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U.S. Department of Labor Publishes Final Rule Raising Salary for White Collar Exemptions

On May 18, the U.S. Department of Labor published the final Rule "Defining and Delimiting the Exemptions for Executive, Administrative, Professional, Outside Sales and Computer Employees." The changes in this new rule are expected to affect over 4 million employees nationwide who are currently classified as exempt executive, administrative, or professional employees.

Important changes in the Rule are the following:

- **Increase in the minimum weekly wage for exempt employees.** The minimum weekly wage for an exempt employee will be the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (currently the South). This results in a salary level of $913 per week, or $47,476 annually for a full-year worker. In New York, this means an increase of $256.75 per week in order to qualify as an exempt employee. In other states, the increase is likely to be even greater.

- **Ability to include certain types of income to meet the requirement.** Up to 10 percent of the salary requirement may be met with nondiscretionary bonuses, incentive payments, and commissions, provided these forms of compensation are paid at least quarterly.

- **Increase in the Highly Compensated Employee Wage.** The minimum annual salary for the exempt Highly Compensated Employee (HCE) is raised to the annualized weekly earnings of the 90th percentile of full-time salaried workers nationally. This results in a salary level of $134,004 annually in order to qualify as an HCE. This is an increase of $34,004 annually.

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Having Fun at "En-Joie the day on HH&K"!

James Orband, Michael Keenan, Tina Fernandez, Gary Tyler, Brent Whiting, Jamey Lawson and Erica Lawson (left photo) Larry Anderson and James Franz (middle photo) Erica Lawson, Tina Fernandez, Michael Keenan and Megan Curinga (right photo) at "En-Joie the Day on HH&K"

U.S. Department of Labor Publishes Final Rule Raising Salary for White Collar Exemptions (continued)

(Continued from page 1)

- **Automatic Increases.** Both the exempt employee weekly wage and the HCE annual earnings will be updated every 3 years. The Department of Labor estimates that at the next update (January 2020), the exempt salary level will likely rise to $984 per week ($51,168 per year), and the HCE total annual compensation will rise to $147,524.

There is no change to the job duties test for the Executive, Administrative, and Professional exemptions.

The Rule has an effective date of December 1, 2016. That means employers must act now to prepare for the changes. Employees who are currently classified as exempt but do not meet the new exempt salary threshold must either receive a pay increase or be re-classified as non-exempt and paid overtime for hours over 40 in a work week. Please keep in mind that increases in pay can also mean increases in the cost of benefits.

Both New York and Federal law include stiff penalties for the failure to correctly pay wages. Employers can be liable for up to three times the unpaid amount of wages (including improperly unpaid overtime). Private lawsuits include awards of damages for attorney's fees, making them attractive for plaintiffs' attorneys.

Determining exempt status is often difficult to begin with, and reclassifying employees can lead to turmoil in the workplace. Employers should act now to educate their workforce about the reasons for the changes, and should plan for making wage changes sooner rather than later.

Article written by Dawn J. Lanouette, Esq. For more information, contact Ms. Lanouette at (607) 231-6917 or via email at dlanouette@hhk.com or John C. Fish, Esq. at (607) 231-6712 or via email at jfish@hhk.com.

Tax Law Update: New IRS Audit Procedures for LLCs and Partnerships

The Bipartisan Budget Act of 2015 (BBA) was signed into law on November 2, 2015 and repealed the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA). The BBA changed the old TEFRA procedures and rules surrounding IRS audits of partnerships and limited liability companies taxed as a partnership (both partnerships and LLCs taxed as partnerships are referred to herein as "partnerships"). The BBA attempts to streamline the IRS partnership audit process so that it is similar to a corporate audit. Partnerships should review their governing documents to ensure the new IRS audit procedures and rules are addressed appropriately and do not have unintended adverse effects on the equity partners.

The effective date of the new IRS audit procedures in the BBA is January 1, 2018. Prior to this date, partnerships may elect for the BBA to apply to them by making an affirmative election on their tax return. After January 1, 2018, certain qualified partnerships with fewer than 100 partners may affirmatively opt out of the BBA each tax year on their tax return. Absent the annual election, the BBA procedures will apply to all partnership tax returns. Current partnership agreements may need to be modified to address how the partnership opts in or out of the new BBA procedures.

The new BBA replaces the old TEFRA "Tax Matters Partner" with a "Partnership Representative." The new Partnership Representative is the exclusive party to receive all IRS correspondence with respect to audits, bind all partners, and act on behalf of the partnership during any audit or judicial proceeding. The Partnership Representative only needs to have a "substantial presence in the United States" and does not need to be a partner or have a stake in the outcome. The designation is not subject to termination for bankruptcy or criminal investigation. If the partnership does not select a Partnership Representative, the IRS may select any person as the Partnership Representative. Current partnership agreements may need to be modified to address how the partnership selects its Partnership Representative and how the Partnership Representative indemnifies the partnership and partners for any errors or omissions it makes during a BBA audit procedure.

