Testimony of J. Randall MacDonald

Senior Vice President, Human Resources, IBM Corporation
&
Chairman, HR Policy Association

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Good morning, Chairman Walberg, Ranking Member Woolsey and Members of the Committee. My name is Randy MacDonald, and I am Senior Vice President, Human Resources, of the IBM Corporation. I am privileged to oversee more than 400,000 IBM employees in 170 countries. For a century, my company has pioneered not only science and technology, but also progressive workforce policies, such as flexible work/life balance arrangements and equal opportunity employment, long before it was law. I am proud to say that IBM's practices and innovations are changing the way the world works.

I also represent a broader segment of the U.S. business community as Chairman of the HR Policy Association (HRPA), the lead organization representing more than 325 Chief Human Resource Officers of the largest corporations doing business in the United States and around the world. Collectively, our companies employ more than ten million employees in the United States - nearly nine percent of the private sector workforce, and 20 million employees worldwide.

The Association recently published the *Blueprint for Jobs in the 21st Century*[1]-- that outlines the comprehensive vision of our many top human resource officers about how to restore job growth and competitiveness in the United States through changes in public policy, education, and public perceptions. That vision is directly relevant to the focus of this hearing, and several of its recommendations are included in my testimony. I encourage you to read the document in its entirety.

Introduction

I appreciate the Committee's invitation to discuss before a Committee of the 112th Congress several problems with the Fair Labor Standards Act (FLSA), originally passed in 1938 in the 75th Congress. I look forward to sharing my company's views and the views of the HR Policy Association, as well as those of the broader business community.

I would like to make 3 points today, Mr. Chairman:

1) First, the economy seen by the 112th Congress has changed drastically since 1938 and the economy confronted by the 75th Congress.

2) Second, this economy of the 112th Congress has an entirely new paradigm for how, where and when we work, as well as how professional employees want and expect to be treated.

3) Third, the Fair Labor Standards Act is failing America. It must be modernized, clarified and made relevant for our 21st century business environment and workforce if U.S. companies are to thrive and continue hiring U.S.-based workers.

Let me be clear from the outset. IBM recognizes the importance and role of the Fair Labor Standards Act in our nation's history. We understand that when the Act was

[1] Available at http://www.hrpolicy.org/initiatives_blueprint.aspx

created in 1938, the U.S. workplace was vastly different than it is today. Many employees not only experienced substandard working conditions but also were forced to work long hours for less than adequate wages for the hours they worked - let alone overtime. We appreciate that the Act established some boundaries to protect workers from unscrupulous employers.

However, let me assure you that as a proud American, and as a business leader, there are few issues about which I am more passionate than reform of the FLSA. With more than 40 years as a human resources executive for several leading companies, and having had the benefit of regular contact with peers across a wide range of industry sectors, I speak from experience when I say there are areas of major disconnect between this 70-year-old labor law and today's rapidly changing workplace environment. The business world of 2011 barely resembles that of the 1930's and 1940's, while our primary labor law is becoming ever more outdated, having barely changed in all that time.

Since testifying before this same Committee just over ten years ago, my fellow HR counterparts and I have watched with despair at Congress' inability to make critical fixes to this aging law. If we, as U.S. companies, are to continue hiring and employing the best and brightest workers in this country, it is critical that you, as the lawmakers with the authority to modernize and clarify this law, do so as soon as possible. It's an imperative if companies like mine, which just celebrated its centennial year in business, are going to be a major U.S. employer for another 100 years.

Simply put, this law is now a job killer. It yields advantages to global competitors without commensurate payback to U.S. workers. If nothing is done to make necessary reforms, we sustain a disincentive for job growth in America, hampering employees' opportunity and giving U.S. employers another reason to invest elsewhere. And, while we sit idly, other countries will continue racing ahead of the U.S., surpassing us in terms of education, innovation and job creation. The disconnect between the FLSA and the modern workplace will continue to grow, increasing tensions between employers, employees and regulators, with the only true beneficiary being the plaintiff's bar.

