DEPARTMENT OF LABOR

Wage and Hour Division

29 CFR Part 541

RIN 1235–AA20

Defining and Delimiting the Exemptions for Executive, Administrative, Professional, Outside Sales and Computer Employees

AGENCY: Wage and Hour Division, Department of Labor.

ACTION: Final rule.

SUMMARY: The Department of Labor is updating and revising the regulations issued under the Fair Labor Standards Act implementing the exemptions from minimum wage and overtime pay requirements for executive, administrative, professional, outside sales, and computer employees.

DATES: This final rule is effective on January 1, 2020.

FOR FURTHER INFORMATION CONTACT: Amy DeBisschop, Director, Division of Regulations, Legislation, and Interpretation, Wage and Hour Division, U.S. Department of Labor, Room S–3502, 200 Constitution Avenue NW, Washington, DC 20210; telephone: (202) 693–0406 (this is not a toll-free number). Copies of this final rule may be obtained in alternative formats (Large Print, Braille, Audio Tape or Disc), upon request, by calling (202) 693–0675 (this is not a toll-free number). TTY/TDD callers may dial toll-free 1–877–889–5627 to obtain information or request materials in alternative formats.

Questions of interpretation and/or enforcement of the agency's regulations may be directed to the nearest WHD district office. Locate the nearest office by calling WHD's toll-free help line at (866) 4US–WAGE ((866) 487–9243) between 8 a.m. and 5 p.m. in your local time zone, or log onto WHD's website for a nationwide listing of WHD district and area offices at *http://www.dol.gov/whd/america2.htm.*

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I. Executive Summary

The Fair Labor Standards Act (FLSA or Act) requires covered employers to pay employees a minimum wage and, for employees who work more than 40 hours in a week, overtime premium pay of at least 1.5 times the regular rate of pay. Section 13(a)(1) of the FLSA, commonly referred to as the ''white collar'' or ''EAP'' exemption, exempts from these minimum wage and overtime pay requirements ''any employee employed in a bona fide executive, administrative, or professional capacity.'' The statute delegates to the Secretary of Labor (Secretary) the authority to define and delimit the terms of the exemption. Since 1940, the regulations implementing the exemption have generally required each of the following three tests to be met: (1) The employee must be paid a predetermined and fixed salary that is not subject to reduction because of variations in the quality or quantity of work performed (the ''salary basis test''); (2) the amount of salary paid must meet a minimum specified amount (the ''salary level test''); and (3) the employee's job duties must primarily involve executive, administrative, or professional duties as defined by the regulations (the ''duties test'').

The Department of Labor (Department) has long used the salary level test as a tool to help define the white collar exemption on the basis that employees paid less than the salary level are unlikely to be bona fide executive, administrative, or professional employees, and, conversely, that nearly all bona fide executive, administrative, and professional employees are paid at least that much. The salary level test provides certainty for employers and employees, as well as efficiency for government enforcement agencies. The salary level test's usefulness, however, diminishes as the wages of employees entitled to overtime increase and inflation reduces the real value of the salary threshold.

The Department increased the standard salary level from $455 per week ($23,660 per year) to $913 per week ($47,476 per year) in a final rule published May 23, 2016 (''2016 final rule''). That rulemaking was challenged in court, and on November 22, 2016, the U.S. District Court for the Eastern District of Texas enjoined the Department from implementing and enforcing the rule. On August 31, 2017, the court granted summary judgment against the Department, invalidating the 2016 final rule because it ''makes overtime status depend predominately on a minimum salary level, thereby supplanting an analysis of an employee's job duties.'' *Nevada* v. *U.S. Dep't of Labor,* 275 F. Supp. 3d 795, 806 (E.D. Tex. 2017). An appeal of that decision to the U.S. Court of Appeals for the Fifth Circuit is being held in abeyance. Currently, the Department is enforcing the regulations in effect on November 30, 2016, including the $455 per week standard salary level, which is the level that was set in a final rule issued April 23, 2004 (''2004 final rule'').

Taking into account the *Nevada* district court's conclusion with respect to the salary level, public comments received in response to a July 26, 2017 Request for Information (RFI), and feedback received at public listening sessions, the Department has undertaken this rulemaking to revise the part 541 regulations so that they effectively distinguish between the white collar employees whom Congress intended to be protected by the FLSA's minimum wage and overtime provisions and bona fide executive, administrative, and professional employees whom Congress intended to exempt from those statutory requirements.

The Department published a Notice of Proposed Rulemaking (NPRM) on March 22, 2019. The NPRM stated that the standard salary level needed to exceed $455 per week to more effectively serve its purpose, but that the 2016 final rule's increase to $913 per week was inappropriate because it excluded from exemption 4.2 million employees whose duties would have otherwise qualified them for exemption, a result in significant tension with the text of section 13(a)(1). Noting the conclusions of the district court that invalidated the 2016 final rule, the Department explained that the 2016 final rule's inappropriately high salary level ''untethered the salary level test from its historical justification'' of ''[s]etting a dividing line between nonexempt and potentially exempt employees'' by screening out only those employees who, based on their compensation level, are unlikely to be bona fide executive, administrative, or professional employees. To address the district court's and the Department's concern with the 2016 final rule and set a more appropriate salary level, the NPRM proposed to rescind the 2016 final rule and update the salary level by applying the same methodology as the 2004 final rule to current earnings data.

In 2004, the Department set the standard salary level at $455 per week ($23,660 per year), which was approximately the 20th percentile of full-time salaried workers in the South and in the retail industry nationally.[1] Accordingly, in the NPRM, the Department proposed to update the standard salary level to the 20th percentile of full-time salaried workers in the lowest-wage Census Region (the South)[2] and/or in the retail industry nationally using current data.[3] This methodology resulted in a proposed standard salary level of $679 per week ($35,308 per year). Additionally, the Department proposed special salary levels for U.S. territories and an updated base rate for employees in the motion picture producing industry. The Department also proposed to allow employers to count nondiscretionary bonuses and incentive payments toward satisfying up to ten percent of the standard salary level or any of the special salary levels applicable to U.S. territories, so long as such bonuses are paid at least annually. Further, the Department proposed to update the highly compensated employee (HCE) total annual compensation level—a higher compensation level that is paired with a reduced duties requirement to provide an alternative basis for exemption under section 13(a)(1). The HCE level was set at $100,000 in the 2004 final rule and increased to $134,004 in the 2016 final rule, but the Department has continued to enforce the $100,000 level in light of the district court's invalidation of the 2016 final rule. In the NPRM, the Department proposed to update the HCE level by setting it equal to the annualized value of the 90th percentile of weekly earnings of full-time salaried workers nationally, resulting in a level of $147,414 per year. The Department proposed to project both the standard salary level and HCE total annual compensation level to January 2020, the final rule's anticipated effective date. Finally, the Department explained its commitment to update the standard salary level and HCE total compensation levels more frequently in the future using notice-and-comment rulemaking every four years. The Department proposed no changes to the standard duties tests.

The 60-day comment period on the NPRM ended on May 21, 2019, and the Department received more than 116,000 comments. The vast majority of these comments, including tens of thousands of duplicate or similar submissions, were campaign comments using similar template language.[4] After considering the comments, the Department has decided in this final rule to maintain the proposed methodology for updating the part 541 standard salary level, but not to inflate the salary level to January 2020. The Department is also finalizing the special salary levels for certain U.S. territories as proposed, and updating the base rate for employees in the motion picture producing industry. Additionally, the Department is finalizing its proposal to permit employers to count nondiscretionary bonuses, incentives, and commissions toward up to 10 percent of the standard salary level or the special salary levels applicable to the U.S. territories, so long as employers pay those amounts at least annually. The Department has also decided to set the HCE total annual compensation threshold equal to the 80th percentile of earnings of full-time salaried workers nationally, without inflating the threshold to January 2020. When applied to updated data, these methodologies result in a standard salary level of $684 per week ($35,568 per year) and an HCE total annual compensation level of $107,432. Finally, the Department intends to update these thresholds more regularly in the future.

The Department estimates that in 2020, 1.2 million currently exempt employees who earn at least $455 per week but less than the standard salary level of $684 per week will, without some intervening action by their employers, gain overtime eligibility. The Department also estimates that an additional 2.2 million white collar workers who are currently nonexempt because they do not satisfy the EAP duties tests and currently earn at least $455 per week, but less than $684 per week, will have their overtime-eligible status strengthened in 2020 because these employees will now fail both the salary level and duties tests. Lastly, an estimated 101,800 employees who are currently exempt under the HCE test will be affected by the increase in the HCE total annual compensation level. The Department has not made any changes to the duties tests in this final rule.

This rule is considered an Executive Order 13771 deregulatory action. When the Department uses a perpetual time horizon to allow for cost comparisons under Executive Order 13771, and using the 2016 rule as the baseline, the annualized cost savings of this rule is $534.8 million with 7 percent discounting.

Because the Department is currently enforcing the 2004 salary level, much of the economic analysis uses the 2004 rule as the baseline for calculating costs and transfers. The economic analysis

[1] 69 FR 22171.