The most significant change the BBA makes is when and how a tax adjustment is made against a partnership. Should the IRS make a tax adjustment after the audit is completed, the assessment is made against the partnership at the partnership level and during the adjustment year, or in the year the audit or judicial proceeding is concluded. The partnership will owe and pay any additional tax in the adjustment year. This is different from the old TEFRA rules, which made any tax adjustment at the partner level and was paid in the review/audit year when the tax item was recognized.

While this may at first appear to be a timing issue, it could adversely affect partnerships whose equity partners or equity percentages differ from the review/audit year to the assessment year. To be equitable, partnership agreements may need to be modified so that withdrawing partners or partners with reduced equity percentages pay their applicable pro-rata portion (based on their equity during the review/audit year) of the additional tax due in the adjustment year. To appropriately address this issue, the partnership agreement may need additional provisions such as indemnification of current partners and modification of the terms on equity transfers and buy-out provisions.

Congress has given partnerships and LLCs until January 1, 2018 to address these new tax audit provisions in their partnership or LLC governing document. It is important to review your current partnership or LLC agreement and make appropriate revisions to properly address these new audit rules.

Article written by Ryan M. Mead, Esq. For more information, contact Mr. Mead at (607) 231-6928 or via email at rmead@hhk.com.

Announcement

Ronald L. Greene, Esq.

Partner Ronald L. Greene has joined the YMCA of Broome County Board of Directors.

Mr. Greene also recently participated in a BCBA CLE, presenting on "The Business of Law."

New York Issues Final Regulations Imposing Enhanced Anti-Money Laundering Measures for Financial Institutions

The New York State Department of Financial Services (the "DFS") has made final its proposed regulation (the "Proposal") mandating enhanced anti-terrorism and anti-money laundering ("AML") requirements under the federal Bank Secrecy Act ("BSA") for financial institutions licensed and regulated by the State. The final regulation, Part 504 of the Superintendent's Regulations ("Part 504") applies to all banks, trust companies, private bankers, savings & loans, savings banks, branches and agencies of foreign banks, check cashers, and money transmitters chartered or licensed by the State ("Regulated Institutions"). Part 504 takes effect January 1, 2017; the first certification or "compliance finding" required by the new rule must be filed with the DFS by April 15, 2018.

Although it does place additional compliance burdens on New York financial institutions, the final Part 504 differs from the Proposal in important ways. The DFS received extensive written comments from industry groups, including the New York Bankers Association and the New York State Bar Association Banking Law Committee, highlighting aspects of the Proposal that were likely to be unduly burdensome or lead to adverse consequences. At least some of the changes requested by the commenters are reflected in the final rule. Most importantly, the Proposal would have, for the first time, potentially subjected the chief compliance officer (or equivalent) of a New York financial institution to criminal sanctions for noncompliance. The final Part 504, while still requiring the board of directors or a "Senior Officer" to certify compliance, states that the regulation will be enforced by the DFS under "applicable laws" but – to the relief of financial institution compliance officers - omits any reference to criminal sanctions.

The Final Rule

The preamble to the final Part 504 states that the DFS has identified "shortcomings in the transaction monitoring and filtering programs" of Regulated Institutions and "a lack of robust governance, oversight, and accountability at senior levels" of these institutions. To address these perceived deficiencies, the following measures are required:

1. Risk Assessment

Regulators generally have expected banks and other financial institutions to implement a BSA/AML program that is risk-based, in accordance with an internal assessment of money laundering risk. Part 504 effectively codifies this requirement, mandating that each Regulated Institution conduct an ongoing and comprehensive assessment of the money laundering risk posed by each customer, product, and line of business.

2. A Transaction Monitoring Program

Reflecting the perceived inadequacies of existing programs at individual institutions, Part 504 spells out the minimum requirements of a transaction monitoring program in granular detail. Among other requirements, the program should be based on the institution's AML Risk Assessment and mapped to specific businesses, products, and customers.

One important change: the Proposal required documentation in "easily understandable language." Apparently in response to comments that this requirement was too vague to provide a basis for compliance, this language was omitted from the final rule.

3. A Filtering Program

The filtering program must be designed to intercept transactions that are forbidden by applicable sanctions of the Treasury's Office of Foreign Assets Control (OFAC). Like the Transaction Monitoring Program, it should be based on the institution's ongoing Risk Assessment. Furthermore, it should incorporate appropriate tools and technology for matching names and accounts. While Part 504 does not mandate any particular tool, it does note that there are automated tools available that use algorithms based on so-called "fuzzy logic." Part 504 states that the Filtering Program may be either automated or manual; however, given the risks involved with non-compliance, most institutions would be well-advised to implement an automated program, if they have not done so already.