The U.S. Economy Has Evolved Since 1938

The health of the U.S. economy – and U.S. companies – depends on modern, clearly understandable, relevant and flexible labor laws and regulations. With over 95% of the world's population and about 80% of the world's purchasing power *outside* of the U.S., the intense pressures of global competition and the globally integrated nature of business allow for nothing less.

When the FLSA was first signed into law, manufacturing, not services, was the predominant business activity in the country. In the seventy years since then, many new industry sectors have been created. Companies large and small, manufacturing and service-based alike, have substantially changed their business models, hiring and employment practices, and they have embraced myriad technological tools, such as e-mail, smart phones, instant messaging, video conferencing, social media and more.

What may not be as obvious is that today's business environment is driven by new global economic forces that are transforming the way work is done, where it is done, by whom it is done, and the skills needed to get it done. America is no longer an economic island or fortress. Our companies, and therefore *our workforce*, must now compete against myriad economic powers throughout the world, who are marshalling their employers, educators, and government resources to match and surpass our past and present successes.[2]

Additionally, there is a blurring of the lines between manufacturing and service-oriented enterprises, and there has been a dramatic shift from goods to nearly 80% services as a percentage of U.S. GDP. This percentage likely will grow higher because even traditional industries, such as heavy equipment, automobiles, consumer products, energy and communications, are relying ever more on services-based innovations. The shift to services is fueled by the emergence of and reliance on smart technological tools and forward-thinking workforce practices to improve efficiencies and out-compete the competition.

The New World of Work in the 21st Century

So, what does the new world of work look like in a growing services-oriented technologically based economy? I can tell you that it looks nothing like what it did in 1938. And, it looks very different from 1947 – the year the Portal-to-Portal Act[3] was signed into law. A look at what my own company created at that time illustrates the point.

IBM Relay Calculator, 1944

In these decades, IBM supplied the systems required to implement the recently passed Social Security Act of 1935 to start building a pension system for senior citizens. We

[2] HR Policy Association's Blueprint for Jobs in the 21st Century, p. xxvii, 2011.
[3] The Act amended the FLSA to provide guidance about what is compensable time, and it exempted regular commute time from compensation.

created the time stamp, a room-size calculator, the first test scoring machine, and the vacuum tube. We also marketed the first commercially successful electric typewriter.

At IBM and in many other companies, the world of work is characterized by a philosophy that work is *something one does, not a place one goes*. It also is characterized by rapid changes in technology and dynamic markets and an imperative from our clients - federal defense agencies, major banks, large utilities and healthcare providers, among others - for 24/7 availability of their systems and services. Companies cannot turn back the clock on this dynamism. But in meeting these challenges, we do what we can, within the confines of the law, to create a better way of working that relieves some familial and personal pressures.

For many people in our current workplace model, fixed office locations are no longer essential for employees to work together and to communicate. Over 40% of IBM's global employee population works outside of a traditional office setting. This number climbs to 50% across our U.S. population. We are not the exception in these practices: Thousands of companies are moving in the same direction.

Recognizing the growing need to balance child or eldercare responsibilities, address medical conditions or work around commuting and other challenges, today's workers often desire, if not require, flexible work options. I am proud that my company has been at the forefront of offering these options to our employees, such as work-from-home, job sharing, compressed work weeks and other alternative work schedules. Workers just entering the job market tend to use technology as an integral part of their lives, giving them greater freedom and flexibility and the chance to work in ways that suit their lifestyle and that encourage their creativity. And many workers desire "exempt" status, a sign to them that they are recognized as skilled professionals and are trusted to manage their time in the manner that meets their needs, while still fulfilling their obligations to the employer.

Thus, the new economy is characterized by technological innovation, dynamic structural and market shifts, new business models, new workforce management models and changing labor pools. The result is dramatic change to workforce organization and culture, employees' expectations, career paths, and to the demands for skills and learning. This new world of work can only lead to the conclusion that we need fresh thinking in U.S. labor law.

The FLSA's Failings

I submit the following question for your consideration, "Why is it that a 70-year-old law, enacted in a different century, which was based on a different model of the U.S. economy, and at a time that pre-dates global competition and nearly all technology we use today, should not be modernized, clarified and made relevant for today's economic realities?"

