THE FAIR LABOR STANDARDS ACT AND REVISIONS TO EXEMPT EMPLOYEE SALARY REQUIREMENTS AS THEY MAY AFFECT RELIGIOUS ORGANIZATIONS

By

Stephen L. Knowles and Thomas Cunniff

June 2016

Caution: Nothing in this memorandum constitutes legal advice. Nor is the memorandum intended to be an exhaustive summary of the law. Every employment problem is unique, and it is impossible to cover every factual situation that might arise or every legal principle that might apply in a particular factual situation. Each situation must be carefully analyzed based on its own facts and reviewed with legal counsel as appropriate.

TABLE OF CONTENTS

Executive Summary

I. What Does the FLSA Require?

The FLSA requires a covered employer to pay employees a minimum wage of $7.25 per hour except for employees covered by an exemption (see Point 1.1).

Non-exempt employees are also entitled to time-and-one-half overtime pay for hours worked in excess of 40 in a single workweek (see Point 1.2).

II. When Does the FLSA Apply?

Employees of churches and religious organizations may be covered if either: (1) the organization is covered (enterprise coverage); or (2) the individual employee is covered.

A. An employer is subject to enterprise coverage (meaning all of its employees are covered) if it participates in interstate commerce and has annual business of at least $500,000 (Point 2.1). Most congregations, synods, and similar religious organizations will not be covered under enterprise coverage because they are not engaged in business, but congregations that are running a substantial business (e.g., a catering business) are likely to be covered. Also, camps and other religious organizations that conduct business may be subject to enterprise coverage. In addition, certain employers are covered notwithstanding the $500,000 requirement, including residential care facilities, preschools, and elementary and secondary schools. Thus, schools and colleges are automatically covered (but teachers do not have to satisfy the minimum salary requirement; see Point 4.1 below).

B. Even if a congregation, synod, or other religious organization is not covered under enterprise coverage, an individual employee may still be covered by the FLSA if the employee's job involves interstate commerce (Point 2.2). For example, the FLSA may cover congregational employees who regularly do business across state lines, or synod employees in synods encompassing multiple states who routinely engage in interstate commerce, which includes interstate communications.

C. The FLSA applies only to employees, not volunteers and independent contractors (Point 2.3).

In summary:

- Schools (including preschools) are automatically covered (although the minimum salary requirement does not apply to teachers—see Point 4.1 below);

- Most congregations and synods are not entirely covered unless they are conducting a business, but;

- Employees of congregations and synods who regularly engage in interstate commerce or communications are likely covered—synods that cover multiple states and congregations near state lines are particularly vulnerable;

- Camps and other ministry organizations that conduct business activities are likely covered.

III. Does the Ministerial Exception Apply to the FLSA?

It is likely, but not certain, that ministerial employees are exempt from the FLSA. Ministerial employees are typically those involved in worship or the transmission of the faith, such as clergy, Christian education directors, and music directors. Point 3 summarizes the basis and scope of the ministerial exception. Note, however, that the ministerial exception would not apply to employees whose duties are not related to worship or transmission of the faith, such as sextons, receptionists, and groundskeepers.

IV. What Employees Are Exempt From the FLSA's Minimum Wage and Overtime Requirements?

Certain employees are exempt from the FLSA's minimum wage and overtime requirements if: (1) they make a certain salary; and (2) their primary duty is the performance of exempt work.

A. For an exemption to apply, the employee must be paid on a "salary basis" in accordance with the rules summarized in Point 4.1. The minimum annual salary is currently $23,660, but this minimum will increase to $47,476 per year effective December 1, 2016. The new minimum will be adjusted every three years beginning January 1, 2020. Teachers do not have to satisfy the salary requirement.

B. In addition, for the exemption to apply, the employee's "primary duty" must be the performance of exempt work in accordance with the rules reviewed in Point 4.2. Exempt work is performed by an executive employee (Point 4.2.1), an administrative employee (Point 4.2.2), or a professional employee (Point 4.2.3).

V. What Are the Major Implications of the Proposed Changes?

Although the increase in the minimum annual salary for exempt status to $47,476 will likely not affect most congregations, it will likely have significant budgetary and managerial implications for those congregations, synods, camps, and other ministries that are affected. Exempt employees will lose their exempt status if the minimum salary is not paid and will become eligible for overtime compensation. Employers will have to track their employees' hours carefully to make sure they are not working overtime or, if they are, that they receive proper compensation. In addition, the Department of Labor has solicited comments regarding possible revisions to the current duties tests, suggesting that exempt status may be more difficult to achieve in the future.

While the potential liability issues under the FLSA are not discussed further below, they merit a brief mention here. It is important to understand that it takes only one disgruntled employee to initiate a collective or class action on behalf of other employees or a governmental audit of an employer's pay classifications. Employees improperly classified as exempt from the FLSA's overtime requirements are entitled to backpay of time-and-one-half overtime for all hours worked over 40 in a single workweek for a period of up to three years. Additional penalties for the employer would include liquidated damages—the amount of backpay doubled—and attorneys' fees and court costs. FLSA claims are likely not covered by employment practices liability insurance and may also result in personal liability on the part of owners and managers.

THE FAIR LABOR STANDARDS ACT AND REVISIONS TO EXEMPT EMPLOYEE SALARY REQUIREMENTS AS THEY MAY AFFECT RELIGIOUS ORGANIZATIONS

By

Stephen L. Knowles and Thomas Cunniff[1]

On May 18, 2016, the U.S. Department of Labor issued its Final Rule making significant revisions to the salary levels necessary for the executive, administrative, and professional exemptions of the Fair Labor Standards Act ("FLSA" or "Act"). Because the previous sentence may mean nothing to the average church leader or administrator, this memorandum is intended to serve as a primer about the FLSA and the revisions made, which take effect December 1, 2016.

1. What Does the FLSA Require?

The FLSA was enacted in 1938 to guarantee American workers a minimum wage and to limit the number of hours employees could work without being paid additional compensation. The FLSA also imposes restrictions on child labor and requires equal pay for men and women performing equivalent work. This memorandum focuses on the minimum wage and overtime requirements of the Act and the circumstances under which employees are exempt from these requirements.