[2] The South Census Region comprises the following: Alabama, Arkansas, Delaware, District of Columbia, Florida, Georgia, Kentucky, Louisiana, Maryland, Mississippi, North Carolina, Oklahoma, South Carolina, Tennessee, Texas, Virginia, and West Virginia.

[3] In 2004, the Department looked to the 20th percentile of full-time salaried workers in the South and in the retail industry nationally to validate the standard salary level set in the final rule. In this final rule, the Department set the standard salary level at the 20th percentile of the combined subpopulations of full-time salaried employees in the South and full-time salaried employees in the retail industry nationwide. Accordingly, the use of ''and/or'' when describing the salary level methodology in this final rule reflects that this data set includes full-time salaried workers who work: (1) In the South but not in the retail industry; (2) in the retail industry but not in the South; and (3) in the South in the retail industry.

[4] Specifically, one organization submitted spreadsheets containing over 56,000 comments from individuals. Of the comments contained in this submission, more than 34,000 were duplicates of comments that were submitted separately by these individuals. Additionally, numerous individual comments associated with this campaign were submitted multiple times. Together, these comments make up the vast majority of the comments received.

quantifies the direct costs resulting from the rule: (1) Regulatory familiarization costs; (2) adjustment costs; and (3) managerial costs. The Department estimates that annualized direct employer costs in the first 10 years following the rule's effective date will be $173.3 million with 7 percent discounting, including $543.0 million in Year 1 and $99.1 million in Year 10. This rulemaking will also give employees higher earnings in the form of transfers of income from employers to employees. Annualized transfers are estimated to be $298.8 million over the first ten years, with 7 percent discounting, including $396.4 million in Year 1.

II. Background

A. The FLSA

The FLSA generally requires covered employers to pay their employees at least the federal minimum wage (currently $7.25 an hour) for all hours worked, and overtime premium pay of at least 1.5 times the regular rate of pay for all hours worked over 40 in a workweek.[5] However, there are a number of exemptions from the FLSA's minimum wage and overtime requirements. Section 13(a)(1) of the FLSA, codified at 29 U.S.C. 213(a)(1), exempts from both minimum wage and overtime protection ''any employee employed in a bona fide executive, administrative, or professional capacity . . . or in the capacity of outside salesman (as such terms are defined and delimited from time to time by regulations of the Secretary, subject to the provisions of [the Administrative Procedure Act] . . .).'' The FLSA does not define the terms ''executive,'' ''administrative,'' ''professional,'' or ''outside salesman.'' Pursuant to Congress's grant of rulemaking authority, since 1938 the Department has issued regulations at 29 CFR part 541 defining the scope of the section 13(a)(1) exemptions. Because Congress explicitly delegated to the Secretary the power to define and delimit the specific terms of the exemptions through notice and comment rulemaking, the regulations so issued have the binding effect of law. *See Batterton* v. *Francis,* 432 U.S. 416, 425 n.9 (1977).

Employees who meet the requirements of part 541 are not subject to the FLSA's minimum wage and overtime pay requirements. Some state laws have stricter exemption standards than federal law. The FLSA does not preempt any such stricter state standards. If a State establishes a higher standard than the provisions of the FLSA, the higher standard applies in that State. *See* 29 U.S.C. 218(a); 29 CFR 541.4.

B. Regulatory History

The Department has consistently used its rulemaking authority to define and clarify the section 13(a)(1) exemptions. The implementing regulations have generally required each of three tests to be met for the exemptions to apply: (1) The salary basis test; (2) the salary level test; and (3) the duties test.

The first version of part 541, establishing the criteria for exempt status under section 13(a)(1), was promulgated in October 1938.[6] The Department revised its regulations in 1940,[7] 1949,[8] 1954, 1958,[9] 1961, 1963, 1967, 1970, 1973, and 1975.[10] A final rule increasing the salary levels was published on January 13, 1981, but was stayed indefinitely on February 12, 1981.[11] In 1985, the Department published an Advance Notice of Proposed Rulemaking that was never finalized.[12] In 1992, the Department twice revised the part 541 regulations. First, the Department created a limited exception from the salary basis test for public employees.[13] The Department then implemented the 1990 law exempting employees in certain computer-related occupations.[14]

From 1949 until 2004, the part 541 regulations contained two different tests for exemption—a ''long'' test that paired a more rigorous duties test with a lower salary level, and a ''short'' test that paired a more flexible duties test with a higher salary level. On April 23, 2004, the Department issued a final rule, which replaced the ''long'' and ''short'' test system for determining exemption status with a single ''standard'' salary level paired with a ''standard'' duties test.[15] The Department set the standard salary level at $455 per week, and made other changes, some of which are discussed below. In the 2004 final rule, the Department also created the HCE test for exemption, which paired a reduced duties requirement with a higher compensation level ($100,000 per year).

On May 23, 2016, the Department issued another final rule, which raised the standard salary level to the 40th percentile of earnings of full-time salaried workers in the lowest-wage Census Region, resulting in a salary level of $913 per week. Additionally, the Department set the HCE total annual compensation level equal to the 90th percentile of earnings of full-time salaried workers nationally ($134,004 annually). The Department also included in the final rule a mechanism to automatically update (every three years) the salary and compensation thresholds, and for the first time permitted nondiscretionary bonuses, incentives, and commissions paid at least quarterly to count toward up to 10 percent of the required salary level.

On November 22, 2016, the United States District Court for the Eastern District of Texas issued a preliminary injunction, enjoining the Department from implementing and enforcing the 2016 final rule, pending further review.[16] On August 31, 2017, the district court granted summary judgment against the Department.[17] The court held that the 2016 final rule's salary level exceeded the Department's authority and that the entire final rule was therefore invalid. The court determined that a salary level that ''supplant[s] an analysis of an employee's job duties'' conflicts with Congress's command to exempt bona fide executive, administrative, and professional employees.[18] As a result of these rulings, the Department has continued to enforce the salary level set in 2004.

On July 26, 2017, the Department published an RFI asking for public input

[5] 29 U.S.C. 201, *et seq.*

[6] 3 FR 2518 (Oct. 20, 1938).

[7] 5 FR 4077 (Oct. 15, 1940). The 1940 regulations were informed by what has come to be known as the Stein Report. *See* ''Executive, Administrative, Professional . . . Outside Salesman'' Redefined, Wage and Hour Division, U.S. Department of Labor, Report and Recommendations of the Presiding Officer [Harold Stein] at Hearings Preliminary to Redefinition (Oct. 10, 1940) (''Stein Report'').

[8] 14 FR 7705 (Dec. 24, 1949); 14 FR 7730 (Dec. 28, 1949). The 1949 regulations were informed by what has come to be known as the Weiss Report. *See* Report and Recommendations on Proposed Revisions of Regulations, Part 541, by Harry Weiss, Presiding Officer, Wage and Hour and Public Contracts Divisions, U.S. Department of Labor (June 30, 1949) (''Weiss Report'').

[9] 23 FR 8962 (Nov. 18, 1958). The 1958 regulations were informed by what has come to be known at the Kantor Report. *See* Report and Recommendations on Proposed Revision of Regulations, Part 541, Under the Fair Labor Standards Act, by Harry S. Kantor, Assistant Administrator, Office of Regulations and Research, Wage and Hour and Public Contracts Divisions, U.S. Department of Labor (Mar. 3, 1958) (''Kantor Report'').

[10] *See* 19 FR 4405 (July 17, 1954); 26 FR 8635 (Sept. 15, 1961); 28 FR 9505 (Aug. 30, 1963); 32 FR 7823 (May 30, 1967); 35 FR 883 (Jan. 22, 1970); 38 FR 11390 (May 7, 1973); 40 FR 7091 (Feb. 19, 1975).

[11] 46 FR 3010 (Jan. 13, 1981); 46 FR 11972 (Feb. 12, 1981).

[12] 50 FR 47696 (Nov. 19, 1985).

[13] 57 FR 37677 (Aug. 19, 1992).

[14] 57 FR 46742 (Oct. 9, 1992); *see* Sec. 2, Pub. L. 101–583, 104 Stat. 2871 (Nov. 15, 1990), *codified at* 29 U.S.C. 213 Note.

[15] 69 FR 22122 (Apr. 23, 2004).

[16] *See Nevada* v. *U.S. Dep't of Labor,* 218 F. Supp. 3d 520 (E.D. Tex. 2016).

[17] *See* 275 F. Supp. 3d 795.

[18] *Id.* at 806.

on what changes the Department should propose in a new NPRM on the EAP exemption.[19] The Department received over 200,000 comments on the RFI. Between September 7 and October 17, 2018, the Department held listening sessions in all five Wage and Hour regions throughout the country, and in Washington, DC, to supplement feedback received as part of the RFI.[20]

On October 30, 2017, the Government appealed the *Nevada* district court's summary judgment decision to the United States Court of Appeals for the Fifth Circuit. On November 6, 2017, the Fifth Circuit granted the Government's motion to hold that appeal in abeyance while the Department undertook further rulemaking to set a new salary level.

On March 22, 2019, the Department issued its NPRM, proposing to update and revise the EAP regulations.

