

Hospitalitas

News and Views for Your Hospitality and Franchise Business

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Summer 2016

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Controversial Overtime Rule Comes in For a Landing

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After two years of wait, debate and overall angst for employers across the country, the new overtime rules were announced on May 18, 2016, and published in the Federal Register on May 23, 2016. As we discussed in an earlier [Hospitalitas article](#), this rule is going to have a tremendous impact on the hospitality industry, but there are some significant and positive changes in the final version of the rules that differ from the rule initially proposed by the Department of

Labor (DOL) last year. The most important news is that the Office of Management and Budget (OMB) listened to employers' concerns about the complexity of compliance and provided an extended period, until December 1, 2016, before the Final Rule becomes effective and employers are required to be in compliance.

Continued on page 2

What You Need to Know About Hospitality REITs

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In February 2016, Hilton Worldwide announced its plans to spin off the bulk of its hotel real estate into a publicly traded real estate investment trust (REIT) to be owned by its shareholders by the end of the year. The company's press release says the separation of the real estate from the hotel operations will allow management teams to fully activate their respective businesses, take advantage of growth opportunities and achieve tax and capital market efficiencies. The

Wall Street Journal described the spin-off transaction as "popular among companies looking to slim down and unlock value in their real estate holdings."

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The Legal Implications of Restaurant-Designed House Brand Craft Beers

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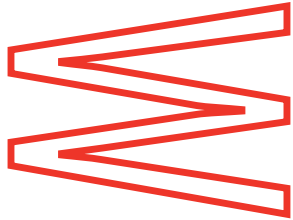
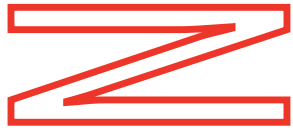
The craft beer industry has been growing at an unprecedented clip in the last few years. Breweries are opening up at an increasing pace throughout the United States as consumers skew more towards locally produced products and unique experiences. Not only is there a paradigm shift in consumer preference when it comes to beer, craft beer is having a profound impact on the culinary world.

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Greetings From Hospitalitas

Hospitalitas is the Baker Donelson newsletter for our clients and friends in the hospitality industry – hotels, restaurants and their suppliers. It is published several times a year when we believe we can deliver first-class, useful information for your business. [Please send us your feedback](#) and ideas for topics you would like to know more about. True to our Southern heritage of hospitality, we'll work hard to make each visit with us something special and worth repeating.



Controversial Overtime Rule Comes in For a Landing, *continued*



“Exemption” From Overtime

The Fair Labor Standards Act (FLSA), the federal wage law, requires employees to be paid at least the federal minimum wage and overtime for any time worked in excess of 40 hours in a workweek. In addition, the FLSA provides strict record-keeping requirements for employees to track their working hours. There are employees, however, who are “exempt” from the FLSA’s minimum wage, overtime and record-

keeping requirements. Exemption depends upon three things:

a) How An Employee Is Paid – Salary Basis

The first requirement for exemption is that the employee must be paid on a “salaried basis,” meaning the employee receives a fixed, guaranteed minimum amount for any workweek in which the employee performs any work. Simply stated, there is no change in salary regardless of the hours worked.

b) How Much An Employee Is Paid – Salary Level/Threshold

Besides being paid on a salary basis, to qualify for an exemption, the employee currently must be paid a minimum of \$23,600 per year (\$455 per week). There is also an exemption for “highly compensated employees” who earn \$100,000 per year.

c) The Kind of Work the Employee Does – Job Duties Test

An employee who meets the salary basis and salary level/threshold tests is exempt only if the employee also performs exempt job duties. There are three primary “white collar” exemptions: Executive, Administrative and Professional. Regardless of the job title, the employee must meet each job duty requirement under one of the exemption categories to satisfy this test.

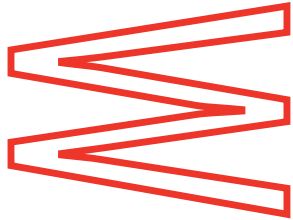
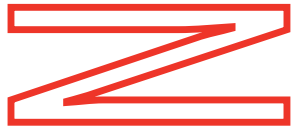
To qualify for exemption from overtime, all three of these tests must be satisfied. Paying salary alone is not enough. A salaried employee is not the same as an “exempt” employee, although the two phrases are often used interchangeably.

The Process – How Did We Get Here?