1.1. Minimum Wage

Under Section 6(a)(1)(C) of the Act, 29 U.S.C. § 206(a)(1)(C), the federal minimum wage is currently $7.25 per hour. Several states and municipalities have adopted higher minimum wages for workers in their jurisdictions. Discussion of such higher minimum wages is beyond the scope of this memorandum.

1.2. Overtime

Calculation Based on the "Workweek"

Section 7(a)(1)(C) of the Act, 29 U.S.C. § 207(a)(1)(C), requires that covered employees be paid at least one and one-half times their regular rate of pay for each hour worked over 40 in a single workweek. A "workweek" is "a fixed and regularly recurring period of 168 hours—seven consecutive 24-hour periods." 29 C.F.R. § 778.105. The workweek often coincides with the calendar week, but does not need to do so. The workweek may begin on any day at any hour and end 168 hours later.

---

[1]Mr. Knowles is the attorney for the Greater Milwaukee Synod of the Evangelical Lutheran Church in America and also acts as counsel to the ELCA's churchwide organization on employment law issues. Mr. Cunniff is Associate General Counsel of the ELCA's churchwide organization.

The following simple example illustrates the time and one-half overtime requirement. An employee whose wage is $10 per hour must be paid $550 for a 50-hour week [($10 x 40 hours = $400) + ($10 x 1.5 x 10 hours = $150)]. Note that the overtime requirement applies only when the hours worked during the week exceed 40. An employee who works 10-hour days from Monday through Thursday and is off for the rest of the week is not due overtime.

For overtime calculations, each workweek must be considered by itself. The Act does not permit workweeks to be averaged over two or more weeks. 29 C.F.R. § 778.104. An employee who works 50 hours during one workweek and 30 hours during the following workweek is entitled to time and one-half overtime for the first week even though the average was 40 hours for the two-week period.

The "Regular Rate"

Overtime is calculated based on the employee's "regular rate," which is always an hourly rate. When an employee's compensation is an hourly wage, the regular rate would normally be the hourly wage. When compensation is described in terms of a salary, the salary must be converted to an hourly rate.

An initial question in this context is whether the salaried employee is "exempt" from the overtime requirements of the Act. As discussed in Points 4.1 and 4.2 below, employees are exempt from being paid overtime if the terms of their employment meet certain tests, including being paid on "a salary basis." Being paid on a salary basis is not the same as being paid a salary, however. The common use of the phrase "salaried employee" to describe an employee who is exempt from the FLSA's overtime requirements is at best misleading and at worst dangerous. An employer is required to pay time and one-half overtime to a salaried employee unless the employee meets the requirements of one of the Act's exemptions. The correct references are therefore to "exempt" and "non-exempt" employees, the terms that are used consistently below.

If a non-exempt employee is paid a salary, the first step for determining overtime liability is to calculate the salary that would be paid on a weekly basis. A monthly salary would be multiplied by 12 and the product divided by 52 to determine the weekly salary. (Another method is to multiply the monthly salary by 0.2308). A semi-monthly salary would be multiplied by 24 and divided by 52 to determine the weekly salary. (Another method would be to multiply the semi-monthly salary by 0.4615.) An annual salary would be converted to its weekly equivalent by dividing by 52. Once the weekly salary is determined, the amount is divided by the number of hours worked that week to obtain the regular rate.

For example, suppose a non-exempt administrative assistant is paid a salary of $52,000 per year. That salary would be converted to a weekly wage of $1,000 by

dividing it by 52. If the employee worked 50 hours in a particular workweek, his or her regular rate for that week would be $20.00 [$1,000 ÷ 50 hours = $20.00]. The employee's proper compensation for that week would be $1,100.00 [($20.00 x 40 hours = $800.00) + ($20.00 x 1.5 x 10 hours = $300.00)].

The foregoing intentionally simple examples are intended only to illustrate the process necessary to determine overtime compensation based on the regular rate. No attempt is made here to illustrate the impact of other types of compensation that could affect the regular rate in a particular workweek, such as non-discretionary bonuses, commissions, or premium pay. Most church-related employers are not likely to provide such additional forms of compensation in any event. The essential point here is that the FLSA, if it applies, requires the payment of time and one-half overtime pay to non-exempt employees who work more than 40 hours in a single workweek.

Comp Time

Sometimes employers grant compensatory time off—"comp time"—in lieu of overtime. A comp time plan in the private sector is permissible only under the following conditions: (i) the employees affected must be paid at a fixed hourly rate or at a regular salary for a fixed number of hours; (ii) the pay period must be longer than a week (biweekly, semi-monthly, or monthly); (iii) time off adjustments must be made within the same pay period; and (iv) comp time must be computed on a time and one-half basis unless taken in the same workweek. Dep't of Labor ("DOL") Op. Ltr. (Sept. 1, 1965), *reprinted in* Wages-Hours 61–66 CCH-WH ¶ 30,996.17. In other words, an employer may give a non-exempt employee who has worked 40 hours as of noon on Friday the afternoon off to avoid overtime liability. A non-exempt employee who has worked 45 hours in the first week of a two-week pay period would have to be given 7½ hours off during the second week.

2. When Does the FLSA Apply?

This question might have been considered first. It is presented second here because we wanted the reader to have a basic understanding of what the FLSA requires if it does apply. Further, even if the Act does not apply to a particular employer, the employer may be subject to a state law or municipal ordinance that imposes similar requirements.

As explained below, employees of churches and religious organizations may be covered if either: (1) the entire organization is covered (enterprise coverage); **or** (2) the individual employee is covered even if the enterprise as a whole is not covered.

2.1. Enterprise Coverage

In 1961 and 1966, the FLSA was amended to extend coverage to all employees of an "[e]nterprise engaged in commerce or in the production of goods for commerce." An "enterprise" is defined generally to include "the related activities performed (either through unified operation or common control) by a person or persons for a common business purpose . . . ." 29 U.S.C. § 203(r)(1). All employees of an enterprise are covered by the Act if two conditions are met:

- The enterprise "has employees engaged in commerce or in the production of goods for commerce, or . . . handling, selling, or otherwise working on goods or materials that have been moved in or produced for commerce by any person;" and

- The enterprise has "an annual gross volume of sales made or business done [of] not less than $500,000 . . . ."