Let me give you just a few examples of how wildly out-of-sync this law really is:

1) Five years ago, we voluntarily reclassified seven thousand of our highly educated computer employees to non-exempt because we could not be certain whether they met the 1990 criteria for the FLSA's computer employee exemption. These workers had salaries averaging $77,000 per annum (and some up to $150,000). We lowered their base salaries by 15% to account for potential overtime and to maintain market-based compensation for similar non-exempt jobs. Not surprisingly, **nearly half of them** contested their reclassification!
2) One major retailer requires its delivery drivers to pick up and drop off their PDAs at the store every day for fear they can't track or prevent their use after hours. So these employees waste time in traffic, burn energy, create pollution and get to spend less time at home.
3) An aerospace company must limit the amount of discretion exercised by highly-educated, entry-level engineers due to the security content of their jobs. Because discretion is a large litmus test in the FLSA, they must be classified as non-exempt – totally at odds with their training and compensation. A real kick in the guts for the self worth of these employees.
4) IBM has inside sales employees and outside sales employees, and both groups drive revenue by selling products and services. Both groups should have the opportunity to earn lucrative compensation. But inside sales workers feel like second class workers because they must be non-exempt. No trust. Lower status. Lower earning potential. What's mind-boggling is that everyone is selling the products or services – only one walks, while the other sits!

Let me address some of the FLSA's most onerous issues and consequences.

Deciphering the Rules on Which White Collar Workers Must Be Paid Overtime is Confusing. A considerable share of the friction with the FLSA by employers and managers alike arises from the "white collar" exemptions and corresponding regulations, which have created numerous difficulties for employers in determining which employees are non-exempt, and thus subject to overtime requirements, and which are exempt. The rules governing the exemptions are so riddled with ambiguities and imprecision that employers – and even the Department of Labor (DoL) – struggle when applying them to *today's* modern workplace. Meanwhile, employers cannot simply assume that because an employee is highly paid, he or she is exempt. Indeed, a survey of HR Policy member companies conducted in June of this year (with 151 companies responding) showed that almost half (48%) of the wage and hour claims settled by companies involved employees earning more than $50,000 per year, with 5% of the cases involving employees earning six figures. Examples of difficulties employers face in determining who does and who does not have to be paid overtime abound. Some of the more prominent examples include:

1. **Computer Employees**. The FLSA and its implementing regulations include an exemption for "computer employees," but the definition is rooted in the technology of the late 1980s, a time before many people had Internet access or email, let alone use of the sophisticated technologies of today.

IBM Personal Computer, 1980s

IBM Data Center, Present

While computer programming and systems design are explicitly exempted from overtime requirements, work performed by information security experts and people who manage huge networks or databases and earn nearly $100,000 a year, is not.

2. **Entry-level Degreed Engineers and Accountants**. The FLSA regulations state that, to be an exempt professional, an employee must perform "work requiring advanced knowledge in a field of science or learning" involving the "*consistent exercise of discretion and judgment.*" Often, as new graduates start their first jobs, they exercise very little discretion or judgment. Instead, they follow the highly complicated rules and principles of the profession and/or directions from those to whom they report, until they acquire sufficient experience on the job. The quandary faced by employers is determining at what point new employees with sophisticated skills cross the threshold into the blurry FLSA definition of a professional. By every other standard, including lucrative starting salaries, these employees would clearly be considered professionals.

Official Exemption Interpretations of the Same Workforce are Inconsistent. Particularly nettlesome is determining what level of "discretion and independent judgment" employees must have to qualify for the Administrative Exemption. Sometimes, not even the Department of Labor's Wage and Hour Division (WHD) can make up its mind. For example, on September 8, 2006, the WHD determined that mortgage loan officers were bona fide administrative employees who are exempt from the FLSA's protections. Yet, on March 24, 2010, the WHD reversed itself and determined that they do not qualify as exempt. If the WHD cannot consistently determine who is a bona fide administrative employee, how are employers supposed to figure it out?