Back in March 2014, President Barack Obama sent an [executive memorandum](#) directing Secretary of Labor Thomas Perez to “modernize and streamline” the overtime exemption regulations. On June 30, 2015, the DOL published its proposed changes to the overtime regulations – more than doubling the \$23,660 salary level to \$50,440 (or \$970 per week) and increasing the salary level for the highly compensated exemption from \$100,000 to \$122,148. Additionally, the DOL proposed a mechanism to automatically update the salary level annually using a fixed percentile of wages or the Consumer Price Index. The DOL’s final regulation was sent to the OMB for review, which was completed on May 18, 2016. The Final Rule was published in the Federal Register shortly thereafter on May 23, 2016.

What is the Final Rule?

The salary threshold is still doubling so it is difficult to call this “good news,” but the Final Rule looks a bit different from the DOL’s proposed rule and contains some concessions that will make it a little more palatable for employers:



Controversial Overtime Rule Comes in For a Landing, *continued*

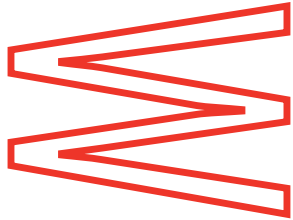
- The 2016 salary threshold will be \$913/week, which is \$47,476/year. This is \$2,964 less than the originally proposed \$50,440 salary threshold. The threshold will be based upon the 40th percentile of the lowest-wage region, currently the South, rather than the entire country as initially proposed. This change is likely the result of criticism the DOL received for basing its proposed rule on national statistics, which did not take into account regional salary fluctuations. For the highly compensated employee exemption (HCE), however, the DOL is still basing the new salary threshold on the weekly earnings of the 90th percentile of full-time salaried workers nationally, which will mean an increase in the HCE annual salary threshold from \$100,000 to \$134,004.
- One of the biggest concessions to employers in the hospitality industry is that bonuses and incentives (including commissions) can be included to satisfy up to 10 percent of the standard salary level (i.e. up to \$4,747 of the annual salary). For the first time, non-discretionary bonuses and incentives (including commissions – which is a shocker, since the DOL basically said no commissions in the proposed rule) can be included AND (also for the first time) the rule even allows employers to make a “catch up” payment. For employers to credit nondiscretionary bonuses and incentive payments toward a portion of the salary threshold, the Final Rule requires such payments to be paid on a quarterly or more frequent basis. If an employee does not earn enough in nondiscretionary bonuses and incentive payments (including commissions) in a given quarter to retain their exempt status, employers may make a lump-sum “catch-up” payment at the end of the quarter. The employer has one pay period to make up for the shortfall.
- The automatic updates will occur every three years beginning January 1, 2020. Rather than the initially proposed annual updates, the Final Rule provides for updates every three years. This will be based on the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage region, which is currently and will likely remain the South. The HCE will also be updated every three years based upon the 90th percentile, using the nationwide statistics. Based upon current trends, it is estimated the standard threshold will be approximately \$51,168 and the HCE \$147,524 in 2020.
- No changes to the duties test. There was some speculation that the DOL would revise the duties test in the Final Rule, but they did not touch them...but that doesn't mean they won't make changes to the test in the future.

When Will The Final Rule Be Effective?

The final rule was published in the Federal Register on May 23, 2016. Although, by law, the OMB was only required to give employers 60 days to comply, it extended the compliance date until December 1, 2016. Employers have between now and the end of November 2016 to get their affairs in order.

What Should The Hospitality Industry Do Now?

Every business sector is preparing for these changes, but the hospitality industry, in particular, should brace itself for impact. Wage and hour claims are old news for hospitality employers. The [National Economic Research Associates, Inc.](#) estimated that between January 2014 and March 2015, the food service industry accounted for 17 percent of all settlement dollars paid in wage-and-hour cases. Nevertheless, wage-and-hour litigation will only increase under the Final Rule as employers grapple



Controversial Overtime Rule Comes in For a Landing, *continued*

with the many positions in the industry just barely meeting the current threshold requirements, including assistant managers, housekeeping supervisors, back office administrators, sales employees, and catering staff.

So What Should You Do Now?