Id. § 203(s)(1).

However, the following employers are considered enterprises for purposes of the Act even if the $500,000 requirement is not met:

- Federal, state, or local governmental agencies;

- Hospitals;

- Residential care facilities primarily caring for sick, aged, mentally ill, or developmentally disabled individuals;

- Schools for mentally or physically handicapped or gifted children; and

- *Preschools, elementary and secondary schools, and colleges and universities*.

Id. §§ 203(r)(1)(2), (s)(1) (emphasis added); *see also Dole v. Shenandoah Baptist Church*, 899 F.2d 1389 (4th Cir. 1990). The activities of the above-listed employers are deemed to be for a business purpose even if the employer is a public or non-profit entity. *Thus, all schools are automatically covered under enterprise coverage, meaning that all their employees are covered unless exempt (see Point 4.1 below regarding teachers).*

Putting aside organizations that are automatically included, however, enterprise coverage under the FLSA is intended to apply to business and commercial activities. Enterprise coverage "does not apply to a private, non-profit enterprise where the eleemosynary, religious or educational activities of the non-profit enterprise are not

in substantial competition with other businesses . . . ." DOL Op. Ltr. FLSA2005-12NA (Sept. 23, 2005). *As a result, most congregations, synods, and other religious organizations will likely not be subject to enterprise coverage (but see Point 2.2 on individual coverage).*[2]

But when "eleemosynary, religious, or education organization[s] . . . . engage in ordinary commercial activities, such as operating a printing and publishing plant, the business activities will be treated under the Act the same as when they are performed by the ordinary business enterprise." 29 C.F.R. § 779.214. Thus, the Supreme Court held that a non-profit religious foundation that ran businesses staffed by recovering drug addicts, derelicts, and criminals was an enterprise obligated to pay its employees minimum wages and overtime pay. *Tony & Susan Alamo Foundation v. Secretary of Labor,* 471 U.S. 290 (1985). Applying this rule, religious organizations that provide services for a fee (e.g., camps[3] and retreat centers) may be covered if their annual sales volume exceeds $500,000.

Not every quasi-commercial activity will be considered to be performed for a business purpose. In *Locke v. St. Augustine's Episcopal Church*, 690 F. Supp. 2d 77, 86–88 (E.D.N.Y. 2010), the defendant congregation's occasional rental of certain real property for social events and its rental of a two-bedroom apartment to the plaintiff custodian was held not to constitute commercial activity, especially since the custodian had been permitted to live in the apartment rent-free for a four-year period. In *Walker v. Interfaith Nutrition Network*, 2015 WL 4276174, at *3–4 (E.D.N.Y. July 14, 2015), the allegation that the defendant rented apartments as a commercial activity was not supported by sufficient factual allegations to plausibly support the conclusion that the defendant was engaged in a commercial enterprise rather than a charitable activity. The court therefore rejected the claim for enterprise coverage under the FLSA.

In summary, while schools are automatically subject to enterprise coverage, most churches and religious organizations will not be subject to enterprise coverage

---

[2]If a congregation operates a preschool, the preschool would be an enterprise covered by the FLSA without regard to the $500,000 requirement even if the preschool is not separately incorporated. Thus, preschool employees would be subject to the requirements of the Act. 29 U.S.C. §§ 203(r)(1) & (s)(1)(B). Such enterprise coverage should not apply to other employees of the congregation. But, as discussed in Point 2.2, other employees of the congregation could be subject to individual coverage.

[3]There is a separate exemption for seasonal camps and other recreational establishments that applies if the camp does not operate for more than seven months in any calendar year or its average receipts for any six months of the preceding year were not more than one-third of its average receipts for the other six months of the year. 29 U.S.C. § 213(a)(3). A detailed discussion of this exemption is beyond the scope of this memorandum.

unless they do more than $500,000 in commercial business per year. Their employees still may be covered on an individual basis, however.

2.2. Individual Coverage

2.2.1. General Rule

Even if the employer is not subject to enterprise coverage, employees may still be covered individually. *See Zorich v. Long Beach Fire Dep't & Ambulance Service*, 118 F.3d 682 (9th Cir. 1997). Individual coverage has been part of the Act since its adoption in 1938. The concept is that the Act covers an individual employee engaged in commerce, the production of goods for commerce, or in an activity closely related to or directly essential to the production of goods for commerce. "Commerce" means "trade, commerce, transportation, transmission, or communication among the several States of between any State and any place outside thereof." 29 U.S.C. § 203(b). In other words, the Act's individual coverage is premised on an individual employee's involvement in interstate commerce. Each individual's coverage must be analyzed on a case-by-case basis.

Minimal involvement in interstate commerce may be sufficient to support individual coverage. Congress "made no distinction as to the volume or amount of shipments in the commerce or of production for commerce by any particular shipper or producer." *United States v. Darby*, 312 U.S. 100, 123 (1941). According to the Department of Labor:

> Although employees doing work in connection with mere isolated, sporadic, or occasional shipments in commerce of insubstantial amounts of goods will not be considered covered by virtue of that fact alone, the law is settled that every employee whose engagement in activities in commerce or in the production of goods for commerce, even though small in amount, is regular and recurring, is covered by the Act.

29 C.F.R. § 776.3.

The term "commerce" is broadly defined for purposes of the Act's individual coverage. Employees are engaged in commerce if their work involves "the movement of persons or things (whether tangibles or intangibles, and including information and intelligence) . . . ." *Id.* § 776.9. The regulation further states: "Also, since 'commerce' as used in the Act includes not only "transmission" of communications but 'communication' itself, employees whose work involves the continued use of the interstate mails, telegraph, telephone or similar instrumentalities for communication across State lines are covered by the Act." *Id.* § 776.10(b) As noted by the Department of Labor, "Examples of . . . interstate

commerce activities include making/receiving interstate telephone calls, shipping materials to another state, and transporting persons or property to another state." DOL Op. Letter FLSA2008-8 (Sept. 29, 2008).