C. Overview of Existing Regulatory Requirements

The regulations in 29 CFR part 541 contain specific criteria that define each category of exemption provided by section 13(a)(1) for bona fide executive, administrative, professional, and outside sales employees, as well as teachers and academic administrative personnel. The regulations also define those computer employees who are exempt under section 13(a)(1) and section 13(a)(17). The employer bears the burden of establishing the applicability of any exemption from the FLSA's pay requirements.[21] Job titles, job descriptions, or the payment of a salary instead of an hourly rate are insufficient, standing alone, to confer exempt status on an employee.

To qualify for the EAP exemption, employees must meet certain tests regarding their job duties [22] and generally must be paid on a salary basis at least the amount specified in the regulations.[23] Some employees, such as business owners, doctors, lawyers, teachers, and outside sales employees, are not subject to salary tests.[24] Others, such as academic administrative personnel and computer employees, are subject to special, contingent earnings thresholds.[25] In 2004, the standard salary level for EAP employees was set at $455 per week (equivalent to $23,660 per year for a full-year worker), and the total annual compensation level for highly compensated employees was set at $100,000.[26] Due to the district court's decision invalidating the 2016 final rule, these are the salary levels the Department is currently enforcing.[27]

The 2004 final rule created the HCE test for exemption. Under the HCE test, employees who receive at least a specified total annual compensation (which must include at least the standard salary amount per week paid on a salary or fee basis) are exempt from the FLSA's overtime requirements if they customarily and regularly perform at least one of the exempt duties or responsibilities of an executive, administrative, or professional employee identified in the standard tests for exemption.[28] The HCE test applies only to employees whose primary duty includes performing office or non-manual work.[29] Non-management production line workers and employees who perform work involving repetitive operations with their hands, physical skill, and energy cannot be exempt under this section.[30]

D. The Department's Proposal

On March 22, 2019, the Department issued its proposal to update and revise the regulations issued under section 13(a)(1) of the FLSA.[31] The Department proposed to update the standard salary level by applying to current data the same method as in the 2004 final rule—*i.e.,* by looking at the 20th percentile of earnings of full-time salaried workers in the lowest-wage Census Region (then and now the South) and/or in the retail industry nationwide. The Department also proposed to update the HCE total annual compensation level using the same method used in the 2016 final rule, setting it equivalent to the 90th percentile earnings of full-time salaried workers nationally. The Department proposed to project both levels to January 2020, the anticipated effective date of a final rule. Additionally, the Department proposed a special salary level of $380 per week for American Samoa, a special salary level of $455 per week for Puerto Rico, the U.S. Virgin Islands, Guam, and the Commonwealth of the Northern Mariana Islands, and a special ''base rate'' threshold of $1,036 for employees in the motion picture producing industry. The Department also proposed to permit employers to use nondiscretionary bonuses and incentive payments to satisfy up to 10 percent of the standard or special salary levels as long as such payments are made at least annually. As to future updates, the Department reaffirmed its commitment to evaluating the part 541 earnings thresholds more frequently, and stated its intent to propose updates to these levels quadrennially. The Department did not propose any changes to the duties tests.

The Department received more than 116,000 timely comments on the NPRM during the 60-day comment period that ended on May 21, 2019. The Department received comments from a broad array of constituencies, including small business owners, employer and industry associations, individual workers, worker advocacy groups, unions, non-profit organizations, law firms (representing both employers and employees), educational organizations and representatives, religious organizations, economists, Members of Congress, state and local governments, professional associations, and other interested members of the public. All timely received comments may be viewed on the *http://www.regulations.gov* website, docket ID WHD–2019–0001.

Some of the comments the Department received were general statements of support or opposition, and the Department also received many identical or nearly identical ''campaign'' comments sent in response to organized comment initiatives. Nearly all commenters favored some change to the currently enforced regulations, and commenters expressed a wide variety of views on the merits of particular aspects of the Department's proposal. Some commenters, including tens of thousands who submitted similar comments as part of a comment

[19] 82 FR 34616 (July 26, 2017).

[20] Listening Session transcripts may be viewed at *www.regulations.gov,* docket ID WHD–2017–0002.

[21] *See, e.g., Idaho Sheet Metal Works, Inc.* v. *Wirtz,* 383 U.S. 190, 209 (1966); *Walling* v. *Gen. Indus. Co.,* 330 U.S. 545, 547–48 (1947).

[22] *See* §§ 541.100 (executive employees); 541.200 (administrative employees); 541.300–.303 (teachers and professional employees); 541.400 (computer employees); 541.500 (outside sales employees).

[23] Alternatively, administrative and professional employees may be paid on a ''fee basis'' for a single job regardless of the time required for its completion as long as the hourly rate for work performed (*i.e.,* the fee payment divided by the number of hours worked) would total at least the weekly amount specified in the regulation if the employee worked 40 hours. *See* § 541.605.

[24] *See* §§ 541.101; 541.303(d); 541.304(d); 541.500(c); 541.600(e). Such employees are also not subject to a fee-basis test.

[25] *See* § 541.600(c)–(d).

[26] 69 FR 22123.

[27] The current text of the Code of Federal Regulations (CFR) reflects the updates made in the 2016 final rule. Therefore, unless otherwise indicated, citations to part 541 refer to the current CFR, and the amendments to the regulatory text reflect the current CFR's inclusion of the 2016 updates. However, because the Department is currently enforcing the 2004 standard salary and total annual compensation levels, the final rule references the 2004 standard salary and total annual compensation levels.

[28] § 541.601.

[29] § 541.601(d).

[30] *Id.*

[31] 84 FR 10900.

campaign (''Campaign Comments''),[32] requested that the Department reject the proposal and defend the 2016 final rule. The Department has carefully considered the timely submitted comments addressing the proposed changes.

Significant issues raised in the comments are discussed below, along with the Department's responses to those comments. Some commenters appear to have mistakenly filed comments intended for this rulemaking into the dockets for the Department's rulemakings concerning the regular rate (docket ID WHD–2019–0002) or joint employer status (docket ID WHD–2019–0003) under the FLSA. The Department did not consider these misfiled comments in this rulemaking.

The Department received a number of comments that are beyond the scope of this rulemaking. These include, for example, a request that the Department reconsider the scope of the exemption at 29 U.S.C. 207(i) for certain employees of retail and service establishments, and a request for tax write-offs for businesses that pass an annual audit by the Department. In addition, some non-profit organizations asked the Department to work with other federal agencies to create a mechanism that non-profits with government grants and contracts could use to adjust reimbursement rates to cover unanticipated increased costs, such as labor costs due to this rule. For example, in a joint comment, the National Council of Nonprofits and others recommended addressing this issue through changes to the relevant Federal Acquisition Regulations. The Department does not address such issues in this final rule.

Some commenters raised miscellaneous issues that more directly relate to other parts of the Department's regulations. For example, one commenter urged the Department to amend its regular rate regulations to allow the exclusion of any payments that do not count toward the salary level test; one commenter requested that private colleges and universities be permitted to use compensatory time off instead of cash payments for overtime hours; two commenters requested a safe harbor from joint-employment liability for franchisors who help their franchisees implement this rule; and one commenter asked the Department to permit hourly paid employees (beyond just computer employees) to qualify for the exemption. Some commenters requested that the Department make changes to the duties test, either as an alternative to raising the salary level more significantly or regardless of what salary level applies. The Department did not propose any of these changes in the NPRM, and declines to make such changes in this final rule.

A number of commenters asked the Department to provide guidance on how the FLSA applies to non-profit organizations. *See, e.g.,* Colorado Nonprofit Association; Independent Sector; National Council of Nonprofits. The Department notes that the FLSA does not provide special rules for non-profit organizations or their employees, nor does this final rule.[33]

E. Final Rule Effective Date

In the NPRM, the Department referenced an anticipated effective date of January 2020 for purposes of projecting forward the proposed standard salary level and proposed HCE total annual compensation level. Many commenters, while not expressly referencing the effective date, conveyed their view that updates to these regulations are ''long overdue.'' *See, e.g.,* Legal Aid at Work; Public Housing Authorities Directors Association; Washington State Budget and Policy Center. Similarly, a few commenters encouraged the Department to increase the standard salary threshold, or to promulgate a final rule, ''as soon as possible.'' *See, e.g.,* International Foodservice Distributors Association; Sergeants Benevolent Association.

Other commenters did specifically address the final rule's effective date. Nearly all of these commenters conveyed the need for employers to have sufficient time to adjust to and implement the rule, but they disagreed on how much time the Department should provide. The National Association of Landscape Professionals favored a period of 90 to 120 days between the rule's publication and its effective date, while several other commenters favored a minimum of 120 days, which was the applicable period of time in the 2004 final rule. *See, e.g.,* Seyfarth Shaw LLP (Seyfarth Shaw); Society for Human Resource Management (SHRM). SHRM thought the effective date should be at least 120 days from the date of publication of the final rule, but acknowledged that the proposed regulations are far more familiar to employers than the changes made in 2004. Other commenters favored a longer period, ranging from six to eighteen months from publication. The U.S. Public Interest Research Group suggested a two-year delay for public interest advocacy groups. Several employer representatives who opposed the proposed HCE level stated that adjusting to the new level would be particularly burdensome. For example, the National Association of Manufacturers stated that the proposed increase would require employers to spend significant time determining whether employees who previously met the HCE test satisfy the standard duties test (and thus remain exempt), and requested that if the Department were to finalize that increase as proposed, it should set a future compliance date that provides sufficient time for employers to adjust to the new HCE level.

