

GROUNDHOG DAY COMES EARLY FOR WEST COAST AUTO DEALERS: ANOTHER LOSS IN SERVICE ADVISOR EXEMPTION BATTLE

Insights
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In a disappointing but perhaps unsurprising decision, the 9th Circuit Court of Appeals once again ruled that service advisors employed by automobile dealerships do not qualify for the Section 13(b)(10)(A) overtime exemption under the federal Fair Labor Standards Act (FLSA). For dealers on the west coast, this might sound like a familiar story. In fact, you would be forgiven if you feel like you are reliving an early version of Groundhog Day and hearing the same story once again. You wouldn't be far off.

The 9th Circuit federal appeals court, which has jurisdiction over employers in California, Washington, Arizona, Oregon, Nevada, Alaska, Hawaii, Idaho, and Montana, initially formed this conclusion with [a stunning March 2015 decision](#), causing many dealerships to adjust their practices. Dealers caught a bit of a break when the [U.S. Supreme Court rejected this interpretation](#) this past summer and sent the case back to the appeals court for a second bite at the apple, leading some dealers to hope for a different outcome.

But yesterday, the appeals court once again reached the same conclusion and handed dealers in these states yet another agonizingly familiar loss. If you haven't adjusted to this current interpretation, you need to familiarize yourself with the decision and decide on a course of conduct to adapt (*Navarro v. Encino Motorcars, LLC*).

QUICK HISTORY LESSON DEMONSTRATES VOLATILE NATURE OF RULE

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In 1974, Congress amended Section 13(b)(10)(A) of the FLSA to ensure that “any salesman, partsman, or mechanic primarily engaged in selling or servicing automobiles, trucks, or farm implements” at covered dealerships were considered exempt from overtime. The U.S. Department of Labor (USDOL) soon issued a 1978 opinion letter providing an interpretation that service advisors were considered exempt, aligning itself with several court decisions that came to the same conclusion. The agency even confirmed its position in a 1987 Field Operations Handbook.

For the next several decades, auto dealers across the country established business practices and compensation models relying on this practice being acceptable under the law. In 2011, however, the USDOL completely reversed course and unleashed a regulation that limited “salesman” to employees who sell automobiles, trucks, or farm implements – an interpretation repeatedly rejected by the courts and long before abandoned in practice.

A Southern California auto dealership challenged the USDOL’s interpretation of the statute by filing a federal lawsuit. In [a 2015 decision](#), the 9th Circuit Court of Appeals excused the USDOL’s radical change in position, describing it as “rationally explained” and supported by regulatory history. It became the first federal court in the country to rule this way, leading to a review by the highest court in the land.

[The Supreme Court disagreed](#) with the 9th Circuit. It concluded the USDOL “did not analyze or explain why the statute should be interpreted to exempt dealership employees who sell vehicles but not dealership employees who sell services (that is, service advisors).” Because it flipped its position and “gave almost no reasons at all,” the Supreme Court found the USDOL’s regulation “procedurally defective” and not entitled to receive deference in the interpretation of the statute.

But, unfortunately, that was not the end of the debate. The Supreme Court sent the case back to the 9th Circuit for further proceedings, ordering the appeals court to review the issue once again without taking the USDOL rule into account. And yesterday, after having a chance to consider the issue anew, the 9th Circuit stuck to its guns and came to the same conclusion it did two years ago: service advisors cannot use Section 13(b)(10)(A) to justify an exemption from overtime under its watch.



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9TH CIRCUIT DECISION: ANOTHER LOSS FOR EMPLOYERS

The 9th Circuit had no trouble arriving at the same conclusion even without relying upon the USDOL's rejected rule. The appeals court concluded that the text of the FLSA demonstrated that Congress never intended to exempt service advisors from overtime. It cited to the "longstanding rule" that requires courts to narrowly construe exemptions against the employers seeking to assert them, rejecting any implication that the exemption categories should be read expansively.

Further, the appeals court said that the legislative history confirms that Congress only intended to exempt salesmen selling cars, and mechanics and partsmen servicing cars, when it passed Section 13(b)(10)(A). "Congress did not intend to exempt service advisors," the court said, citing passages from hearings held in 1966 before various legislative subcommittees.

Once again, the 9th Circuit admitted that its conclusion directly conflicted with decisions from other courts: specifically the 4th and 5th Circuits, several federal district courts, and the Supreme Court of Montana. However, the court concluded that it was "unpersuaded by the analysis of those decisions" and declined to follow their lead.

WHAT DOES THIS MEAN FOR DEALERSHIPS?

Those employers outside of the 9th Circuit (California, Washington, Arizona, Oregon, Nevada, Alaska, Hawaii, Idaho, and Montana) should note that this ruling applies only within its jurisdiction. This decision changes nothing outside of these states (although there is a danger that other courts could soon follow the 9th Circuit's lead).

For those dealers in the 9th Circuit's territory, there is no doubt that this decision once again undercuts the Section 13(b)(10)(A) overtime exemption for service advisors. However, it does not mean that service advisors can never be exempt from FLSA overtime. Section 7(i) of the FLSA provides another overtime exception for certain employees paid under a bona fide commission pay plan.

Section 7(i) allows you to exempt from overtime any employee:

- of a “retail or service establishment” (meaning any location where 75% of the annual dollar volume of sales is not for resale and is recognized as retail sales in the particular industry);
- who earns more than half of their compensation by commissions on goods or services for a “representative period” (of not less than one month); and
- whose regular hourly rate of pay for each overtime workweek is more than 1.5 times the FLSA’s minimum wage.

Of course, you must determine whether the applicable overtime laws of a state or another jurisdiction include any exception like Section 7(i), or whether any provision similar to Section 7(i) is different in meaningful ways such that you would need to adjust your pay practices. While 7(i) might be a viable alternative, it won’t work in every scenario and needs to be evaluated for compliance.

WHAT’S NEXT?

This undesirable interpretation is now the current law of the land on the west coast, although, as the above history indicates, it would not be surprising to see another change to this position. The employer could request a full review by the entire panel of 9th Circuit judges (an *en banc* review), or the Supreme Court could step in once again, either of which could lead to another reversal – this time in the employer’s favor.

A more likely hope for employers, however, could rest with the impending change in administration. President-elect Trump’s nominee for Secretary of Labor appears to be much more willing to scrap burdensome regulations interpretations than his predecessors. Andrew Puzder has already signaled his dislike for other expansive wage and hour regulations by the USDOL, and once he is in charge, employers could start to see some of the more onerous rules rolled back. However, such a change would not be as simple as flipping a switch, and any such regulatory changes could take time – and are certainly not foregone conclusions.

Another possibility is that Congress could amend the FLSA to resolve the dispute in the favor of the dealers. With Republicans controlling both houses of Congress and about to take the White House, industry advocates may very well

push to make explicit what the 9th Circuit found to be at best “implicit” and “ambiguous.” It would be fairly simple for Congress to amend the exemption list to specifically include “service advisors” alongside salesmen, partsmen, and mechanics, which would resolve the debate once and for all.

Until a full panel of the court, the Supreme Court, the new USDOL, or Congress alters the current interpretation, dealers on the west coast need to adjust to the new reality, even if it feels like a bad nightmare being relived again and again and again.

For more information, visit our website at www.fisherphillips.com or contact your regular Fisher Phillips attorney or any member of our [Automotive Dealership Practice Group](#).

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