The applicable regulation, 29 C.F.R. § 776.10(b), states in effect that not every use of the mail or other communications channels is enough to establish coverage. The regulation then adds, however:

> But if the employee, as a regular and recurrent part of his duties, uses such instrumentalities in obtaining or communicating information or in sending or receiving written reports or messages, or orders for goods or services, or plans or other documents across State lines, he comes within the scope of the Act as an employee directly engaged in the work of "communication" between the State and places outside the State.

2.2.2. DOL Guidance on Employees of Churches and Religious Organizations

Churches and other religious organizations are not automatically exempt from the FLSA's requirements. The FLSA may apply to the work of an individual employee engaged in interstate commerce even if the employer is not a commercial enterprise. The Department of Labor's guidance on individual coverage puts the onus on the employer to determine when an individual is covered and reiterates that each factual situation is unique.

With respect to individual coverage generally, the Department states, "As a practical matter, the [DOL Wage and Hour Division] does not assert individual coverage over an employee . . . who may on isolated occasions spend an insubstantial amount of time performing individually covered work." DOL Field Operations Handbook § 11a01(a) (1994). Thus, the Department has stated that "individual coverage will not be asserted for employees who *occasionally* devote *insubstantial* amounts of time" to activities like making and receiving interstate telephone calls, sending or receiving interstate mail or electronic communications, and making bookkeeping entries related to interstate commerce. DOL Op. Ltr. FLSA2005-12NA (Sept. 23, 2005) (emphasis added), *citing* Field Operations Handbook § 11a.01(a) (1994). But the Department also cautions that if it is apparent over an extended time period "that the pattern of individual coverage is regular and recurrent, the employee involved is so covered in each workweek in which he does such work, regardless of whether the amount of time spent in this work is substantial or insubstantial." DOL Field Operations Handbook § 11a01(a) (1994).

In a 2005 letter ruling, the Department concluded that the FLSA's individual coverage did not apply to certain church employees because they were not engaged in interstate commerce. DOL Op. Ltr. FLSA2005-12NA (Sept. 23, 2005). The Department further noted that custodians would ordinarily not be covered unless they "clean offices of the church or synagogue where goods are regularly produced for shipment across state lines." *Id.* The Department also stated, however, that "Employees of a church or synagogue are individually covered under the FLSA where they regularly and recurrently use the telephone, telegraph, or the mails for interstate communication or receive, prepare, or send written material across state lines." *Id.*, *quoting* DOL Op. Ltr. (Nov. 4, 1983).

The Department reiterated the foregoing principles in a two-page commentary accompanying the Final Rule entitled "Overtime Final Rule and the Non-Profit Sector." The Department again noted that individual coverage may be based on making or receiving interstate telephone calls, shipping materials to another state, or transporting persons or property to another state. The Department stressed that individual coverage may apply even though the employee is not engaging in the activities for a business purpose. "For example," the Department stated, "If an employee regularly calls an out-of-state store and uses a credit card to purchase for a non-profit that provides free meals for the homeless, that employee is protected by the FLSA, even though the non-profit may not be covered as an enterprise." The Department added, however, that it will not assert individual coverage for "an employee who on isolated occasions spends an insubstantial amount of time performing such work . . . ."

Very recently, in *Walker v. Interfaith Nutrition Network*, 2015 WL 4276174 (E.D.N.Y. July 14, 2015), two maintenance workers sued a nonprofit corporation that operated soup kitchens, emergency shelters, and housing programs. To attempt to establish individual FLSA coverage, they pled that, during their employment, they had used and handled goods and equipment manufactured in other states, routinely made purchases from out-of-state vendors, and routinely made telephone calls to out-of-state companies. These allegations were not sufficient to state a claim upon which relief could be granted and the complaint was dismissed pursuant to Fed. R. Civ. P. 12(b)(6). The court held that handling equipment made in other states did not establish the workers' participation in interstate commerce. The averment on "routine" purchases from out-of-state vendors was not supported by factual allegations sufficient to show the purchases were other than sporadic and occasional. Similarly, insufficient facts were pled to show that the "routine" out-of-state telephone calls constituted regular and recurrent involvement in interstate commerce. 2015 WL 4276175 at *4–5; *see also Locke v. St. Augustine's Episcopal Church*, 600 F. Supp. 2d 77, 82–83, 90–92 (E.D.N.Y. 2010) (rejecting FLSA claims against an Episcopal congregation and its rector brought by the congregation's former custodian).

Based on the foregoing, most employees of most churches will probably not qualify for individual coverage under the FLSA. Most church employees are not engaged in interstate commerce on a regular basis, and the occasional interstate mailing, telephone call, or order of Christian education supplies is likely not sufficient to trigger coverage. The situation may be different for churches that are near state lines with members from more than one state. The employees of such churches may be engaged in interstate commerce (e.g., mailings and telephone calls) on a regular basis. Similarly, synods whose boundaries cross state lines may have employees who are engaged in interstate commerce on a regular basis.

Please note that even if the Department of Labor declines to assert jurisdiction, individual plaintiffs may sue religious organizations. The line between regular and recurrent activities required to support individual coverage as opposed to isolated and insubstantial activities may be difficult to draw. These cases will likely turn on their specific facts, and it is impossible to set forth a general rule that will govern all situations.

2.3. Necessity of an Employment Relationship

The FLSA does not apply unless an employment relationship exists. Therefore, it does not apply to volunteers or independent contractors.

The Act itself does not provide helpful definitions. An "employer" is defined to include "any person acting directly or indirectly in the interest of an employer in relation to an employee . . . ." while "the term 'employee' means any individual employed by an employer." *Id.* §§ 203(d), (e)(1). The Act defines "employ" as "to suffer or permit to work." *Id.* § 203(g).

Volunteers

The Act does state that a volunteer is not an employee, but only in specific contexts. Individuals who perform volunteer work for state or local governments are not employees. *Id.* § 203(e)(4)(A). The same is true for "individuals who volunteer their services solely for humanitarian purposes to private non-profit food banks and who receive from the food banks groceries." *Id.* § 203(e)(5). Significantly, individuals may be considered "volunteers only where their services are offered freely and without pressure or coercion, direct or implied, from an employer." 29 C.F.R. § 553.101(c). Any employer planning to establish that a particular individual is a volunteer rather than an employee should carefully document the relationship to avoid any doubt that the individual's services are offered freely and without coercion. In its commentary on the non-profit sector accompanying the Final Rule, the Department cautioned that employees of a non-profit organization should not, on a voluntary basis, perform for their employer the same type of work they perform as employees.

