Statement
On behalf of the
National Restaurant Association
&
Besh Restaurant Group

ON: AN EXAMINATION OF THE ADMINISTRATION'S OVERTIME RULE AND THE RISING COSTS OF DOING BUSINESS

TO: U.S. SENATE COMMITTEE ON SMALL BUSINESS AND ENTREPRENEURSHIP

BY: OCTAVIO MANTILLA, CO-OWNER, BESH RESTAURANT GROUP

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By: Mr. Octavio Mantilla

On Behalf of the National Restaurant Association & the Besh Restaurant Group

Senate Committee on Small Business and Entrepreneurship
428A Russell Senate Office Building
Washington, DC 20510

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Good Morning Chairman Vitter, Ranking Member Shaheen, and distinguished members of the Committee. Thank you for the opportunity to testify today on the impact that the proposed overtime regulations would have on restaurants like mine and the concerns we have with some of the ideas floated by the Department of Labor ("Department") for the final regulation.

My name is Octavio Mantilla and I am a Co-Owner of the Besh Restaurant Group. I'm honored to share the perspective of my company and the National Restaurant Association.

Today, my testimony will focus on some of the issues that my company and the industry have been struggling with in preparing for potential changes to the current overtime regulations. At the end of the day, I need to ensure that Besh Restaurant Group is fully compliant with the law, while remaining economically healthy and vibrant. Some of the issues I would like to address today include:

1. The adjustments to the duties test being considered;
2. The proposed salary level; and,
3. The proposed automatic increases.

I would also like to point out that the overall overtime regulatory proposal is adding to the tremendous amount of uncertainty created by the level of federal regulations from the last five years.

Besh Restaurant Group

I was born in Nicaragua and moved to New Orleans as a child. At sixteen, I got my first job in a restaurant as a dishwasher and later waiting tables. I continued to work my way up and eventually moved through all managerial levels.

While working in the industry, I earned a bachelor's degree from Tulane University and an MBA from the University of New Orleans. I would not have been able to achieve these

milestones without the flexibility that being a manager provided me. As a manager, while making less than many waiters, I had more flexibility to manage my work schedule and attend classes. I could not take a six hour or eight hour shift and go to school, as required from full-time hourly employees. The flexibility of being on salary was a big help to me. I would not be where I am today without that opportunity.

After graduating, I helped open Harrah's Casino & Hotel in New Orleans and then worked in St. Louis as Harrah's Director of Food Operations. I have opened numerous fine dining restaurants for Harrah's nationwide. My story is repeated in our industry over and over. In fact, nine in ten restaurant managers started in entry-level positions and eight in ten restaurant owners also began in our industry with an entry-level position. Doing away with the flexibility entry-level salaried managers have to, among other things, go back-and-forth from work to school would diminish professional growth opportunities in our industry.

I returned to New Orleans to be reunited with my old friend Chef John Besh at Besh Steakhouse at Harrah's. John and I became partners in the Besh Restaurant Group, combining his vast experience in restaurant operations with my passion for customer service. Since becoming John's partner, the Besh Restaurant Group has expanded to include the restaurants of La Provence, Lüke New Orleans, Domenica, Lüke San Antonio, Borgne, Pizza Domenica, Johnny Sanchez Baltimore, Johnny Sanchez New Orleans, Shaya and Willa Jean.

Earlier this year, the Besh Restaurant Group acquired a space in New Orleans to house a new private events venue, dubbed Pigeon & Prince. Executive Chef Erick Loos of La Provence is helming the culinary development for the space.

The Restaurant and Foodservice Industry

The National Restaurant Association is the leading trade association for the restaurant and foodservice industry. Its mission is to help members like me establish customer loyalty, build rewarding careers, and achieve financial success. The industry is comprised of one million restaurant and foodservice outlets employing over 14 million people. Restaurants are job-creators.

While small businesses comprise the majority of restaurants—more than nine in ten restaurants have fewer than 50 employees—the industry as a whole is the nation's second-largest private-sector employer, employing about ten percent of the U.S. workforce. In addition, more than seven out of ten eating and drinking establishments are single-unit operators. However, the restaurant business model produces relatively low profit margins of only four to six percent before taxes, with labor costs being one of the most significant line items for a restaurant. The restaurant industry is highly labor-intensive and combined with the low profit margins it creates low profits per employee.

Adjustments to the duties test are not necessary and should be avoided.

It is clear to operators in the industry that any reduction in litigation that the Department seeks to obtain with the proposed rule's increase in the salary threshold would be lost if the

changes being considered to the duties test became final. In particular, the industry is extremely troubled by the notion that the Department is looking at California's over-50% quantitative requirement, also known as a "long" duties test structure, for an exempt employee's primary duty.