Relatedly, multiple commenters requested that the Department ''phase in'' any new salary/compensation levels over a period of time. Suggested phase-in periods varied widely. Independent Sector and the National Council of Young Men's Christian Associations of the United States of America (YMCA) favored a two-year phase-in period. An individual employee commenter proposed a 3- to 5-year phase-in period for non-profit organizations. Some commenters who requested a phase-in period did not specify a particular timeframe. Many commenters who supported a phase-in cited the importance of providing sufficient time for employers to adapt to and implement the new levels. *See, e.g.,* Lutheran Services in America; National Grocers Association (NGA).

The Department has set an effective date of January 1, 2020, for the final rule. The Department agrees with the commenters who expressed the view that this update to the regulations is ''long overdue,'' and with those who encouraged the Department to increase the salary level as soon as possible. The time between this rule's publication and effective date exceeds the 30-day minimum required under the Administrative Procedure Act (APA), 5 U.S.C. 553(d), and the 60 days mandated for a ''major rule'' under the Congressional Review Act, 5 U.S.C. 801(a)(3)(A). While the 2004 rule provided for 120 days between the rule's publication and effective date,[34] the Department agrees with commenters who acknowledged that this final rule will be far more familiar to employers than the substantial changes provided in the 2004 final rule.[35]

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32 *See supra* note 4.

33 The Department has issued specific guidance on the application of the FLSA to non-profit entities. *See* Fact Sheet #14A: Non-Profit Organizations and the Fair Labor Standards Act (FLSA), available at: *https://www.dol.gov/whd/regs/compliance/whdfs14a.pdf.*

34 *See* 79 FR 22126.

35 The 2004 final rule included several significant changes, including: (1) A significant percentage increase in the salary threshold; (2) a significant

Additionally, while the 2016 rule provided 192 days from the rule's publication until its effective date, the salary level increase in this rule is more modest, and affects fewer workers—two factors that favor a shorter period. Moreover, given that the Department is currently enforcing the 2004 standard salary level, which an overwhelming majority of commenters agreed needs to be updated, the Department concludes that a lengthier delayed effective date would be imprudent. Additionally, a January 1 date may be convenient for those employers who use the calendar year as their fiscal year, or who use budgets, software systems, or other practices on a calendar-year basis. The Department is also declining to delay the effective date, or create a phase-in, specifically for non-profits. As discussed in more detail in the standard salary level discussion below, consistent with past practice, the Department is declining to create special rules for the application of the part 541 exemptions to non-profits.

While some employer representatives expressed concern that the proposed HCE level increase would pose unique challenges for employers compared to the change to the standard salary level, given the change in methodology for setting the HCE threshold in the final rule, discussed in further detail below, the Department does not believe a delayed effective date for this provision is necessary. The Department believes that the January 1, 2020 effective date will provide employers adequate time to make any changes that are necessary to comply with the final regulations, and for similar reasons concludes that a phase-in of the new thresholds is not warranted. The Department will also provide significant outreach and compliance assistance, and will issue a number of guidance documents in connection with the publication of this final rule.

III. Need for Rulemaking

The primary goal of this rulemaking is to update the standard salary level that helps define and delimit the EAP exemption. This will ensure that the level works effectively with the standard duties test to distinguish potentially exempt EAP employees from overtime-protected white collar workers. Due to the *Nevada* district court's decision invalidating the 2016 final rule, the Department has been enforcing the standard salary level of $455 a week. The Department recognizes that this level should be updated to reflect current earnings. In the NPRM, the Department proposed using the methodology from the 2004 final rule to calculate the salary threshold using current data. The Department explained that this method would keep the standard salary level aligned with the intervening years' growth in earnings. It further stated that the 2004 approach has withstood the test of time, would restore the salary level to its traditional purpose of serving as a dividing line between nonexempt and potentially exempt employees, would address concerns that led to the 2016 rule's invalidation, and would ensure that the FLSA's intended overtime protections are fully implemented.

The Department is also updating the total annual compensation requirement for the HCE test for exemption to ensure that this threshold remains a meaningful and appropriate standard when paired with the more-lenient HCE duties test. In an effort to modernize the part 541 regulations to account for changing methods of workplace compensation, the Department also proposed allowing nondiscretionary bonuses and incentive payments (including commissions) to count toward up to 10 percent of the standard or special salary levels. Finally, in its proposal the Department explained the importance of updating the salary thresholds more frequently. Regular updates promote greater stability, avoid the disruptive salary level increases that can result from lengthy gaps between updates, and provide appropriate wage protection for those under the threshold. With these goals in mind, in the NPRM, the Department affirmed its intention to issue a proposal to update the earnings thresholds every four years, unless the Secretary determines that economic or other factors warrant forestalling such an update.

IV. Final Regulatory Revisions

The Department is formally rescinding the 2016 final rule and is replacing it with a new rule that updates the part 541 earnings thresholds. The Department is setting the standard salary level by applying the methodology from the 2004 final rule to current data, resulting in a new standard salary level of $684 per week. In addition, the Department is setting a special salary level of $455 per week for Puerto Rico, the U.S. Virgin Islands, Guam, and the Commonwealth of the Northern Mariana Islands; a special salary level of $380 per week for American Samoa; and an updated weekly ''base rate'' of $1,043 per week for the motion picture producing industry. Nondiscretionary bonuses and incentive payments (including commissions) paid on an annual or more frequent basis may be used to satisfy up to 10 percent of the standard salary level or the special salary levels applicable to the U.S. territories. The Department is also setting the HCE annual compensation amount at the 80th percentile of full-time salaried workers nationally, resulting in a new HCE level of $107,432. These revisions are discussed in further detail below.

A. Standard Salary Level

i. History of the Standard Salary Level

Congress enacted the FLSA on June 25, 1938, and the first version of part 541, which the Department issued in October 1938, set a salary level of $30 per week for executive and administrative employees.[36] The Department updated the salary levels in 1940, maintaining the salary level for executive employees, increasing the salary level for administrative employees, and establishing a salary level for professional employees. In setting those rates, the Department considered surveys of private industry by federal and state government agencies, experience gained under the National Industrial Recovery Act, and Federal Government salaries to identify a salary level that reflected a reasonable ''dividing line'' between employees performing exempt and nonexempt work.[37] Taking into account salaries paid in numerous industries and the percentage of employees earning below these amounts, the Department set the salary level for each exemption slightly below the average salary dividing exempt and nonexempt employees.

In 1949, the Department evaluated salary data from state and federal agencies, including the Bureau of Labor Statistics (BLS). The Department considered wages in small towns and low-wage industries, wages of federal employees, average weekly earnings for exempt employees, starting salaries for college graduates, and salary ranges for different occupations such as bookkeepers, accountants, chemists, and mining engineers.[38] The Department also looked at data showing increases in exempt employee salaries since 1940,

reorganization of the part 541 regulations; (3) the elimination of the short and long test structure that had been in place for more than 50 years and the creation of a single standard test; and (4) the creation of a new test for highly compensated employees. In contrast, here the Department is not changing the standard duties test or reorganizing the regulations, and so this rule will be much less complicated for employers to implement.

[36] 3 FR 2518.

[37] Stein Report at 9, 20–21, 30–31.

[38] Weiss Report at 10, 14–17, 19–20.

and supplemented it with nonexempt employee earnings data to approximate the ''prevailing minimum salaries of exempt employees.'' [39] Recognizing that the ''increase in wage rates and salary levels'' since 1940 had ''gradually weakened the effectiveness of the present salary tests as a dividing line between exempt and nonexempt employees,'' the Department considered the increase in weekly earnings from 1940 to 1949 for various industries, and then adopted new salary levels at a ''figure slightly lower than might be indicated by the data'' to protect small businesses.[40] Also in 1949, the Department established a second, less-stringent duties test for each exemption, which applied to employees paid at or above a higher ''short test'' salary level. The original, more-rigorous duties test became known as the ''long test.'' Apart from the differing salary requirements, the most significant difference between the short test and the long test was that the long test limited the amount of time an exempt employee could spend on nonexempt duties, while the short duties test did not include a specific limit on nonexempt work.[41]

In 1958, the Department set the long test salary levels using data collected by WHD on salaries paid to employees who met the applicable salary and duties tests, grouped by geographic region, broad industry groups, number of employees, and city size, and supplemented with BLS and Census data to reflect income increases for white collar and manufacturing employees during the period not covered by the Department's investigations.[42] The Department then set the long test salary levels for exempt employees ''at about the levels at which no more than about 10 percent of those in the lowest-wage region, or in the smallest size establishment group, or in the smallest-sized city group, or in the lowest-wage industry of each of the categories would fail to meet the tests.'' [43] Thus, the Department set the long test salary levels so that about 10 percent of workers performing EAP duties in the lowest-wage regions and industries would not meet the salary level test and would therefore be nonexempt based on their salary level alone.