Independent Contractors

Independent contractors are also not considered to be employees. It bears mention, however, that "misclassification" of employees is a significant area of potential liability in employment law. The misclassification may involve erroneously classifying non-exempt employees as exempt as well as erroneously classifying employees as independent contractors. In the latter context, whether a person is properly classified as an independent contractor or as an employee varies from one body of law to another.

For purposes of the FLSA, courts apply an "economic realities" test. Without attempting an exhaustive review of the economic realities test, we note that a leading treatise lists the following factors as important in determining the nature of the relationship:

- The degree to which the putative employee is independent rather than subject to the control of the putative employer with regard to the manner in which the work is performed.
- Whether the alleged employee has the opportunity for profit or loss in the arrangement.
- The degree to which the alleged employee has invested in the facilities and equipment used in the business.
- The permanency and duration of the relationship between the two parties.
- The degree of skill required to perform the work.
- The extent to which the services performed constitute an integral part of the business for which they are performed.

L. Leader, *Wages and Hours: Law and Practice*, § 201A[1][b] (2015). The overall focus is whether the individual is economically dependent on the "employer" or engaged in his or her own business. While no one factor is determinative, the lack of investment in facilities or equipment and the absence of a realistic opportunity for profit or loss in the arrangement are signs of an employment relationship, especially when there is a high degree of control and the relationship appears to be of indefinite duration.

Many employees are improperly classified as independent contractors. An organization seeking to avoid the FLSA's requirements by labeling an individual as an independent contractor should consider the decision very carefully in consultation with a qualified employment lawyer.

We must also emphasize that the labels used to describe any particular relationship or status are never controlling. The independent contractor label will be summarily rejected if the individual concerned should properly be classified as an employee.

3. Would the Ministerial Exception Insulate an Employer From Liability Under the FLSA?

While the answer is probably yes, at least for ministerial employees, the Supreme Court has not yet ruled on this precise question. In *Hosanna-Tabor Evangelical Lutheran Church and School v. EEOC*, 123 S. Ct. 694 (2012), the Court held that the Free Exercise and Establishment Clauses of the First Amendment bar ministers from asserting claims under the employment discrimination laws against the churches that employ them. 123 S. Ct. at 704–08. An individual does not necessarily have to be ordained to be considered a "minister." Whether an individual is a minister depends on the overall facts and circumstances, including the individual's treatment by the employing church, the individual's education and training, the individual's own characterization of the services provided, and whether the individual's duties reflect a role in carrying out the church's mission and conveying its message. *Id.* at 708–10. Significantly, however, the Court emphasized that its decision focused only on the ministerial exception in the context of claims asserted under the employment discrimination laws. "We express no view," the Court said, "on whether the exception bars other types of suits, including actions by employees alleging breach of contract or tortious conduct by their religious employers." *Id.* at 710.

Other courts addressed the existence of a ministerial exception in the context of the FLSA in cases predating *Hosanna-Tabor*. In *Schleicher v. Salvation Army*, 518 F.3d 472 (7th Cir. 2008), the Seventh Circuit dealt with the claims of a husband and wife who were both commissioned officers in the Salvation Army, a status equivalent to ordination. The Schleichers administered an adult rehabilitation center that, among other things, operated thrift shops staffed by "drunkards, drug addicts and other unfortunates whom the Salvation Army [was] attempting to redeem." 518 F.3d at 476. The thrift shop employees were covered by the FLSA, the court said, but the Schleichers were not. *Id.* at 475–76. Similarly, in *Rosas v. Corp. of the Catholic Archbishop of Seattle*, 627 F.3d 1288 (9th Cir. 2010), the Ninth Circuit rejected the minimum wage claim of a Roman Catholic seminarian, holding that his claim was barred by the ministerial exception.

The proposed application of the ministerial exception to a mashgiach (kosher supervisor)—an inspector appointed by a board of Orthodox rabbis to enforce Jewish dietary laws—has had mixed results. In *Shaliehsabou v. Hebrew Home of Greater Washington, Inc.*, 363 F.3d 299, 307–11 (4th Cir. 2004), a panel of the Fourth Circuit held that the kosher supervisor of a predominantly Jewish nursing home was covered by the ministerial exception and could not assert FLSA claims against his

employer. In *Altman v. Sterling Caterers, Inc.*, 879 F. Supp. 2d 1375, 1383–86 (S.D. Fla. 2012), the court held that the ministerial exception (assuming without conceding its existence in the context of the FLSA) did not apply to a kosher supervisor employed by a commercial caterer.

It must be emphasized that the ministerial exception applies only to employees whose jobs are ministerial in nature, e.g., pastors, Christian education leaders, music directors, and others responsible for worship and Christian education. The ministerial exception would likely not apply to individuals who hold exempt positions but who would not be considered ministers.

4. Exemptions From the FLSA's Minimum Wage and Overtime Requirements

Section 13(a) of the FLSA, 29 U.S.C. § 213(a), exempts certain otherwise-covered employees from the Act's minimum wage and overtime requirements, including "any employee employed in a bona fide executive, administrative, or professional capacity . . . ." These exemptions are often characterized as the "white collar" exemptions. Except as stated below, for an exemption to apply, the employee must satisfy both a "salary basis" requirement and a "duties test."[4]

4.1. Salary Basis Requirement

Minimum Threshold

Currently, the amount of the salary for each of the three white collar exemptions must be at least $455 per week, which is equivalent to $23,660 per year. 29 C.F.R. § 541.600(a). The minimum salary requirement and salary basis requirements do not apply to lawyers, medical doctors, and teachers, however. 29 C.F.R. §§ 541.303–541.304.