Here are some initial steps:

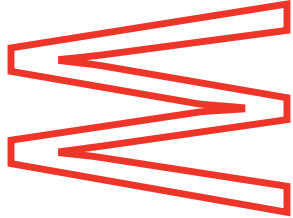
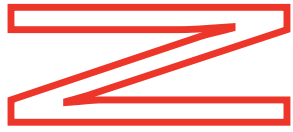
1. Identify employees who will need to be reclassified, i.e. employees who are currently exempt but paid less than \$47,476 annually.
2. Determine the number of hours the employee works. This seems simple but exempt employees are not required to track their hours and, therefore, employers may not be fully aware of the hours an exempt employee is working.
3. Analyze the financial impact. Will you raise pay to the new threshold level, reclassify employees as nonexempt and pay overtime, or lower pay to offset the overtime requirement?
4. Review job descriptions and tasks of impacted positions to determine if certain exempt tasks may be reassigned or maintained with the current position.
5. Consider how pay changes or other changes in job assignments may impact your organization. Will you need to make process or structural changes?
6. Develop administrative plans to ensure compliance when the regulations become official. This means you will need to prepare and train your managers.

Lastly, don't hesitate to seek legal help to ensure compliance and help maneuver through the DOL regulations and classification changes. These rules are complex, and there are serious financial consequences if you are found to be in violation of them. The DOL's budget for FY2017 includes \$277 million for wage and hour division enforcement, an increase of \$50 million from FY2016. Now that the rule is finalized, the DOL will send out its auditors to ensure employers are in compliance.

Hang on – it's going to be a bumpy ride.

What You Need to Know About Hospitality REITs, *continued*

In recent years, companies in various industries, including telecommunications, correctional institutions and gaming, have spun off their real estate holdings into REITs. After the spin-off, the core company leases the real estate back from the newly spun-off REIT. The core company can then concentrate its efforts on the core business, and the REIT can concentrate its efforts on the real estate business, in addition to having the tax advantages. These types of transactions are designed to be tax deferred and are extremely complicated and controversial, so much so that in December 2016, Congress passed and the President signed legislation that effectively prohibits future tax-deferred spin-offs of REITs from non-REIT companies. Hilton Worldwide is able to proceed with its spin-off because it had applied for a private letter ruling from the IRS prior to the effective date of the legislation.



What You Need to Know About Hospitality REITs, *continued*



So, what is a REIT and why is it suited to owning hotel properties? And what opportunities remain for hotel operators to “slim down and unlock value?”

REITs are creations of the tax law which allow smaller investors the opportunity to invest in large real estate projects that might otherwise be available only to wealthy and institutional investors. Although a

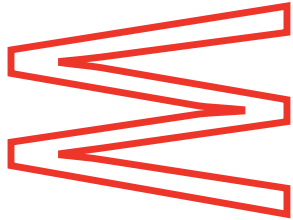
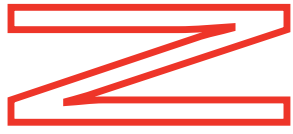
REIT would normally be taxed as a corporation, the tax law requires a REIT to distribute dividends of at least 90 percent of its ordinary taxable income annually and allows it to deduct those dividends from its taxable income. REITs use this dividends-paid deduction to essentially make it a non-taxable entity. Individual REITs generally specialize in holding properties of a certain character. For example, a REIT might specialize in hotel properties, office buildings, health care properties or apartment buildings. Some REITs’ stock is listed on a stock exchange. Other REITs may offer their stock in public offerings without being listed on an exchange. Still other REITs are privately-held (subject to certain ownership requirements).

Like many historic real estate deals structured as partnerships, generally only one level of federal income tax applies to the earnings of a REIT. Its shareholders are generally taxable at ordinary income rates (not the lower qualified dividends rate) on dividends received from the REIT. REITs (especially those owned more than 50 percent by U.S. shareholders) can also be an attractive investment for foreign investors seeking exposure to U.S. real estate.

In order to receive this favorable tax treatment, the tax law places a complicated web of restrictions on the nature of the income, assets and operations of a REIT. These restrictions seek to ensure that REITs are primarily investors in real estate, collecting “passive” types of income, generally rents and mortgage loan interest. A REIT will lose its tax-favored status if it has too much income from sources other than real estate assets, has too many non-real estate assets, holds ownership interests in non-REIT entities above relatively low levels or fails to distribute the required amounts of dividends to its shareholders. Because REITs must distribute their earnings annually to their shareholders, a REIT cannot finance growth through retained earnings. Instead, REITs actively raise capital in the securities markets to finance their growth.

Income derived from the operation of a hotel would not qualify as good REIT income for tax purposes. Therefore, a REIT that owns a hotel property needs another entity to operate the property. Conversely, hotel operators may want to expand without tying up available capital in real estate.