The Department followed a similar methodology when determining the salary level increase in 1963. The Department examined data on salaries paid to exempt workers collected in a 1961 WHD survey.[44] The salary level for executive and administrative employees was increased to $100 per week, for example, when the 1961 survey data showed that 13 percent of establishments paid one or more exempt executives less than $100 per week, and 4 percent of establishments paid one or more exempt administrative employees less than $100 per week.[45] The professional salary level was increased to $115 per week when the 1961 survey data showed that 12 percent of establishments surveyed paid one or more professional employees less than $115 per week.[46] The Department noted that these salary levels approximated the same percentages used to update the salary level in 1958.[47]

The Department applied a similar methodology when adopting salary level increases in 1970. After examining data from WHD investigations, BLS wage data, and information provided in a report issued by the Department in 1969 that included salary data for executive, administrative, and professional employees, the Department increased the long test salary level for executive employees to $125 per week when the salary level data showed that 20 percent of executive employees from all regions and 12 percent of executive employees in the West earned less than $130 a week.[48] The Department also increased the long test salary levels for administrative and professional employees to $125 and $140 per week, respectively.

In 1975, rather than follow the prior approaches, the Department updated the 1970 salary levels based on increases in the Consumer Price Index, but adjusted downward ''to eliminate any inflationary impact.'' [49] This resulted in a long test salary level for the executive and administrative exemptions of $155 per week, and $170 per week for the professional exemption. The short test salary level increased to $250 per week in 1975.[50] The salary levels adopted were intended as interim levels ''pending the completion and analysis of a study by [BLS] covering a six-month period in 1975.'' [51] Although the Department intended to increase the salary levels based on that study of actual salaries paid to employees, the process was never completed, and the ''interim'' salary levels remained in effect for the next 29 years.

In 2004, the Department replaced the separate long and short tests with a single ''standard'' salary level test of $455 per week, which was paired with a ''standard'' duties test for executive, administrative, and professional employees, respectively. The Department noted, in accord with numerous comments received during that rulemaking, that as a result of the outdated salary level, ''the 'long' duties tests [had], as a practical matter, become effectively dormant'' because relatively few salaried employees earned below the short test salary level.[52] The Department estimated that 1.3 million workers earning between $155 and $455 per week would become nonexempt under the new standard salary level.[53]

In setting the new standard salary level in 2004, the Department used Current Population Survey (CPS) Merged Outgoing Rotation Group (MORG) data collected by BLS that encompassed most salaried employees, including nonexempt salaried employees. The Department selected a standard salary level of $455 per week, which at the time was roughly equivalent to earnings at the 20th percentile of two subpopulations: (1) Salaried employees in the South and (2) salaried employees in the retail industry nationwide. Although prior salary levels had been based on salaries of approximately the lowest 10 percent of exempt salaried employees in low-wage regions and industries, the Department explained that the change in methodology was warranted in part to account for the elimination of the short and long tests, and because the data sample included nonexempt salaried employees, as opposed to only exempt salaried employees.[54] As in the past, the Department used lower-salary data sets to accommodate businesses for which salaries were generally lower due to geographic- or industry-specific reasons.

[39] *Id.* at 12.

[40] *Id.* at 8, 14–20. The Department also justified its modest increases by noting evidence of slow wage growth for executive employees ''in some areas and some industries.'' *Id.* at 14.

[41] The Department instituted a 20 percent cap on nonexempt work as part of the long duties test for executive and professional employees in 1940, and for administrative employees in 1949. By statute, beginning in 1961, retail employees could spend up to 40 percent of their hours worked performing nonexempt work and still be found to meet the duties tests for the EAP exemption. *See* 29 U.S.C. 213(a)(1).

[42] Kantor Report at 6.

[43] *Id.* at 6–7.

[44] 28 FR 7002 (July 9, 1963).

[45] *Id.* at 7004.

[46] *Id.*

[47] *See id.*

[48] 35 FR 884–85.

[49] 40 FR 7091.

[50] *Id.* at 7092. Each time the short test was increased between 1949 and 1975, it was set significantly higher than the long test salary levels.

[51] *Id.* at 7091.

[52] 69 FR 22126.

[53] *Id.* at 22123.

[54] *Id.* at 22167.

The Department published a final rule updating the salary level twelve years later, in 2016.[55] The Department set the standard salary level at an amount that would exclude from exemption the bottom 40 percent of full-time salaried workers (exempt and nonexempt) in the lowest-wage Census Region (the South).[56] The Department estimated that increasing the standard salary level from $455 per week to $913 per week would make 4.2 million workers earning between those levels newly nonexempt, absent other changes by their employers.[57] The Department made no changes to the standard duties test. As previously discussed, on August 31, 2017, the U.S. District Court for Eastern District of Texas declared the 2016 final rule invalid, and the Department's appeal of that decision is being held in abeyance. Until the Department issues a new final rule, it is enforcing the part 541 regulations in effect on November 30, 2016, including the $455 per week standard salary level.

ii. Purpose of the Salary Level Requirement

The FLSA states that its minimum wage and overtime requirements ''shall not apply with respect to . . . any employee employed in a bona fide executive, administrative, or professional capacity . . . (as such terms are defined and delimited from time to time by regulations of the Secretary . . .).'' [58] The Department has long used a salary level test as part of its method for defining and delimiting that exemption.

In 1949, the Department summarized the role of the salary level tests over the preceding decade, explaining:

> In this long experience, the salary tests, even though too low in the later years to serve their purpose fully, have amply proved their effectiveness in preventing the misclassification by employers of obviously nonexempt employees, thus tending to reduce litigation. They have simplified enforcement by providing a ready method of screening out the obviously nonexempt employees, making an analysis of duties in such cases unnecessary. The salary requirements also have furnished a practical guide to the inspector as well as to employers and employees in borderline cases. In an overwhelming majority of cases, it has been found by careful inspection that personnel who did not meet the salary requirements would also not qualify under other sections of the regulations as the Divisions and the courts have interpreted them.[59]

The Department again referenced these principles in the Kantor Report, reiterating, for example, that the salary level tests ''provide['']a ready method of screening out the obviously nonexempt employees[,]'' and that employees ''who do not meet the salary test are generally also found not to meet the other requirements of the regulations.'' [60] The 2003–2004 rulemaking also referenced these principles.[61] Likewise, this final rule updates the standard salary level in light of increased employee earnings, so that it maintains its usefulness in ''screening out the obviously nonexempt employees.''

For over 75 years the Department has used a salary level test as a criterion for identifying bona fide executive, administrative, and professional employees. Some statements in the Department's regulatory history have at times, however, suggested a greater role for the salary level test. These include, for instance, a statement from the 1940 Stein Report that salary is '' 'the best single test of the employer's good faith in characterizing the employment as of a professional nature.' '' [62] The Stein Report also stated that ''if an employer states that a particular employee is of sufficient importance . . . to be classified as an 'executive' employee and thereby exempt from the protection of the [A]ct, the best single test of the employer's good faith in attributing importance to the employee's services is the amount he pays for them.'' [63]

As explained in the NPRM, the *Nevada* district court's invalidation of the 2016 final rule has prompted the Department to clarify these and similar statements in light of the salary level test's purposes and regulatory history. The concept of a ''dividing line'' should not be misconstrued to suggest that the Department views the salary level test as an effort to divide all exempt employees from all nonexempt employees. A salary level is helpful to determine who is not an exempt executive, administrative or professional employee—the employees who fall beneath it. But the salary level has significantly less probative value for the employees above it. They may be exempt or nonexempt. Above the threshold, the Department evaluates an employee's status as exempt or nonexempt based on an assessment of the duties that employee performs. An approach that emphasizes salary alone, irrespective of employee duties, would stand in significant tension with the Act. Section 13(a)(1) directs the Department to define and delimit employees based on the ''capacity'' in which they are employed. Salary is a helpful indicator of the capacity in which an employee is employed, especially among lower-paid employees. But it is not ''capacity'' in and of itself.

The district court's summary judgment decision endorsed the Department's historical approach to setting the salary level and held the 2016 final rule unlawful because it departed from it. The district court approvingly cited the Weiss Report and explained that setting ''the minimum salary level as a floor to 'screen[ ] out the obviously nonexempt employees' '' is ''consistent with Congress's intent.'' [64] Further endorsing the Department's earlier rulemakings, the district court stated that prior to the 2016 final rule, ''the Department ha[d] used a permissible minimum salary level as a test for *identifying* categories of employees Congress intended to exempt.'' [65] The court then explained that in contrast to these acceptable past practices, the 2016 standard salary level of $913 per week was unlawful because it would exclude from exemption ''so many employees who perform exempt duties.'' [66] In support, the court cited the Department's estimate that, without some intervening action by their employers, the new salary level would result in 4.2 million workers who meet the duties test becoming nonexempt.[67] The court also emphasized the magnitude of the salary level increase, stating that the 2016 final rule ''more than double[d] the previous minimum salary level'' and that ''[b]y raising the salary level in this manner, the Department effectively eliminate[d] a

[55] 81 FR 32391 (May 23, 2016).