The Final Rule requires that, beginning December 1, 2016, exempt employees be paid a salary of at least $913 per week, which is equivalent to $47,476 per year. The

[4]This memorandum does not discuss the exemptions that apply to certain computer employees and to outside sales employees, which are described in 29 C.F.R. § 541.400–541.504. It bears mention, however, that computer employees meeting the primary duty test described in 29 C.F.R. § 541.400(b) may be exempt under current law if paid on a on a salary basis of not less $455 per week or on an hourly basis at a rate of not less than $27.63 per hour. On December 1, 2016, when the Final Rule takes effect, the salary basis requirement changes to $913 per week ($47,476 per year).

Department will adjust that minimum beginning January 1, 2020, and every three years thereafter.[5]

"Salary Basis" Rule and Its Exceptions

The salary payment to an exempt employee must be made "on a salary basis," which means more than simply being paid a salary. For the "salary basis" requirement to be met, the general rule is that the employee must regularly be paid "a predetermined amount constituting all or part of the employee's compensation, which amount is not subject to reduction because of variations in the quality or quantity of the work performed." *Id.* § 541.602(a).[6]

Subject to certain exceptions, discussed below, "an exempt employee must receive the full salary for any week in which the employee performs any work without regard to the number of days or hours worked." *Id.* In other words, an employee is not paid on a salary basis if the employer makes deductions from the salary for absences occasioned by the employer or by the operating requirements of the employer's business. But an exempt employee does not need to be paid for any workweek during which he or she performs no work at all. *Id.*

The exceptions to the foregoing general rule prescribed in 29 C.F.R. § 541.602(b) are briefly summarized as follows:

- An employer may make a deduction from salary if the employee is absent for one or more full days for personal reasons, other than sickness of disability. Note that two full days' worth of salary may be deducted if the employee is absent for two full days for personal reasons. If the absence if for one and one-half days, only one day's worth of salary may be deducted.

- An employer may make a deduction from salary if the employee is absent for one or more full days due to sickness or disability (including work-related accidents) if the deduction is made pursuant to a bona fide plan, policy, or practice of providing compensation for loss of salary due to sickness of disability. The employer is not required to pay the employee's salary for full-day absences for which the employee is compensated under the plan, policy, or practice. Deductions for such full-day absences

---

[5]The $47,476 annual minimum is equivalent to the 40th percentile of the earnings of full-time non-hourly workers in the lowest-wage Census Region of the United States. The triennial adjustments are intended to preserve the 40th percentile equivalency.

[6]The Final Rule allows an employer to apply non-discretionary bonuses, incentives, and commissions to satisfy up 10 percent ($4,747.60) of the minimum salary requirement. Such additional payments must be made at least quarterly, however.

may also be made before the employee has qualified under the plan, policy, or practice and after the employee has exhausted the leave allowance available.

- An employer is not allowed to make deductions from an exempt employee's salary for absences due to jury duty, attendance as a witness at a legal proceeding, or temporary military leave. But the employer is allowed to set off any amounts the employee receives for jury fees, witness fees, or military pay for a particular week against the salary due for that particular week.

- An employer may make a deduction from an exempt employee's pay for a penalty imposed in good faith due to the employee's violation of a safety rule of major significance. Rules prohibiting smoking in oil refineries and coal mines are examples of safety rules of major significance because they are designed to prevent serious danger in the workplace or conditions that would harm other employees.

- An employer may make a deduction from an exempt employee's pay for an unpaid disciplinary suspension of one or more full days imposed in good faith because of the employee's violation of workplace conduct rules, e.g., rules forbidding sexual harassment or workplace violence. The suspension must be imposed pursuant to a written policy affecting all employees.

- An employer is not required to pay a full week's worth of salary during the initial or final week of employment. For example, an employee who starts work on a Tuesday may be paid 80% of a week's salary for the first week of employment, and an employee whose last day of work is a Wednesday may be paid 60% of the normal salary for that last week.

- As also specified in 29 C.F.R. § 825.206, an employer may make deductions for time an employee spends on unpaid leave under the Family and Medical Leave Act, even a partial-day absence. An employee taking a partial-day unpaid absence under the FMLA may be paid only for the hours he or she works without disrupting his or her status as an exempt employee.

The general rule and exceptions described above are important. An employer who makes improper deductions from an exempt employee's salary risks the loss of the exemption because it may appear there was no intent to pay the employee on a salary basis. 29 C.F.R. § 541.603. The loss of the exemption would mean the employee would be owed time-and-one-half overtime pay for every hour worked

over 40 in a single workweek, not to mention the other penalties imposed by the FLSA.

As long as the employee's salary is not docked, it may be appropriate to allow the employee to cover an absence by applying accrued paid time off. The Department of Labor stated in an opinion letter that an employer may reduce an accrued PTO leave bank to cover a partial-day absence:

> To respond to your specific concern about whether or not an exempt employee's accrued PTO leave bank may be reduced for partial day absences, the answer is yes. Where an employer has a benefits plan (e.g., vacation time, sick leave), it is permissible to substitute or reduce the accrued leave in the plan for the time an employee is absent from work, whether the absence is a partial day or a full day, without affecting the salary basis of payment, if the employee nevertheless receives in payment his or her guaranteed salary. Payment of the employee's guaranteed salary must be made, even if an employee has no accrued benefits in the leave plan and the account has a negative balance, where the employee's absence is for less than a full day.

DOL Op. Ltr. on Leave Bank Deductions Under the Salary Basis Test, Jan. 7, 2005, http://www.dol.gov/whd/opinion/FLSA/2005/2005 _01_07_7_ FLSA_PaidTimeOff.pdf.

Certain professionals are considered exempt even if they are not paid on a salary basis. This category is limited to teachers, lawyers, and physicians (including medical doctors, osteopathic physicians, podiatrists, dentists, and optometrists). *Id.* §§ 541.303–541.304. The category does not include physician assistants and nurse practitioners, and by extension, registered nurses. *See Belt v. EmCare, Inc.*, 444 F.3d 403 (5th Cir. 2006).

Highly Compensated Employees

The "highly compensated" category of exempt employees also bears mention. Under 29 C.F.R. § 541.601 as presently in force, an employee who regularly performs one or more of the exempt duties of an executive, administrative, or professional employee will be considered exempt if he or she receives total annual compensation of at least $100,000 per year. The total annual compensation must include at least $455 per week paid on a salary basis. The remaining compensation may include commissions, nondiscretionary bonuses, and other nondiscretionary compensation earned during a 52-week period.