Although the spin-off technique announced by Hilton Worldwide is no longer available as a means to separate real estate from operations, hotel operators and REITs can continue to serve both their interests through the REIT’s development or funding of new construction, or the sale of hotel properties to the REIT and the leasing back of those properties by the hotel operator. In addition, REIT shareholders of all sizes can choose to invest in a hotel-oriented or other category of REIT without having to be at the table when the property is developed or purchased.



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What You Need to Know About Hospitality REITs, *continued*

The capital-raising experience of REITs, the limitations on a REIT's business operations and the capital needs of the hospitality industry combine nicely to make REITs attractive as a source of capital for the industry and an investment vehicle for investors of any size, foreign and domestic, to share in the earnings from hospitality properties.

The Legal Implications of Restaurant-Designed House Brand Craft Beers, *continued*



Chefs and restaurateurs are designing restaurant concepts and menus around craft beer and locally sourced products. Restaurants are now offering food and beer pairings in the same manner as they have historically offered food and wine pairings. Some restaurants are even employing bartenders and servers who have achieved some level of cicerone certification, the beer equivalent of attaining sommelier status in the wine world.

Restaurants are not only embracing and enhancing consumer education as it relates to beer; a growing trend with everyone from chef-driven restaurants to larger scale franchises is designing proprietary private label beverage products to offer patrons. The chef, in collaboration with a local brewery, specifically designs these house brand craft beers in order to provide the optimal pairing with the restaurant's food.

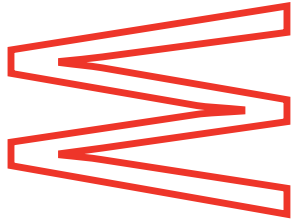
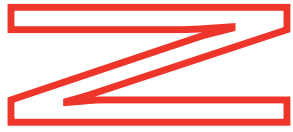
So, what exactly is a private label product? A private label product is generally some retail owned brand placed on a particular product that is manufactured by a third party. Traditionally, it has been a strategy implemented by large retailers and grocery store chains in order to gain access to a product market without having to incur the cost of manufacturing the product.

Large retailers and grocery stores have offered private label products in just about every imaginable product line as a means to compete with more premium products from a price perspective. Retailers such as Kroger and Trader Joe's have even started offering private label craft beers a few years ago.

Witnessing consumers trading up from more macro-produced beverage products to more craft-oriented products has provided the perfect opportunity for Kroger and Trader Joe's to move into the craft segment. Both have created house brand beers and contracted the manufacturing to a third-party beverage manufacturer with capacity. This white label structure has granted Kroger and Trader Joe's a relatively clear path to the craft beer consumer segment.

While the grocery store motivation behind white labeling craft beer is motivated more by providing a product at a competitive price, the white labeling of craft beer by restaurants is driven more by consumer experience.

The most prevalent example of white labeling craft beer by a restaurant is the manufacture of some seasonal or one-off beers, like a beer for an anniversary party or celebration. However, many restaurants are beginning to offer more regular house brands on a rotating tap.



Tennessee Hospitality & Tourism Law Symposium at Baker Donelson July 12

On July 12, Baker Donelson's Nashville office will host the Tennessee Hospitality & Tourism Association's Fifth Annual Law Symposium, a full day of substantive programming covering key legal issues and trends facing the hospitality industry. [Click here](#) for more information or to register.

The Legal Implications of Restaurant-Designed House Brand Craft Beers, *continued*



Evil Twin Brewing Company partnered with the Chef Daniel Humm of NoMad in Manhattan for a private label beer called NoMader Weisse. Chef Bryan Voltaggio, the proprietor of eight restaurants in the Washington, D.C., Maryland, and Virginia area, partnered with Flying Dog Brewery on a smoked beer called Backyard Ale.

Even here in the Southeastern United States, restaurants are collaborating with local breweries. James Beard-nominated Chef Jesse Houston, collaborated with Lucky Town Brewing Company to brew an oyster stout for his restaurant Saltine in Jackson, Mississippi.

So, what does the legal relationship look like when a retailer such as a restaurant wants to offer a house beer that is brewed by a brewery? You may be surprised to learn that due to regulatory reasons, the brewery manufacturing the house beer cannot sell it directly to the restaurant.

Generally, a private label manufacturing agreement governs the relationship between the restaurant and the brewery. Pursuant to this agreement, the brewery agrees to brew a proprietary beer for the restaurant. The parties need to address intellectual property issues, manufacturing quality control processes, brewing capacity, and other federal and state regulatory matters.