[56] *Id.* at 32408.

[57] *Id.* at 32393.

[58] 29 U.S.C. 213(a)–(a)(1).

[59] Weiss Report at 8.

[60] Kantor Report at 2–3; *see also* U.S. Dep't of Labor, *28th Annual Report of the Secretary of Labor for the Fiscal Year Ended June 30, 1940* (1940), at 236 (''[T]he power to define is the power to exclude.'').

[61] *See* 69 FR 22165; 68 FR 15560, 15570 (Mar. 31, 2003).

[62] 81 FR 32413 (quoting Stein Report at 42); *see also* 69 FR 22165 (quoting Stein Report at 42).

[63] Stein Report at 19; *see also id.* at 5 (''[T] he good faith specifically required by the [A]ct is best shown by the salary paid.''); *id.* at 19 (salary provides ''a valuable and easily applied index to the 'bona fide' character of the employment for which exemption is claimed''); *cf.* Weiss Report at 9 (''[S]alary is the best single indicator of the degree of importance involved in a particular employee's job.''); Kantor Report at 2 (''[Salary] is an index of the status that sets off the bona fide executive from the working squad-leader, and distinguishes the clerk or subprofessional from one who is performing administrative or professional work.''). The Department ''is not bound by the [Stein, Weiss, and Kantor] reports,'' though they have been carefully considered. 69 FR 22124.

[64] 275 F. Supp. 3d at 806 (quoting Weiss Report at 7–8); *see also id.* at 807 at n.6 (supporting salary level that operates ''as more of a floor'') (internal quotation marks and citation omitted).

[65] *Id.* at 806 (emphasis in original).

[66] *Id.* at 807.

[67] *Id.* at 806.

consideration of whether an employee performs 'bona fide executive, administrative, or professional capacity' duties.'' [68] The district court declared the final rule invalid because the Department had unlawfully excluded from exemption ''entire categories of previously exempt employees who perform 'bona fide executive, administrative, or professional capacity' duties.'' [69]

By excluding from exemption, without regard to their duties, 4.2 million workers who would have otherwise been exempt because they passed the salary basis and duties tests established under the 2004 final rule, the 2016 final rule was in tension with the Act and with the Department's longstanding policy of setting a salary level that does not ''disqualify[ ] any substantial number of'' bona fide executive, administrative, and professional employees from exemption.[70] A salary level set that high does not further the purpose of the Act, and is inconsistent with the salary level test's useful, but limited, role in defining the EAP exemption.

The Department has therefore reexamined the 2016 final rule in light of the district court's decision and the salary level's historical purpose. The district court's decision underscores that except at the relatively low levels of compensation where EAP employees are unlikely to be found, the salary level is not a substitute for an analysis of an employee's duties. It is, at most, an indicator of those duties. For most white collar, salaried employees, the exemption should turn on an analysis of their actual functions, not their salaries, as Congress instructed. The salary level test's primary and modest purpose is to identify potentially exempt employees by screening out obviously nonexempt employees.

In light of these considerations, as noted in the NPRM, the Department has concluded that, while an increase in the standard salary level from $455 per week is warranted, the increase to $913 per week in the 2016 final rule was inappropriate. The Department has therefore engaged in this rulemaking to realign the salary level with its appropriate limited purpose, to address the concerns about the 2016 final rule identified by the district court, and to update the salary level in light of increased employee earnings.

iii. Standard Salary Level Proposal

In its NPRM, the Department proposed to rescind formally the 2016 final rule and to update the salary level by setting the salary level equal to the 20th percentile of earnings of full-time salaried workers in the lowest-wage region (the South) and/or in the retail industry nationally. The Department applied this method to pooled CPS MORG data for 2015 to 2017, adjusted to 2017, producing a level of $641 per week. To reflect employees' anticipated compensation at the time the rule would become effective, the Department then inflated this level to January 2020 using the compound annual growth rate in earnings since the 2004 rule. This methodology resulted in a proposed salary level of $679 per week ($35,308 per year). The Department estimated that at this level, 1.1 million employees who earn at least $455 per week but less than $679 per week would, without some intervening action by their employers, gain overtime eligibility.

The Department also stated that applying the 2004 final rule's methodology to set the salary level would ensure that overtime-eligible workers continue to receive the protections Congress intended, while avoiding the concerns that led to the invalidation of the 2016 rule. 84 FR 10903. The Department explained that adhering to the 2004 final rule's methodology was reasonable and appropriate, noting that it has enforced the 2004 final rule's salary level for nearly 15 years—the second-longest period (after the salary levels set in 1975) for any part 541 salary test. *Id.* at 10909. The Department stated that applying this well-established method would also promote familiarity and stability in the workplace, without causing significant hardship or disruption to the economy. *Id.* The Department also noted that the 2004 final rule has never been challenged, and so applying the 2004 salary level methodology would minimize the uncertainty and potential legal vulnerabilities that could accompany a novel and untested approach. *Id.*

iv. Standard Salary Level Final Rule

In the final rule, the Department adopts its proposed methodology for setting the standard salary level, with one minor modification. The Department will set the salary level equal to the 20th percentile of earnings of full-time salaried workers in the lowest-wage region (the South) and/or in the retail industry nationally. To calculate the salary level, the Department used updated CPS earnings data that BLS has compiled since the Department drafted its proposal. Specifically, the Department applied the adopted methodology to pooled CPS MORG data for July 2016 to June 2019, adjusted to reflect 2018/2019. As discussed below, rather than projecting the salary level to January 2020, as proposed in the NPRM, the Department has instead used the most recent data available at the time the Department drafted this final rule. This results in a salary level of $684 per week.

The Department believes that this method will set an appropriate dividing line between nonexempt and potentially exempt employees by screening out from exemption employees who, based on their compensation, are unlikely to be bona fide executive, administrative, or professional employees. In addition, the use of earnings data from the South and the retail industry will ensure that the salary level is suitable for employees in low-wage regions and industries. This approach will also maintain the prominence of the duties test by ensuring that the salary level alone does not disqualify from exemption a substantial number of employees who meet the duties test. This is consistent with the duties test's historical function, and will alleviate a major concern—overemphasis on the salary level test—that led to the 2016 rule's invalidation.

Once this rule is effective, white collar employees who are subject to the salary level test and earn less than $684 per week will not qualify for the EAP exemption, and therefore will be entitled to overtime pay. Employees earning this amount or more on a salary or fee basis will be exempt if they meet the standard duties test. As a result of this updated salary level, 1.2 million currently exempt employees who earn at least $455 but less than the updated standard salary level of $684 per week will, without some intervening action by their employers, gain overtime eligibility. In addition, 2.2 million white collar workers earning within this salary range who are currently nonexempt because they do not meet the standard duties test will have their overtime-eligible status strengthened because their exemption status will be clear based on their salary alone.

v. Discussion of Comments

1. Threshold Issues

As was the case in the responses to the July 26, 2017 RFI and in feedback received at the public listening sessions, commenters to the NPRM overwhelmingly agreed that the salary

[68] *Id.* at 807 (quoting 29 U.S.C. 213(a)(1)).

[69] *Id.* at 806 (quoting 29 U.S.C. 213(a)(1)).

[70] Kantor Report at 5. In contrast, had the Department simply applied the 2004 methodology to set the standard salary level, the 2016 final rule would have resulted in approximately 683,000 workers who satisfied the duties test becoming nonexempt. *See* 81 FR 32504 (Table 32).

level should be increased from the currently enforced level of $455 per week, which was set in 2004. Only a few commenters asserted that the salary level should not be updated; these commenters generally expressed concern that it would be difficult for employers to absorb any increase to the salary level. *See* Home Care Association of America; South Butler Community Library. Fisher & Phillips LLP and the National Federation of Independent Business (NFIB), however, questioned whether the Department has authority to set a salary level at all.

The vast majority of commenters also agreed that the Department should continue to set the salary level on a nationwide basis rather than having different salary levels that vary by region, industry, or some other factor. *See, e.g.,* Associated General Contractors of America (AGC); National Council of Nonprofits; National Employment Law Project (NELP); National Propane Gas Association; Partnership to Protect Workplace Opportunity (PPWO). A few commenters suggested that the Department set multiple salary levels, such as by region or state or for urban and rural areas. *See* Council for Christian Colleges and Universities; Idaho Division of Human Resources; Lutheran Services in America. A few other commenters advocated for industry-specific salary levels, *see* National Newspaper Association, or exemptions from the salary level test for specific industries, *see* Family Focused Treatment Association, or for ''seasonal'' employers, *see* Corps Network. Special Olympics sought a special salary level for non-profits, while the National Council of Nonprofits opposed such a carve-out.