Even DoL Gets Sued. Meanwhile, the limitations on the Department's own ability to distinguish between who is and who is not exempt under the Administrative Exemption have been exposed. The example is a recent action brought against the Department

involving the exempt status of more than *1,900 of its own employees*, including the awarding of back pay to a number of them. In addition to a large number of administrative employees, those eligible included highly paid computer professionals, paralegals, litigation support specialists, pension law specialists, as well as highly paid Wage & Hour Division compliance specialists.[4]

Exempt Status Does Not Govern the Amount of Compensation. The absurdity of the struggle of who is and is not exempt is further highlighted by the fact that the ultimate determination does not necessarily determine *how much* employees get paid but rather *how* they get paid - hourly versus salaried. The amount an employee is paid is determined by a variety of factors, including market rates, education, experience, performance and so forth.

Litigation is Exploding. FLSA compliance problems are exacerbated by the fact that the statute not only provides for enforcement by the DoL, but also by private actions. As a result, the private bar has taken advantage of the law's lack of clarity by pursuing highly lucrative class actions against employers who struggle to ascertain what is required. The number of FLSA lawsuits has quadrupled from about 1,500 per year in the early 1990s to nearly 7,000 in 2010,[5] and this does not count the number of cases brought under state laws which often vary from the federal law. In the HR Policy Association survey, 56 per cent indicated they had been sued within the past 10 years, with 13 per cent being sued four or more times. Faced with the uncertainties of the law, companies often settle these cases, with a median settlement cost of $7.4 million for federal cases and $10 million for state cases.[6] My own company has not gone untouched in this area. Approximately five years ago, we were sued by computer professionals claiming they should have been non-exempt. While admitting no guilt, we settled the case for $65 million, approximately a third of which went to the plaintiffs' attorneys.

There is No Federal Preemption of State Law. On top of all the problems created by the federal wage and hour laws, additional inflexibilities and complexities are created by state laws, which are not preempted as long as they are more "protective."[7] For example, California has significantly narrower criteria for which employees are exempt from overtime. In order to be considered an exempt computer employee in California, an individual must perform duties involving the exercise of discretion more than 50 percent of the time in *each work week* and earn at least $79,050 annually.[8] In contrast, under federal law, there is no discretion requirement, the exemption is measured over a longer period of time and is not based on a hard-and-fast percentage test, and the employee needs to earn at least $455/week if paid on a salary basis or be paid a minimum of $27.63/hour if paid on an hourly basis.[9] Thus, two different employees performing the

[4] Cf. http://www.sniderlaw.com/pages/FLSADOL.html
[5] U.S. Courts, Annual Report of the Director, Table C-2A. Year ending June 2010.
[6] Samuel Estreicher and Kristina Yost, "Measuring the Value of Class and Collective Action Employment Settlements: A Preliminary Assessment, New York University School of Law, Working Paper No. 08-03, January 2008.
[7] 29 U.S.C. 218.
[8] California Labor Code Section 515.5.
[9] http://www.dol.gov/whd/regs/compliance/fairpay/fs17e_computer.pdf

same work for the same client in the same company, one working in California and another working in another state, may be scheduled and compensated completely differently as a result of the different threshold and minimum pay requirements.

In a different example, federal statute differs from that of certain states in defining a workweek and the threshold for hours that would necessitate overtime payments. In California, most employees must be paid overtime for any hours worked in excess of *eight in a single day*, regardless of how many hours he or she works the rest of the week. Federal law does not address a per-day hour limitation, instead defining 40 hours per work week as the threshold.

"Professionals" Often Resent Hourly Status

Contrary to popular belief, "professional," or white collar workers, often resent being classified as hourly employees. The feedback I have heard, both directly from employees and from my peers, is that employees aspire to be exempt, salaried workers as they grow through their careers. In fact, I have had an employee literally weeping on my shoulder when she was reclassified to non-exempt status. Exempt status is often viewed as a higher rung on the corporate ladder, compared with non-exempt status. Their focus is on getting the job done and doing it well, not simply on putting in hours at the office.