Again, there were several important changes. The Proposal would have required the institution to establish "watch lists that reflect current legal or regulatory requirements" including, but not limited to, OFAC. Responding again to commenters' concerns regarding the uncertainty of what was expected, the final Part 504 omits any reference to "watch lists" and now is specific to the OFAC sanctions list. The Proposal had expressly prohibited "tinkering" with the Transaction Monitoring or Filtering Programs in order to minimize the number of alerts generated or Suspicious Activity Reports ("SARs") filed by the Regulated Institution. The final Part 504 softens this provision. It no longer prohibits making changes, but does require that the institution document the reason for any changes and make the documentation available to the Superintendent for inspection.

4. Certification

Perhaps most significantly, the Proposal would have explicitly required that the institution's Chief Compliance Officer (or equivalent) annually prepare and sign a certification, addressed to the DFS, confirming that he/she has reviewed, or caused to be reviewed, the institution's Transaction Monitoring and Watch List Filtering programs and that both programs comply with the requirements set forth in the Proposal. The Proposal stated that an officer who files a false or incorrect certification may be subject to criminal prosecution. The final Part 504 omits any reference to criminal sanctions and responds to numerous comments expressing concern about the burden this would have put on individual compliance officers. Among other things, the New York State Bar Association comment letter noted that this requirement would have had the perverse effect of making it difficult for an institution with compliance problems to hire a competent compliance officer. The final Part 504 replaces this provision with a requirement for an annual Board Resolution or Senior Officer(s) Compliance Finding to be filed with the Superintendent; there is no longer any mention of criminal liability. "Senior Officer" is defined more broadly so that one or more different officers could sign the certification.

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In short, while federal law already requires all institutions to have a BSA/AML compliance program in place, Part 504 raises the bar for New York institutions whose programs are not sufficiently robust. In particular, it mandates requirements for transaction monitoring and filtering that may go beyond what the institution is already doing in these areas.

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U.S. Supreme Court Expands the Scope of First Amendment Employee Retaliation Claims in *Heffernan v. City of Patterson*

On April 26, 2016, in *Heffernan v. City of Patterson*, the Supreme Court of the United States decided that when an employer demotes an employee out of a desire to prevent the employee from engaging in protected political activity, the employee is entitled to challenge that unlawful action under the First Amendment of the United States Constitution and 42 U.S.C. §1983, ***even if*** the employer's actions are based on a factual mistake about the employee's behavior.

Heffernan involved Jeffrey Heffernan, a New Jersey police officer in the City of Patterson Police Department. In 2005, Patterson's mayor was running a contested reelection campaign. During the campaign, Heffernan's mother, who was bedridden, asked Heffernan to drive downtown and pick up a campaign yard sign supporting the mayor's opponent.

Members of the Patterson Police Department saw Heffernan pick up the sign from the headquarters of the mayor's opponent and concluded that Heffernan was supporting the opponent. In fact, Heffernan admitted that he was not involved in the campaign, and Heffernan's supervisors had made a factual mistake about his involvement. The next day, Heffernan's supervisors demoted him from detective to patrol officer and assigned him to a "walking post," due to "overt involvement" in the political campaign.

Heffernan filed an action against Patterson in New Jersey federal court, pursuant to 42 U.S.C. § 1983, and argued that the Department's actions violated his constitutional right to free speech. The District Court of New Jersey rejected Heffernan's argument and reasoned that, since he was not actually engaging in political speech, his First Amendment rights were not violated, despite the fact that his supervisors believed that he was exercising his rights to free speech.

Heffernan appealed, and the U.S. Court of Appeals for the Third Circuit affirmed, holding that "a free-speech retaliation claim is actionable . . . only where the adverse action at issue was prompted by an employee's *actual*, rather than *perceived*, exercise of constitutional rights."

On future appeal, however, the United States Supreme Court reversed. In a 6-2 opinion authored by Justice Breyer, the Court noted that 42 U.S.C. § 1983 authorizes anyone who is "depriv[ed]" of a "right . . . secured by the Constitution" to bring suit against the government in federal court. Justice Breyer acknowledged the ambiguity in the term "right," and questioned whether such "right" focuses on the employee's actual activity, or upon the supervisor's motive and belief regarding what the activity is.

In other words, the question before the Supreme Court was: can an employee bring suit alleging violations of First Amendment rights *even if the employee acknowledges that he was not exercising his First Amendment rights*, but the employee's supervisors believed that he was?

Ultimately, the Court held in favor of the employee. The Court reasoned as follows:

> When an employer demotes an employee out of a desire to prevent the employee from engaging in political activity that the First Amendment protects, the employee is entitled to challenge that unlawful action under the First Amendment and 42 U. S. C. §1983—even if, as here, the employer makes a factual mistake about the employee's behavior.