The Department maintains that the FLSA's delegation of authority to the Secretary to ''define[ ] and delimit[ ]'' the terms of the section 13(a)(1) exemption includes the authority to set a salary level. While the language of section 13(a)(1) precludes the Department from adopting a salary-only test because salary ''is not 'capacity' in and of itself,'' 84 FR 10907; *see also* 81 FR 32429; 69 FR 22173, the Department's broad authority to ''define and delimit'' the terms of the EAP exemption permits it to use a salary level test as one criterion for identifying bona fide executive, administrative, and professional employees. The Department has used such a test for over 75 years, and its authority to establish a salary level is well-established. *See, e.g., Wirtz* v. *Miss. Publishers Corp.,* 364 F.2d 603, 608 (5th Cir. 1966); *Fanelli* v. *U.S. Gypsum Co.,* 141 F.2d 216, 218 (2d Cir. 1944); *Walling* v. *Yeakley,* 140 F.2d 830, 832–33 (10th Cir. 1944). As noted in the NPRM, ''[a] salary level is helpful to determine who is not an executive, administrative or professional employee'' because it ''is a helpful indicator of the capacity in which an employee is employed, especially among lower-paid employees.'' 84 FR 10907.

The Department agrees with the vast majority of commenters who supported increasing the salary level. The currently enforced level of $455 was set a decade and a half ago in 2004. Like all previous salary levels, its effectiveness as a dividing line between nonexempt and potentially exempt employees has diminished over time, and the level should therefore be updated to align with growth in earnings in the intervening years. While the Department is sensitive to the views of commenters who contended that any increase would be challenging for businesses, historical experience has shown that incremental, reasonable salary level increases such as the one in this final rule are feasible and do not have significant adverse economic consequences. Additionally, as discussed below, the salary level set in this final rule takes these commenters' concerns into account by using wages in the South and the retail industry.

As in the past, the Department chooses to set a nationwide salary level and declines to establish multiple salary levels based on region, industry, employer size, or any other factor. Having multiple salary levels would make the regulations more complicated; for example, regional variations would introduce unnecessary complexity, particularly for employers and employees who operate or work across state lines. As the Department has explained when previously rejecting regional salary thresholds, adopting multiple different salary levels would, at minimum, create significant administrative difficulties ''because of the large number of different salary levels this would require.'' 69 FR 22171; 81 FR 32411. Likewise, the Department declines to set any additional industry-specific salary levels. The Department has rarely created such levels.[71] Instead, as the Department has previously noted, the 2004 methodology ''addresses the concerns'' of commenters advocating for multiple salary levels ''by looking toward the lower end of the salary levels and considering salaries in the South and in the retail industry.'' 69 FR 22171. This approach avoids the new compliance burdens that multiple salary levels would entail, while ensuring that the salary level is low enough that it exempts bona fide EAP employees in those regions and industries.[72]

2. The New Salary Level

Commenters diverged regarding the appropriate level at which to set the new salary level. As a general matter, with some exceptions, employer representatives supported the Department's proposal, while employee representatives opposed it and favored a level at least as high as the one set in the 2016 final rule.

The vast majority of employer representatives supported the Department's proposal to use the 2004 methodology to update the salary level. *See, e.g.,* HR Policy Association; National Association of Home Builders (NAHB); Small Business Legislative Council; PPWO; Wage and Hour Defense Institute. Employer representatives who supported the proposed level generally agreed with the Department's assessment that the 2004 methodology was faithful to the salary level's purpose of screening out only those employees who are obviously nonexempt, while avoiding a de facto salary-only test that would impermissibly replace the role of the duties test. *See, e.g.,* Bloomin' Brands; Job Creators Network; National Retail Federation (NRF); PPWO; Seyfarth Shaw.

Commenters who supported the proposal also stated that unlike the 2016 final rule, the proposal was suitable and manageable for low-wage regions and

[71] A special level for the motion picture producing industry has been in place for over six decades due to the ''peculiar employment conditions existing in the industry.'' 18 FR 2881. Academic administrative employees meet the compensation requirement if they are paid on a salary basis ''at a rate at least equal to the entrance salary for teachers in the educational establishment by which the employee is employed.'' 29 CFR 541.600(c). The Department has otherwise refrained from setting industry-specific salary levels.

[72] Some commenters asked the Department to permit employers to prorate the salary level for part-time employees. *See, e.g.,* College and University Professional Association for Human Resources (CUPA–HR); Council for Christian Colleges and Universities; Idaho Division of Human Resources. The Department has never prorated the salary level for part-time positions, and it specifically considered and rejected similar requests in its 2004 and 2016 final rules. *See* 81 FR 23422; 69 FR 22171. As the Department has previously explained, employees hired to work part time, by most definitions, do not work in excess of 40 hours in a workweek, and overtime pay is not at issue for these employees. An employer may pay a nonexempt employee a salary to work part time without violating the FLSA, so long as the salary equals at least the minimum wage when divided by the actual number of hours (40 or fewer) the employee worked. *See* FLSA2008–1NA (Feb. 14, 2008). To the extent that commenters are concerned about the exemption status of seasonal employees, the Department notes that ''[e]xempt employees need not be paid for any workweek in which they perform no work.'' 29 CFR 541.602(a)(1).

industries, and for small businesses. *See, e.g.,* American Hotel and Lodging Association (AHLA); American Society of Travel Advisors (ASTA); CUPA–HR; LeadingAge; Society of Independent Gasoline Marketers of America (SIGMA); YMCA. Many also conveyed that the proposed level would not produce the same negative effects—*e.g.,* increased employer burdens and diminished workplace flexibility—as the 2016 final rule. *See, e.g.,* National Association of Landscape Professionals; Seyfarth Shaw. Some also noted that the 2004 rule has withstood the test of time for the past 15 years and has never been challenged in court. *See, e.g.,* Job Creators Network; SIGMA. Additionally, many of these commenters agreed with the Department that the proposed rule was responsive to the district court's concerns that led to the invalidation of the 2016 final rule. *See, e.g.,* Ogletree, Deakins, Nash, Smoak & Stewart, P.C.; SHRM.

Many employer representatives maintained that the proposed rule's salary level resulted in a more appropriate number of employees who would become newly nonexempt—1.1 million in the first year—compared to the 2016 final rule, which would have resulted in 4.2 million such workers in the first year. They noted that the smaller number of newly nonexempt employees would make it easier for employers to absorb the costs of compliance, *see* U.S. Small Business Administration Office of Advocacy (SBA Advocacy), would lessen the legal risk associated with the rule, *see* National Restaurant Association (NRA); Wage and Hour Defense Institute, and would ensure that the salary level maintains its historic screening function, *see* AGC; Chamber of Commerce of the United States of America (Chamber); NRF.

A few commenters, while generally supportive of the Department's approach in the NRPM, advocated for a salary level lower than the one proposed. These stakeholders maintained that to ensure that the salary level could accommodate low-wage regions and industries, the Department should exclude higher-wage states from the earnings data used to set the salary level. For example, some commenters urged the Department to include only the East South Central and West South Central Census Divisions, which include the lower-wage states of Kentucky, Tennessee, Alabama, Mississippi, Louisiana, Arkansas, Oklahoma, and Texas, *see* Chamber; Food Marketing Institute (FMI); International Franchise Association (IFA); NRA, while AHLA recommended excluding Maryland, Virginia, and the District of Columbia from the data set. Others suggested generally that the Department use a narrower geographic area than the entire South, using the East South Central Census Division (Alabama, Kentucky, Mississippi, and Tennessee) as an example. *See* Kentucky Retail Federation; SBA Advocacy.

Employee representatives, conversely, generally stated that the salary level should be raised significantly above the level proposed in the NPRM or that the duties test should be significantly strengthened. *See, e.g.,* National Women's Law Center (NWLC); Public Justice Center; UnidosUS. Many commenters supported the level in the 2016 final rule or something similar to it. *See, e.g.,* American Association of Retired Persons (AARP); American Federation of State, County, and Municipal Employees (AFSCME); Campaign Comments; International Union, United Automobile, Aerospace & Agricultural Implement Workers of America (UAW). A few advocated that the salary level be set even higher, at $1,176 per week ($61,152 per year), using median earnings data. *See* National Employment Lawyers Association (NELA); Nichols Kaster, PLLP (Nichols Kaster); Rudy, Exelrod, Zieff & Lowe, LLP (Rudy Exelrod); Texas Employment Lawyers Association (TELA).

Many employee representatives maintained that the salary level proposed in the NPRM is inconsistent with the purpose of the FLSA and the EAP exemption. In general, these commenters contended that the proposed salary level was too low to adequately distinguish between bona fide EAP employees and those who were intended to be eligible for overtime, and that the rule would result in the exemption of lower-wage workers with limited bargaining power, whom the statute was designed to protect. *See, e.g.,* NELP; NELA; Texas RioGrande Legal Aid; Washington State Budget and Policy Center. Several commenters stated that the proposal would inappropriately exempt employees who perform significant amounts of nonexempt work. *See, e.g.,* National Council of Jewish Women; Women Employed. The American Federation of Labor and Congress of Industrial Organizations (AFL–CIO) disagreed that the salary level test's primary purpose is to screen out obviously nonexempt employees, contending that statements to that effect in the Weiss and Stein reports were ''not proposals for setting the long duties salary threshold'' but ''defending the salary tests against criticism,'' and that the salary levels described in those reports as having ''screening'' functions were accompanied by the more rigorous long duties test.