Significant to note is that exempt professionals often enjoy greater workplace and work time flexibility, allowing them to better meet their personal and professional obligations in ways that benefit both them and the employer. The legal burden, risk and administrative nightmare of tracking all time worked by non-exempt "professionals," requires inordinate time and monetary resources to manage. One way companies have dealt with this is to restrict non-exempts' ability to utilize flexible work alternatives because of the difficulty of verifying the actual working time of the mobile worker. In fact, the survey of HRPA members I mentioned previously found that in ensuring compliance with the FLSA for their non-exempt employee populations, 32 per cent of companies have imposed restrictions on telecommuting, 56 per cent restrict the use of PDAs, and 44 per cent impose restrictions on flexible scheduling.

Naturally, most "professional" non-exempts do not desire these restrictions, but they been necessitated by the outdated, unclear and inflexible statute which never contemplated the mobile work opportunities of today.

Contrary to non-exempt workers, exempt employees are paid a consistent and predictable salary, not subject to the uncertainties of never-guaranteed, inconsistent overtime. Also, overtime is not something every hourly worker is entitled to work, nor does every worker want to work overtime just to achieve financial parity with their exempt counterparts in related job classifications.

Exempt employees may be eligible for different promotion opportunities, compared to their non-exempt counterparts. This is the result of differences in professional band levels between exempts and non-exempts and different promotional tracks that

companies create for each population. Moreover, benefits based on base pay, such as corporate retirement contributions to 401(k) accounts or other fringe benefits, may be disparate between exempt and non-exempt employees as a result of differences in base pay rates between the populations.

Suggested Fixes to the FLSA's 21st Century Failings

There are several specific actions Congress can take to fix obvious problems with the FLSA right now. These fixes, listed below, would not only help restore the U.S. as a good place to invest and hire American workers, but they would be a strong signal of Congressional intent to spur job creation in the U.S.

Modernize the Computer Employee Exemption. The solution is to modernize the definition of computer employees by explicitly including the broader range of 21st century computer-related duties, such as securing, updating, maintaining and testing of existing applications without modifying code, that some professionals perform today.

Explanation: The Computer Employee exemption was first introduced 20 years ago to address the absence of any exemption for the developing computer industry. The exemption criteria, *defined narrowly and based on the state of technology 20 years ago*, do not align to modern IT jobs and have not kept up with changes in responsibilities of those professionals. Moreover, modern computer professionals require a higher level of independent thought and knowledge to perform their duties, and they are highly educated. They often have advanced degrees and must constantly study to keep up with changing technology. Despite this, many computer professionals must be classified as non-exempt under current law.

Clarify the "De minimis" Exception to Paid Time. The solution is to update and clarify the rules, such that insignificant IT-related activities are explicitly included in the "de minimis" exception and are not considered "time worked." Also, the law should make it clear that, even if engaging in insignificant IT-related activities does constitute time worked, these activities do not trigger the start of the work day or signify the end of the workday. Thus, "normal" commute would remain non-compensable time, as it is under current law.

Explanation: For non-exempt employees, all time worked must be recorded and compensated. However, the modern workplace gives rise to minor IT-related activities outside of the work day (e.g., checking email/calendar/voicemail before or after leaving for work, or using a PDA to check a schedule change). The "de minimis" exception addressing these circumstances is *not defined in the law*, leaving open to varying interpretations what activity is considered compensable, as well as what activity triggers the start of the work day or ends the work day. Unfortunately, there has been a lack of consistency in current interpretation of these issues. The result is legal uncertainty and risk; it also interferes with our ability to provide non-exempts workplace and time flexibility.

Expand Exemption for Well-Compensated, Commissioned Inside Salespeople. The solution is to eliminate this artificial and outdated distinction under the FLSA to account for 21st century communications, sales methods and customer buying habits. Inside sales employees (currently non-exempt) should be treated the same as their outside sales counterparts (exempt), provided they meet specific criteria. Under these arrangements, the compensation structure for sales roles will equitably support pay for performance based on sales targets and achievement.