A long duties test would mandate a percentage limitation on non-exempt work that a manager can perform. The problems with the long duties test structure are well known and also acknowledged by the Department of Labor in the 2004 Overtime Rule. In 2004, the Department stated that the strict percentage limitations on nonexempt work in the long duties test would impose significant monitoring requirements and recordkeeping burdens. It also acknowledged that employers would have to conduct a detailed analysis of the substance of each particular employee's daily and weekly tasks in order to determine if the exemption applied. Finally, distinguishing which specific activities are inherently a part of an employee's exempt work has proven to be a subjective and difficult evaluative task that is prompting contentious disputes and increased litigation in California.

If the Department of Labor now decides to enact changes to the duties test based only on answers to the general questions asked in the proposed regulation, rather than on the basis of comments on any specific proposal, the requirements of the Administrative Procedure Act ("APA"), the Regulatory Flexibility Act, and the various Executive Orders related to regulatory activity would not have been followed. I should not be expected to know how labor law works in California. The Department should not seek input based on hypotheticals and, instead, should explain in an actual regulatory proposal that the regulated community can consider, evaluate, and comment upon. Adding new major regulatory text to a final regulation with no opportunity to see it beforehand directly contradicts the goal of the APA.

Moreover, the Department optimized the duties test in 2004 to reflect the realities of the modern economy, a move that recognized the unique roles and responsibilities restaurant managers have. In our industry, managers need to have a "hands-on" approach to ensure that operations run smoothly. Any attempt to artificially cap the amount of time exempt employees can spend on nonexempt work would place significant administrative burdens on restaurant owners, increase labor costs, cause customer service to suffer and result in an increase in wage-and-hour litigation.

I am also extremely concerned that the Department expresses throughout the proposed regulation its belief that any amount below its proposed salary level would necessitate a more rigorous and restrictive long duties test. The realities associated with a more rigorous and restrictive long duties test exist regardless of the salary level chosen by the Department. Even if the salary level did not increase at all, a more rigorous and restrictive long duties test would still place significant administrative burdens on restaurant owners.

Thus, the Department should leave the concurrent duties rule in place and untouched. The concurrent duties test rule recognizes that front-line managers in restaurants play a multi-faceted role in which they often perform nonexempt tasks at the same time as they carry out their exempt, managerial function. It recognizes that exempt and nonexempt work are not mutually exclusive.

The Department's own Field Operations Handbook highlights that "performing work such as serving customers or cooking food during peak customer periods" does not preclude exempt status. Exempt supervisors make these decisions while remaining responsible for the success or failure of business operations under their management and can both supervise subordinate employees and serve customers at the same time.

The Department's proposed minimum salary level is inadequate for our industry and makes the exemption inoperative in my part of the country.

The Department believes its proposed salary level does not exclude from exemption an unacceptably high number of employees who meet the duties test. However, when applied to my industry, the contrary is true.

Even before adjusting for regional economic and market differences, most managers and crew supervisors in our industry do not meet the proposed salary level of $970 per week. Some of these employees would qualify as exempt under the new proposed salary level only if the Department allowed bonuses to be used to calculate the employee's salary level.

The purpose of setting a salary level, historically, has been to "provid[e] a ready method of screening out the obviously nonexempt employees." In other words, the salary level should be set at a level at which the employees below it would clearly not meet any duties test. With its proposed changes, however, the Department is upending this historic rationale and setting the salary level at a point at which all employees above the line would be exempt. This would greatly limit employers in the restaurant industry from availing themselves of the exemption.

For example, the median annual base salary paid to crew and shift supervisors in our industry is $38,000. Even those in the upper quartile at $47,000 would not qualify as exempt under the Department's proposed $50,440 salary level for 2016. Likewise, the median base salary for restaurant managers is $47,000, while the lower quartile stands at $39,000.

These are employees who would meet the duties test but who would become non-exempt under the proposed salary level. It is clear that, at least in reference to the restaurant industry, the proposed salary level does exclude from exemption an unacceptably high number of employees who meet the duties test. The impact would be magnified in many regions of the country.

In my own region, the proposed minimum salary level of $50,440 per year would represent an outsized income for entry-level managers. These would be the managers entering our Managers Training Program at a salary of about $35,000. Generally, these are employees that are being promoted, while learning how to perform their new duties. The proposed threshold increase (and the lower $47,000 now reported in newspapers) would be too large for us to absorb, so those positions would end up being moved back to an hourly rate, which I can assure you they would all view as a demotion.

While this would be an easy transition to make from a management and bookkeeping standpoint, it does remove the certainty of a fixed paycheck that they currently have. More

problematic is that we use salaried versus non-salaried to set eligibility for extra paid vacation, currently as well as management investment/ownership pool and annual profit-sharing bonuses. Probably the biggest benefit is the flexibility that we are able to extend to our salaried employees, paying full wages while they get to accommodate college schedules—as I once did.

The ability to delineate programs and perks by salaried versus non-salaried has been a great tool for upper management as well as a great benefit for our employees. Setting a minimum rate that is inappropriate for entry-level managers will end up reducing the benefits of our managers, not because we want to, but because of secondary consequences of the proposed changes.