In most circumstances, the restaurant owns the intellectual property associated with the beer, but cannot take possession of the product until it passes through the three-tier system, the standard regulatory distribution system for almost every state in the United States.

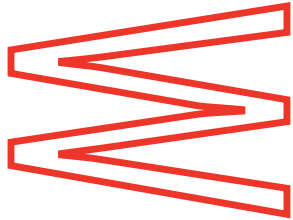
So, the chef or restaurateur needs to understand that there is usually another party to the transaction that is not necessarily a party to the private label manufacturing agreement and that is the brewery's distributor.

Creating house brand craft beers is a sound strategy for chefs and restaurateurs that want to stay on the front end of the craft beer curve, but these relationships trigger meaningful legal consequences. Before undertaking the process of collaborating with a local brewery, the restaurant owner should consider the myriad of related issues and make sure the agreement is reduced to an executed contract.

FDA Finalizes Revisions to Nutrition/Supplement Facts Labeling

[Kyle Diamantas](#), 407.367.5440, kdiamantas@bakerdonelson.com

On Friday, May 20, the United States Food and Drug Administration (FDA), an agency within the U.S. Department of Health and Human Services, announced its final revisions to the labeling requirements for conventional foods and dietary supplements. According to the FDA, the revisions are necessary to help consumers make informed choices about the food they purchase and consume.



Date Shift for July and October FBN Meetings

Scheduling conflicts have necessitated a date change for both the July and October IFA Franchise Business Network meetings which Baker Donelson hosts in Memphis, Nashville, Knoxville, New Orleans, Birmingham and Orlando. The July meeting will be on July 29, while the October meeting will be October 7. Both are lunch meetings which will run from 11:30 a.m. – 1 p.m. CST. As the IFA notes on its website, FBN attendees network with others in the franchise

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FDA Finalizes Revisions to Nutrition/Supplement Facts Labeling, *continued*



Among the changes to the nutrition facts label, which applies to packaged foods except certain meat, poultry and processed egg products, are: an updated design; increases in certain font sizes (primarily to highlight the prominence of “calories” and “servings”); revisions of “serving sizes” to more closely reflect the amounts of food that people actually eat per sitting; a declaration of grams and a percent daily value for “added sugars;” a dual column design to

indicate both “per serving” and “per package” caloric and other nutrition information for certain multi-serving food products; and a declaration of vitamin D and potassium that includes the actual gram amount in addition to the percent daily value amount. The content of vitamins A and C, a feature on existing nutrition facts labels, will no longer be required on the new nutrition facts label.

Additionally, for containers of foods between one and two servings, such as a 20-ounce soft drink, the caloric intake amount and display of other nutrients will be required to be stated as one serving because people typically consume it in one sitting. “Calories from Fat” will also be removed because, according to the FDA, the type of fat is more important than the amount. “Total Fat,” “Saturated Fat” and “Trans Fat” will continue to be required on the new nutrition facts label.

The FDA announced it is also making changes to the supplement facts label found on dietary supplements in order to make dietary supplement labeling consistent with the revisions to the nutrition facts label for conventional foods.

Manufacturers with \$10 million or more in annual food sales will be required to use the new nutrition facts label by July 26, 2018. Manufacturers with less than \$10 million in annual food sales will have until July 26, 2019, to comply.

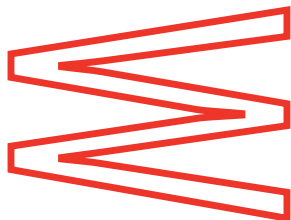
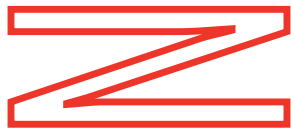
To read the FDA’s press release, [click here](#).

For more information about how these new regulations may affect your business or related matters, please contact [Kyle Diamantas](#) or any member of the Firm’s [FDA Group](#).

Some Tennessee Employers Will Be Required To Use E-Verify Starting 1/1/2017

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Starting January 1, 2017, all Tennessee employers with 50 or more employees will be required to use the E-Verify system in order to verify the employment eligibility of workers hired on or after that date. Currently, employers with six or more employees must either use E-Verify or request and retain certain documents from each employee. For employers with 50 or more employees, the new law will eliminate the document retention option in favor of mandatory E-Verify use.