Under the Final Rule, the minimum annual salary threshold for a highly compensated employee increases to $134,004 as of December 1, 2016. This threshold will be subject to adjustment by the Department of Labor every three years beginning January 1, 2020.

4.2. Exempt Duties Requirement

In addition to the salary requirement, in order for an employee to qualify for one of the exemptions, his or her "primary duty" must be the performance of exempt work. *Id.* § 541.700(a).

"Primary duty" is defined as "the principal, main, major or most important duty that the employee performs." *Id.* The determination of a person's primary duty must be made under the facts and circumstances of each case, emphasizing the character of the job as a whole. The relevant factors include:

- The relative importance of the employee's exempt duties in comparison with other types of duties the employee performs;
- The amount of time the employee spends performing exempt work compared to other types of work;
- The degree to which the employee is free from direct supervision;
- The relationships between the salary paid to the employee and the wages paid to other employees for the non-exempt work performed by the employee classified as exempt.

Id.

According to the regulation, the amount of time the employee spends performing exempt work may be a "useful guide" in the determination of whether exempt work constitutes the employee's primary duty. *Id.* § 541.700(b). Thus, an employee who spends more than 50 percent of the workday on exempt duties would, in general, satisfy the primary duty requirement. But time alone is not the sole test, at least under present law. An employee spending less than 50 percent of working time performing exempt duties may nonetheless qualify for the exempt classification if the other factors are present.

Work is considered to be exempt work if it is directly and closely related to the performance of exempt duties. "Directly and closely related" work may include "physical tasks and menial tasks that arise out of exempt duties, and the routine work without which the exempt employee's exempt work cannot be performed properly." Example would include "recordkeeping; monitoring and adjusting machinery; taking notes; using the computer to create documents or presentations;

opening the mail for the purpose of reading it and making decisions; and using a photocopier or fax machine." 29 C.F.R. § 541.703(a).

More than one exemption may apply to a particular employee. For example, a particular employee whose primary duty involves both exempt administrative and exempt executive work would still be considered to be exempt. Work that is exempt under one of the white collar exemptions would not defeat the exempt status of work under one of the other exemptions. *Id.* § 541.708.

4.2.1. Duties Test for Executive Exemption

Under 29 C.F.R. § 541.100, the executive exemption applies to an employee:

- Whose primary duty is the management of the enterprise where the employee works, or the management of a customarily recognized department or subdivision of the enterprise;

- Who customarily and regularly directs the work of two or more other employees; and

- Who is authorized to hire and fire other employees or whose recommendations regarding the hiring, firing, promotion, or other status change for other employees is given particular weight.

To qualify for the executive exemption, the employee must customarily and regularly direct the work of two or more other employees. The phrase "two or more other employees" is intended to mean two full-time employees or their equivalent. *Id.* § 541.104(a)–(b). The hours worked by a supervised employee cannot be credited more than once to different executives. Therefore, if two managers share the responsibility for supervising the same two employees in the same department, the executive exemption does not apply. But a full-time employee who works four hours per day for one supervisor and four hours per day for a different supervisor is considered a half-time employee for each of the supervisors. *Id.* § 541.104(d).

The distinction between assistant manager and an assistant to the manager is potentially important. An assistant manager whose primary duty is the performance of exempt work may qualify for the executive exemption even if some of the assistant manager's working time is spent on non-exempt duties. In contrast, an employee who works as an assistant to the manager of a particular department and who supervises two or more employees in the department only when the manager is absent does not qualify as an executive employee. *Id.* § 541.104(c).

4.2.2. Duties Test for Administrative Exemption

Under 29 C.F.R. § 541.200, the administrative exemption applies to an employee:

- Whose primary duty is the performance of office or non-manual work directly related directly related to the management or general business operations of the employer or the employer's customers; and

- Whose primary duty includes the exercise of discretion and independent judgment with respect to matters of significance.

The first of the two duties requirements for the administrative exemption is that the employee's primary duty must be to perform work directly related to the management or general business operations of the employer or the employer's customers. Under 29 C.F.R. § 541.201(a), the phrase "directly related to the management or general business operations" relates to assisting with the running of the business, as opposed to working on a production line or selling products. Examples may include work in tax, finance, accounting, quality control, human resources, public relations, Internet and database administration, and legal and regulatory compliance. *Id.* § 541.201(b). An employee whose primary duty is the performance of work directly related to the management or general business operations of the employer's customers may also qualify for the administrative exemption, e.g., an employee working as a tax expert or financial consultant for customers. *Id.* § 541.201(c).

The second duties requirement for the administrative exemption is that the employee's primary duty "must include the exercise of discretion and independent judgment with respect to matters of significance." *Id.* § 541.202(a). The term "matters of significance" relates to "the level of importance or consequence of the work performed." *Id.*

The exercise of independent judgment suggests that the employee is authorized to make an independent choice without immediate direction or supervision. Such choices may be subject to further review, however. The exercise of discretion and independent judgment does not require unlimited authority and the total absence of further review. *Id.* § 541.202(c).

As is usually the case in employment law, application of the phrase "discretion and independent judgment with respect to matters of significance" depends on the overall facts and circumstances. Section 541.202(b) specifies the following factors as relevant:

- Whether the employee is authorized to formulate, affect, interpret, or implement management policies or operating practices;

- Whether the employee carries out major assignments in conducting the operations of the business;

- Whether the employee performs work that affects business operations to a substantial degree even if the assignments relate only to operations of a particular segment of the business;

- Whether the employee is authorized to commit the employer in matters having a significant financial impact;

- Whether the employee is authorized to waive or deviate from established policies and procedures without prior approval;

- Whether the employee is authorized to negotiate and bind the employer on significant matters;

- Whether the employee provides consultation or expert advice to management;

- Whether the employee is involved in planning long-term or short-term business objectives;

- Whether the employee investigates and resolves matters of significance on behalf of management; and

- Whether the employee represents the employer in handling complaints, arbitrating disputes, or resolving grievances.