In reaching this conclusion, the Court cited the text of the First Amendment, which provides that "Congress shall make no law . . . abridging the freedom of speech." The Court found that this language focused on the activity of the government, as opposed to the actions of an individual. Since the government in this case was engaging in an unconstitutional policy, imposing liability was appropriate, regardless of the employee's intent.

In addition, the Court discussed the policy and constitutional considerations in imposing liability. The Court explained that the constitutional harm at issue consisted of discouraging employees from engaging in protected activities, since discharging employees for perceived engagement in political activities can send a message that employees "engage in protected activity at their peril." The Court reasoned that an employer's mistaken belief about the employee's activity did not diminish this constitutional harm.

In its decision, the Court assumed, but did not decide, that the policy that Heffernan's employers implemented was unconstitutional. However, the Court noted that there was evidence in the record suggesting that Heffernan was demoted due to violating a neutral policy prohibiting police officers from overt involvement in any political campaign. The Court therefore sent the case back to the lower court for consideration of the constitutionality of the policy that was actually being implemented.

In summary, *Heffernan* marks an expansion of First Amendment protections and employee retaliation claims brought under 42 U.S.C. § 1983. Under *Heffernan*, actual engagement in protected speech is no longer required to bring suit. The government's mere belief that an employee has engaged in protected speech, whether or not correct, is sufficient to bring a First Amendment employee retaliation claim.

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Presentations

John R. Bedosky, Esq.

Partner John R. Bedosky presented on June 20, 2016 at the National Business Institute Trusts 101 Seminars in Bloomington, MN.

HH&K Annual Firm Picnic

Our HH&K Family enjoying time together at the Firm picnic.

What's in a Name?
Why a Tradename that the State Approved Can Still Lead to Trademark Troubles

Selecting a tradename is one of the most exciting parts of launching a new business venture. Unfortunately, even experienced business owners can be misled by what it means when the Department of State approves a new venture's tradename. Department of State approval of a new venture's proposed tradename means only that another entity is not already organized to do business in the State under the proposed name; it does not mean that the new venture itself is free to do business under the proposed name.

For most business owners, it comes as a very counterintuitive and a very unwelcome surprise to learn that they may not be legally allowed to do business under a tradename that the Department of State approved. The reason this happens is because the Department of State's approval of a new venture's proposed tradename does not account for whether another entity owns trademark rights to the proposed name.

Trademark rights grant an entity using a trademarked name potentially exclusive use of the name nationwide. This means that a company headquartered in California can, under certain circumstances, prevent a company headquartered in New York from using a tradename if the California company owns trademark rights to the name. Because the Internet has made it so easy to survey what tradenames other companies located across the country are using, it is increasingly common for companies to enforce their trademark rights on a nationwide scale.

The best way to avoid running afoul of another company's trademark rights when selecting a tradename for a new venture is to perform a trademark clearance search. A trademark clearance search will determine whether any company owns trademark rights to any name or term that is the same as or similar to the tradename that a new venture wishes to adopt. If a company does own trademark rights to a name that is similar to the name a new venture wishes to adopt, the new venture can tweak its proposed name as needed to avoid trademark problems. If the trademark clearance search reveals no problems, the new venture can proceed with little risk of encountering problems with its tradename.

A new venture's tradename is its calling card to the world. Tradenames adorn advertising, web sites, business cards, and products. Most companies invest heavily in growing their business and establishing goodwill under their tradename. Abandoning a tradename after investing heavily in growing goodwill associated with the tradename is a very costly setback for any business, new or old. A trademark clearance search can substantially reduce the likelihood of that setback ever befalling a company.

Article written by Michael Keenan, Esq. For more information, contact Mr. Keenan at (607) 231-6927 or via email at mkeenan@hhk.com.

Presentations

HH&K Partners participated in the Broome County Bar Association—Continuing Legal Education Valuation Seminar, on July 19, 2016. Erica Lawson served as a moderator for the Program. Dawn Lanouette presented a section entitled "Healthcare Transactions—What You Don't Know Can Kill Your Deal." Paul Sheppard presented on "Real Estate Valuation in Tax Certiorari and Eminent Domain Proceedings."

Paul T. Sheppard presented at July's Broome County Bar Association— CLE 2016 Valuation Seminar.

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Thank You for Another Successful "EnJoie the Day on HH&K"

A great big thank you to all of our distribution partners—Chemung Canal Trust Co., MaineSource Food & Party Warehouse, Manley's Mighty Mart, Mirabito Convenience Stores, NBT/Pennstar Bank and Wegmans —for helping us to make "En-Joie the Day on HH&K" a huge success once again! The weather was fantastic, the turnout was amazing, and we were thrilled to hear people tell us how much fun they had! We are grateful for the opportunity to be able to share this event with our community and the deserving charitable organizations it supports.

FOR MORE INFORMATION

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