and
- ✓ Representing the company in handling complaints, arbitrating disputes or resolving grievances.

Employees can exercise discretion and independent judgment even if their decisions or recommendations are reviewed at a higher level. For example, policies formulated by a company’s credit manager may be subject to review by higher company officials. However, the exercise of discretion

and independent judgment must involve more than the use of skill in applying well-established techniques and procedures. The regulations make clear that it also does not include clerical or secretarial work, work recording or tabulating data, or work performing mechanical, repetitive, recurrent or routine work.

The following are examples of types of employees found to exercise discretion and independent judgment:

- ✓ Insurance claims adjusters (if their duties include activities such as interviewing insureds and witnesses, inspecting property damage, preparing estimates, making recommendations regarding coverage of claims, and negotiating settlements);
- ✓ Employees in the financial services industry (if their duties include work such as collecting and analyzing information regarding customers’ income, assets, investments, etc; determining which financial products best suit customers’ needs; and advising customers regarding advantages and disadvantages of financial products);
- ✓ An employee who leads a team of other employees assigned to complete major projects for the employer;
- ✓ An executive/administrative assistant to a business owner or senior executive of a large business if such employee, without specific instructions, has been delegated authority regarding matters of significance;
- ✓ Human resources managers who formulate, interpret or implement employment policies;
- ✓ Management consultants who study the operations of a business and propose changes in organization;
- ✓ Purchasing agents with authority to bind the company on significant purchases (even if they must consult with top management when making a purchase commitment); and
- ✓ Employees performing work related to academic operations and functions in an elementary or secondary school system, or institution of higher education, such as department heads, employees with responsibility for administration of academic departments, and academic counselors who assist students with academic problems and advise students concerning degree requirements.

Checklist for Employers

Generally, before classifying an employee as exempt from the FLSA’s overtime

requirement under the administrative exemption, employers should carefully evaluate the particular facts and circumstances using the following checklist:

- ✓ Is the employee paid a predetermined and fixed salary of at least \$455 per week that is not subject to reductions because of variations in the quality or quantity of work performed?
- ✓ Is the employee’s primary duty the performance of office or non-manual work directly related to the management or general business operations of the employer (or the employer’s customers)?
- ✓ Does the employee’s primary duty include the exercise of discretion and independent judgment with respect to matters of significance?

Each of these three questions must be answered in the affirmative before the administrative exemption applies. Where the call is a close one, employers should confer with employment counsel. Note also that a number of states, including, for example, Pennsylvania and California, have wage laws that are more stringent than the FLSA. Employers must be aware that the FLSA does not preempt any such stricter state standards. If a state or local law establishes a higher standard than the provisions of the FLSA, the higher standard applies.

If you have any questions regarding this topic, please call any attorney in our employment law team at 781-622-5930.

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