Explanation: The Fair Labor Standards Act creates an artificial disparity between "inside" and "outside" sales employees. Specifically, sales employees who travel out of the office to a customer's place of business are exempt, while most employees who conduct sales from a *fixed office location* are non-exempt. In other words, inside sales employees must be paid on an hourly basis and be subject to strict record keeping requirements, rigid time schedules and more stringent monitoring of their work.

We and others across many industries believe these restrictions are out of sync with today's customer service needs, and the opportunities offered by technology, as well our sales employees' pursuit of and ability to enjoy greater workforce flexibility to balance both their work/family needs and their ability to increase their earnings. These restrictions create an artificial and outdated distinction between sales reps, although both have responsibility for the same territories, have the same accounts, have challenging sales quotas, work in partnerships on teams together and are paid off the same sales results. The legal limitations associated with non-exempt inside sales also make it hard for us to attract and retain the best talent for this critical element of how we approach the marketplace.

Remove Disincentives for Performance-Based Bonuses. The solution is to allow employers to exclude, from the "regular rate," payments rewarding employees for meeting or exceeding the productivity, quality, efficiency, or sales goals specified in an employer's gain-sharing, incentive bonus, commission, or performance contingent bonus plan.

Explanation: Employers are discouraged from paying bonuses and other forms of incentive pay to non-exempt employees because the law requires such amounts to be included in the employee's rate of pay for purposes of calculating overtime. For example, an employer may want to extend pay-for-performance incentives to non-exempt employees by offering annual incentive payments for achieving certain performance targets. However, payment of the incentive will require recalculation of overtime pay for the year. Moreover, when making the decision to provide such incentives, the employer often doesn't know how much overtime the employees will work, thus preventing an accurate projection of costs. To avoid this administrative complexity and potential legal exposure, some employers simply conclude that they are not going to extend incentive pay programs to non-exempt employees.

If anything, the law should encourage employers to reward their employees for achieving certain performance goals. Yet, the current law discourages this with the administrative

hurdle of requiring that those amounts be calculated into base pay for purposes of determining the overtime rate ("regular rate").

Allow Preemption of State and Local Wage and Hour Laws. The solution is either a broad preemption of state and local wage and hour laws, or at the very least, a safe harbor or irrebuttable presumption favoring any employer doing business in multiple states who is operating in compliance with the Fair Labor Standards Act.

Explanation: As is the case under the National Labor Relations Act and the Employee Retirement Income Security Act, there is a strong need for broad preemption under all federal employment laws, but it is particularly essential under the wage and hour laws. Multi-state employers should be able to achieve uniformity in how employees performing the same job for the same company are paid and the scheduling rules that apply to them regardless of what state or locality those employees happen to work in.

Determine Where the Law's Protections and Resources Are Most Needed. We propose that stakeholders should address the current exempt/nonexempt morass in a way that provides clarification to employers, employees, the Department of Labor and the federal courts, while also targeting the protections of the law to those who need it and avoiding the law's inherent inflexibilities for those who do not.

Explanation: The task most desperately needed in a comprehensive reform of the law is to identify the abuses that are to be addressed. This primarily involves identifying the occupations and situations where employees are most vulnerable. Making these determinations should be based on hard data, as well as industry and occupational profiles. Ultimately, empirical evidence will demonstrate the degree of wage and hour protections needed for certain groups of workers. The objective would be a consensus on a strategic overhaul of the FLSA that achieves the correct balance between protections against abuses and the flexibility employers and employees need to ensure the competitive enterprise.

Conclusion:

Plain and simple: The U.S. leads in innovation. The U.S. leads through companies like IBM in work practices. However, the U.S. doesn't lead in contemporary workplace rules. The FLSA binds our businesses and our workers in European-style regulatory knots that restrain growth, innovation, jobs and work/life flexibility. But, we aren't Europe. America fixes problems, and this is one we must fix.

Mr. Chairman and distinguished Members of the Committee, on behalf of IBM and the HR Policy Association, I would like to thank you again for the opportunity to testify before you today. We strongly encourage your leadership in accomplishing the immediate and longer-term goals, and we stand ready to work with you and your staff to draft legislation that provides the solutions outlined in my testimony.