The National Restaurant Association suggested at least three alternatives considered by the Department that would be better options:

1) "Alternative 1" calculated a new salary level by adjusting the 2004 salary level of $455 for inflation from 2004 to 2013, as measured by the CPI–U, and results in a salary level of $561 per week ($29,250 per year).
2) "Alternative 2" used the 2004 method to set the salary level at $577 per week ($30,085 per year).
3) Understanding that the Department now finds the salary level it set in 2004 as too low, the industry is also willing to support "Alternative 3," which would set the salary level at $657 per week ($34,255 per year).

I would like to point out that the Department estimated that 75 percent of newly overtime-protected employees would see no change in compensation and no change in hours worked based on the proposed regulations. However, in the restaurant industry salaried employees enjoy a number of benefits not available to hourly employees, as shown by my own example. Thus, in addition to getting paid a salary regardless of the fact that they may not be working over 40 hours a week, these newly overtime-protected employees could lose flexibility as well as benefits, including substantive bonuses, paid vacation, and flex time.

Finally, throughout the proposed regulation, the Department created the impression that salaried employees feel they are being taken advantage of by virtue of their exempt status. In reality, employees often view reclassifications to non-exempt status as demotions, particularly where other employees within the same restaurant continue to be exempt. Most employees view their exempt status as a symbol of their success within my company. It will be demoralizing for people who are working as entry-level managers and want to continue to move up to now be treated as hourly employees.

Automatic salary level increases will only perpetuate bad policy.

Putting aside legal objections to the Department's attempt to permanently index the salary level, at $47,000 or $50,440, an automatic yearly increase tied to CPI-U would make the exemption perpetually unusable for large portions of our industry.

The Department's other proposed alternative of indexing the salary level to the 40th percentile of non-hourly employees is a non-starter. Preliminary research points to it resulting in a death spiral that would render the exemption obsolete in just a few years. The relevant data used to determine the 40th percentile of full-time salaried workers is found in the Current Population Survey from the Bureau of Labor Statistics (BLS). The data consists of the total weekly earnings for all full-time non-hourly paid employees.

As the new salary level becomes effective, the number of workers who report to the BLS that they are paid on a non-hourly basis will decrease as workers who fail the salary test in year one (and subsequent years) are reclassified as non-exempt. This will result in a dramatic upward skewing of compensation levels for non-hourly employees. If the 40th percentile test is adopted, in the years following the proposal, the salary level required for exempt status would be so high as to effectively eradicate the availability of the exemptions in our industry.

For example, the Department predicts that the initial salary level increase will impact 4.6 million currently exempt workers. Employers must then choose to:

1) Reclassify such workers as nonexempt and convert them to an hourly rate of pay;
2) Reclassify such workers as nonexempt and continue to pay them a salary plus overtime compensation for any overtime hours worked; or,
3) Increase the salaries of such workers to the new salary threshold to maintain their exempt status.

The Department estimates that only 67,000 of currently exempt workers will see an increase in their salaries to bring them up to the new salary threshold in order to maintain their exempt status. The overwhelming majority of affected employees would be reclassified as non-exempt. In our industry, particularly under the proposed $970 per week salary level, most of these employees will be converted to an hourly method of payment.

One economic analysis that the Association was able to review states that if just one quarter of the full-time, non-hourly workers earning less than the proposed 40th percentile were reclassified as hourly workers each year, in five years the new 40th percentile salary level would be $1,393 per week ($72,436 per year). The more likely scenario is that an even greater percentage of employees would be reclassified from salaried to hourly. If just half of full-time, non-hourly employees are converted to hourly positions, the 40th percentile salary level would increase to $1,843 per week ($95,836 per year) by 2020.

In the current proposed rulemaking, the Department proposes to announce a new salary level each year in the Federal Register without notice-and-comment, without a Regulatory Flexibility Act analysis, and without any of the other regulatory requirements established by various Executive Orders.

Conclusion

The Department should have granted at least as much time as it did in 2004 for the regulated community to comment on the proposed regulation, particularly given the proposal's

complexity and unusual new theories and mandates. Above all, the restaurant industry would find the use of a long duties test to be the wrong approach. The Department says it is attempting to "modernize" and "simplify" the applicability of the exemption, but a return to a long duties test would absolutely nullify any efforts to modify and simplify the rules. However, if the Department is inclined to mandate a new duties test, it should comply with all regulatory requirements and allow for notice and comment on any specific new duties test proposal.

In closing, I would like to state that I am not against increasing the salary threshold for exempt status, but it has to be a reasonable level so entry-level managers in my restaurant can still benefit. I am both proud and grateful for the responsibility of serving America's communities—creating jobs, boosting the economy, and serving our customers. My industry is committed to working with Congress to find solutions that foster job growth and truly benefit our communities. It is part of the Besh Restaurant Group's mission "to encourage growth from within and find like-minded partners to take the helm at our restaurants." The proposed overtime regulations may end up making it harder for these like-minded partners to move up in my company.

Thank you again for the opportunity to testify before you today regarding my industry's concerns with the proposed overtime regulations. I look forward to your questions.