Significantly, the exercise of discretion and independent judgment must involve more than the skillful application of established techniques, procedures, or standards. Nor does the exercise of discretion and independent judgment include clerical or secretarial work, recording or tabulating data, or performing other repetitive, recurrent, or routine work. 29 C.F.R. § 541.202(e). Similarly, the potential for a large financial loss if the job is not done properly does not mean the employee is exercising discretion and independent judgment with respect to matters of significance. For example, the fact that a mistake in the operation of expensive equipment would cause financial loss to the employer does not mean that the operator exercises discretion and independent judgment. *Id.* § 541.202(f).

4.2.3. Duties Test for Professional Exemption

In general, the professional exemption applies to employees whose primary duty is the performance of work requiring knowledge of an advanced type in a field of science or learning customarily acquired by a prolonged course of specialized intellectual instruction or requiring invention, imagination, originality, or talent in a recognized field of artistic or creative endeavor. 29 C.F.R. § 541.300(a). The

regulations address three types of professionals: learned professionals, creative professionals, and teachers.

The professional exemption applies to an employee whose primary duty satisfies the following three tests:

- The employee must be engaged in the performance of work requiring advanced knowledge, i.e., work that is primarily intellectual in nature and that involves the consistent exercise of discretion and judgment.

- The advanced knowledge must be in a field of science or learning, including law, medicine, theology, accounting, actuarial computation, engineering, architecture, teaching, the various types of sciences, pharmacy, and other occupations that have a recognized professional status as opposed to the mechanical arts or skilled trades.

- The advanced knowledge must be customarily acquired by a prolonged course of specialized intellectual instruction, i.e., where specialized academic training and possession of an academic degree are normally prerequisites to performing the work.

Id. § 541.301(a)–(d).

The creative professional exemption applies to an employee whose primary duty is the performance of work requiring invention, imagination, originality, or talent in a recognized field of artistic or creative endeavor. A "recognized field of artistic or creative endeavor" includes fields like music, writing, acting, and the graphic arts. The distinguishing feature of the creative professions is the requirement of "invention, imagination, originality, or talent," which are different concepts than requirements like intelligence, diligence, and accuracy that may be associated with other jobs. Examples of employees covered by the creative professional exemption include actors, musicians, composers, conductors, and soloists. *Id.* § 541.302(a)–(c).

The professional exemption also covers teachers, i.e., "any employee with a primary duty of teaching, tutoring, instructing or lecturing in the activity of imparting knowledge and who is employed and engaged in this activity as a teacher in an educational establishment by which the employee is employed." *Id.* § 541.303(a). An "educational establishment" includes elementary and secondary schools, colleges and universities, and other educational institutions recognized under state law, such as special schools for gifted or disabled children and nursery school programs. *Id.* §§ 541.303(a), 541.204(b).

The minimum salary requirement and the salary basis requirement do not apply to the professional teachers exemption. *Id.* § 541.303(d).

5. Implications for the Future

The required minimum salary for an exempt employee will increase significantly. Under current law, an employee making $23,660 per year who meets the appropriate duties test would be exempt and not entitled to overtime. When the Final Rule takes effect on December 1, 2016, the required minimum annual salary will be $47,476. This required minimum could be potentially devastating for a small non-profit organization covered by the FLSA.

Important Questions to Think About Now

While the Final Rule does not take effect until December 1, 2016, there are important questions that religious organizations must consider now.

The first and overriding question is whether the FLSA might apply to an enterprise operated by the organization or to certain employees of the organization.

Assuming the answer to the first question is affirmative, then the organization must decide whether there are any exempt employees who are currently paid less than $47,476 annually. If so, the following questions should be considered:

- Should the organization give a raise to an employee who is just under the new threshold? If so, how would this affect the salaries of higher-level employees?

- Should an employee reclassified from exempt to non-exempt status be paid an hourly wage or continue to be paid a salary? Remember that the salary of a non-exempt employee must be converted to a "regular rate" (which is always an hourly rate) for overtime calculations (see Point 1.2).

- If an employee who used to be exempt but is now non-exempt regularly works more than 40 hours per week, should the employer lower "base" pay to allow for overtime and keep total pay approximately the same?

- Will the employer prohibit or restrict overtime work by formerly exempt employees?

- Would a reorganization or redistribution of work help to reduce the number of overtime hours worked by previously exempt employees?

- Is there a system in place to track all hours worked by formerly exempt employees?

The last point above may be particularly challenging. Non-exempt employees are required to keep track of their hours worked. Many tasks that exempt employees

perform during evenings and on weekends without separate compensation—dealing with emails is a good example—are compensable when performed by non-exempt employees. An organization that allows employees to work from home should take the steps necessary to ensure that all working hours are recorded so non-exempt employees are properly compensated.

Religious organizations should determine whether they are or may be subject to the FLSA (or a similar state law), and, if so, whether they are in compliance with the applicable requirements, especially the requirements dealing with the exempt status of their employees. Such a determination means a careful consideration of not only what job descriptions say, but also what employees actually must do to accomplish their jobs. Moreover, even if exempt employees are paid in accordance with the minimum salary threshold now in effect, an organization will need to determine whether it can afford to pay the additional amount necessary to preserve exempt status and, if not, how it will implement the recordkeeping requirements necessary for non-exempt employees. All of these issues should be reviewed with the organization's own legal counsel.

Possible Additional Questions for the Future

It is also significant that the Department of Labor's Notice of Proposed Rulemaking issued in July 2016 and preceding the Final Rule solicited comments regarding possible revisions to the duties tests for the white collar exemptions. For example, the Department solicited comments on the following questions:

- What, if any, changes should be made to the duties tests?
- Should employees be required to spend a minimum amount of time performing work that is their primary duty in order to qualify for exemption? If so, what should that minimum amount be?
- Should the Department look to the State of California's law (requiring that 50 percent of an employee's time be spent exclusively on work that is the employee's primary duty) as a model? Is some other threshold that is less than 50 percent of an employee's time worked a better indicator of the realities of the workplace today?

Defining and Delimiting the Exemptions for Executive, Administrative, Professional, Outside Sales and Computer Employees, 80 Fed. Reg. 38516, 38543 (July 6, 2015).

While the Department did not propose any changes to the duties tests, it seems apparent that such changes may be considered and that achieving exempt status may become more difficult in the future.