Date Shift for July and October FBN Meetings, *continued*
community, meet potential customers and make new business contacts while taking advantage of educational programs and legislative information made available to them at no charge. If you are located in one of Baker Donelson's host markets and are interested in more information, or would like to suggest a topic or speaker for an upcoming meeting, please contact Laura Ellis at lellis@bakerdonelson.com or 615.726.5550.

Some Tennessee Employers Will Be Required To Use E-Verify Starting 1/1/2017, *continued*



As with similar laws in many states, the Tennessee law is not clear about which employers are covered by the requirement and the location of workers who trigger the E-Verify requirement. The definitions of “employer” and “employee” include no reference to location of either. The state’s web site on the law refers to “Tennessee employers” without defining that term, and says employees count “whether in Tennessee or outside of Tennessee.”

This new requirement results from a 2016 amendment to the Tennessee Lawful Employment Act of 2011. To see the newly enacted bill, [click here](#). For the web page of the Tennessee Department of Labor & Workforce Development relating to the law (not yet updated to reflect the new bill), [click here](#). For Baker Donelson’s alert about the original requirement when it was enacted in 2011, including a summary of penalty provisions still in effect, [click here](#).

News Briefs

Baker Donelson On Top Companies List Again



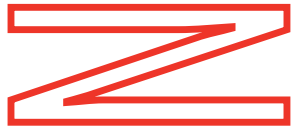
For the seventh consecutive year, Baker Donelson has been named one of Fortune’s 100 Best Companies to Work For®. The Firm is ranked 32nd on the prestigious list, which recognizes companies that have exceptional workplace cultures.

In naming Baker Donelson to the list, Fortune noted the Firm “balances hard work with a laid-back culture” and highlighted the Firm’s work providing legal advice to the homeless as well as its parental leave policy, which offers 16 weeks of paid leave for both male and female attorneys to take as primary caregivers and which also allows intermittent leave for both primary and non-primary caregiver attorneys.

Buckberg Named to Franchise Times “Legal Eagles Hall of Fame”



Joel R. Buckberg, leader of the Firm’s Commercial Transactions and Business Counseling Group and a co-chair of the Franchise and Hospitality Industry Service Team, has been inducted into the “Legal Eagles Hall of Fame” for being named to the “Legal Eagles” list ten consecutive years by *Franchise Times*, a national publication for franchisors and multi-unit franchisees.



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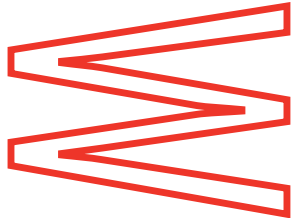
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News Briefs, *continued*



Buckberg Named to Franchise Times “Legal Eagles Hall of Fame”, *continued*

An annual listing that recognizes franchise law attorneys on the basis of input from their peers and clients, the “Legal Eagles” list includes leading franchise attorneys from across the country. To be included in the list, attorneys must be nominated by their peers or clients and must meet the criteria of the Franchise Times editorial panel. Attorneys who have been named to the list for ten years in a row are inducted into the “Legal Eagles Hall of Fame.” Mr. Buckberg is one of 11 inductees for 2016 and was featured in the April edition of the publication.



Matthew McLaughlin Recognized in Inaugural JD Supra “Readers’ Choice Awards”



Matthew P. McLaughlin has been recognized as a 2016 Readers’ Choice Award winner by JD Supra. Mr. McLaughlin is listed among the top ten authors nationwide in the Food & Beverage Industry for the excellent reach attained with readers through written contributions in 2015. JD Supra recognized a total of 200 top authors nationwide across 26 categories in their inaugural Readers’ Choice Awards.

Of counsel in Baker Donelson’s Jackson, Mississippi office, Mr. McLaughlin chairs the Firm’s craft brewery and craft distillery team, drawing on his experience working with regional craft breweries and craft distilleries in all aspects of their operations. He focuses his practice on corporate and business transactions including advising companies on corporate and commercial finance matters, economic development incentives and non-traditional sources of capital. Mr. McLaughlin has extensive industry experience which includes manufacturing, food and beverage, energy and technology sectors.



Baker Donelson and the Alabama Brewer’s Guild

Attorney Matthew McLaughlin will present two sessions at the Alabama Brewer’s Guild annual membership meeting in Nashville August 3-6. His topics include “From Startup to Expansion, Preparing Your Brewery or Distillery to Raise Capital” and “Trademark Primer and Best Practices.” More information is available at www.albeer.org.

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