Commenters also noted that according to the Department's own estimates, 84 FR 10951, the proposed rule would result in 2.8 million fewer workers newly entitled to overtime pay in the first year than the 2016 final rule. *See* Joint Comment from 77 Members of Congress; National Partnership for Women and Families; Nichols Kaster. Many of these commenters also cited estimates by EPI, which projected that the proposed rule, compared to the 2016 final rule, would result in $1.2 billion fewer dollars in earnings transfers to employees and would affect 8.2 million fewer workers, including 3.1 million workers who would have gained the right to overtime pay and 5.1 million workers who are already overtime-eligible but would have had their overtime protections strengthened by the 2016 final rule's higher salary level because of a reduced risk of misclassification. These commenters stated that the narrowed scope of the proposed rule would be detrimental to these employees, who include millions of women, people of color, and parents of children under 18. *See* EPI; National Partnership for Women and Families. Some maintained, for example, that a higher salary level that would affect more workers would provide such workers with more income, improve upward mobility, and/or provide workers with more time to spend with their families. *See* AARP; Campaign Comments. Several commenters highlighted the lower number of affected employees (compared to the 2016 final rule) in their particular states. *See, e.g.,* Maryland Center on Economic Policy; Washington State Budget and Policy Center.

Some commenters also asserted that the proposed salary level would result in a higher risk of misclassification relative to the 2016 final rule, as well as more litigation, because more employees' exempt status would turn on the duties test rather than the salary level test. *See* NELA; Winebrake & Santillo LLC. A group of 14 state attorneys general and the Attorney General for the District of Columbia (State AGs) stated that these misclassification consequences would extend to state wage-and-hour laws that contain EAP exemptions that track the federal standard.

Commenters who opposed the proposed rule also criticized the Department's reliance on the reasoning of the *Nevada* district court's decision.

See AFL–CIO; EPI; NELP; NWLC; State AGs. These commenters took issue with the district court's conclusion that the 2016 final rule's salary level was too high because it classified as nonexempt over 4 million previously exempt workers based on their salaries alone, and as a result impermissibly displaced the role of the duties test. AFL–CIO and EPI asserted that the raw number of newly nonexempt workers under a new salary test should not determine the test's appropriateness since that number depends on several factors, such as the amount of time since the previous update and whether the methodology used in the last update was sound. Relatedly, the AFL–CIO stated that it is unclear why the 2016 final rule's salary level, which would have resulted in 4.2 million newly nonexempt employees, was impermissibly high, but the proposed rule's salary level, which would result in 1.1 million (the Department's estimate) to 1.4 million (EPI's estimate) newly nonexempt employees, is not. The AFL–CIO also asserted that the Department preemptively responded to the district court's views in the 2016 final rule, while it and other employee representatives contended that the rationale that the Department put forth in support of the 2016 final rule was more persuasive than the district court decision that invalidated it. *See* AFL–CIO; EPI; NELP; NWLC.

Many employee commenters asserted that if the Department did not substantially raise the salary level above the proposed level, it should establish a more rigorous duties test such as the former long test, which set specific limits on the performance of nonexempt work. *See, e.g.,* AARP; House and Senate Democratic Caucuses of the Michigan Legislature; National Council of Jewish Women; Women Employed. Some commenters recommended instituting a more rigorous duties test regardless of the salary level the Department adopts. *See* AFL–CIO; State of Wisconsin Department of Workforce Development.

Finally, several employee representatives also asserted that by adopting the 2004 methodology in the NPRM, the Department perpetuated a methodological error that the 2016 final rule characterized as a ''mismatch.'' *See* AFL–CIO; Economic Policy Institute (EPI); NELP; NWLC; 81 FR 34400. According to this view, while the Department had historically used two tests for exemption—a long test that paired a more rigorous duties test with a lower salary level, and a short test that paired a less rigorous duties test with a higher salary level—in 2004, the Department instead paired a less rigorous duties test with a lower salary level, resulting in historically nonexempt workers being instead classified as exempt. These commenters stated that the 2004 methodology failed to adjust for changes from the long/short test structure, and that a significantly higher salary level is necessary to account for the absence of the long duties test, which restricted the amount of nonexempt work lower-wage white collar employees could perform while still being classified as exempt. Some of these commenters contended that, as a result, the 2004 methodology results in a salary level that exempts certain historically nonexempt employees because employees who traditionally passed the long salary test and failed the long duties test became exempt under the 2004 final rule's standard salary level and duties tests. *See, e.g.,* NELA; Nichols Kaster; Senator Patty Murray. Some commented that the Department unreasonably relied on the functional dormancy of the long test to justify its adoption of the standard test in 2004, given that the Department did not update the short and long test thresholds between 1975 and 2004. One commenter, EPI, noted that the Department did not include the methodology for the Kantor long test, which used the lowest 10 percent of exempt salaried employees in low-wage regions and industries, as an alternative in the NPRM or elsewhere in the proposal.

Conversely, employer representatives disagreed with the ''mismatch'' rationale. They stated, for example, that the standard duties test is not identical to the short duties test, and that in 2004, the Department accounted for its change in the structure and data set used for the EAP exemption by adjusting the percentile used for determining the salary level. *See* Chamber; NRA. More generally, nearly all employer representatives opposed any changes to the standard duties test. *See, e.g.,* Bowling Proprietors Association of America; NGA; PPWO.

The Department appreciates the thoughtful comments it received regarding the salary level. After considering these comments, the Department has decided to retain the approach from the proposed rule with one small change. As proposed, the Department is using CPS earnings data to set the salary level equal to the 20th percentile of full-time salaried workers in the lowest-wage Census Region (the South) and/or the retail industry nationwide. To set the salary level, the Department applied this methodology to pooled CPS MORG data for July 2016 to June 2019, adjusted to reflect 2018/2019. This results in a final rule salary level of $684 per week ($35,568 for a full-year worker). For the reasons discussed below, the Department is not inflating the salary level forward to January 2020 as was proposed in the NPRM, but instead has used the most recent available actual wage data.

As an initial matter, the Department believes that the proposed salary level is consistent with, and faithful to, the FLSA's purpose. As noted in the NPRM, the FLSA explicitly directs that bona fide executive, administrative, and professional employees ''shall not'' be subject to the statute's minimum wage and overtime requirements. 29 U.S.C. 213(a)(1); 84 FR 10903. As such, when defining the contours of the EAP exemption, while the Department must, of course, ensure that employees who are subject to the Act's coverage receive its benefits, it must also ensure that employees whom Congress has directed ''shall'' be exempt from coverage are, in fact, exempt. The 2016 final rule was in tension with this purpose, as it would have newly disqualified 4.2 million workers from exemption simply because of their salaries, regardless of their duties.

The Department believes that this final rule strikes the appropriate balance by using the salary level, in line with its historical purpose, to screen out obviously nonexempt employees. As explained above, the Department articulated this purpose in the Weiss Report in 1949, when it explained that the salary level tests ''prevent[ed] the misclassification by employers of obviously nonexempt employees, thus tending to reduce litigation'' and ''simplified enforcement by providing a ready method of screening out the obviously nonexempt employees'' who, ''[i]n an overwhelming majority of cases . . . would also not qualify under other sections of the regulations as the Divisions and the courts have interpreted them.'' Weiss Report at 8. Likewise, in the Kantor Report, the Department stated the salary level tests ''provide[ ] a ready method of screening out the obviously nonexempt employees,'' and that employees ''who do not meet the salary test are generally also found not to meet the other requirements of the regulations.'' Kantor Report at 2–3. The Department referenced the screening function again in the 2004 final rule. *See* 69 FR 22165. This principle has been at the heart of the Department's interpretation of the EAP exemption for over 75 years.

The Department disagrees with the proposition advanced by some employee representatives that this articulation of the salary level's modest purpose misreads the Weiss and Kantor reports, or that it applies only when paired with the long duties test. Both reports explicitly characterize the minimum salary level as ''simplif[ying] enforcement by providing a ready method of screening out the obviously exempt employees.'' Kantor Report at 3; Weiss Report at 8. And both confirm that under an appropriate salary level test, employees earning below the salary level generally would not meet the requirements of the duties test.[73] While these reports were written while a more rigorous duties test was in effect, they nonetheless affirm that a minimum salary level's purpose is to serve as a ''screening'' mechanism.

Conversely, as explained in the NPRM, the 2016 final rule went beyond this purpose, and instead suggested that the salary level had a much greater role to play in determining exempt status. For example, in the 2016 final rule the Department took the position that, in light of the single standard duties test that is less rigorous than the long duties test, ''the salary threshold must play a greater role in protecting overtime-eligible employees,'' and that ''it [was] necessary to set the salary level higher . . . because the salary level must perform more of the screening function previously performed by the long duties test.'' 81 FR 32412, 32465–66.[74]

As a result, the $913 per week salary level newly excluded 4.2 million salaried workers from exemption regardless of the duties they performed. The district court concluded that this would exclude from exemption ''so many employees who perform exempt duties,'' and in fact excluded ''entire categories of previously exempt employees who perform 'bona fide executive, administrative, or professional capacity' duties[.]'' 275 F. Supp. 3d at 806–7. Accordingly, it invalidated the rule.

In sum, as explained in the NPRM, the Department believes that the 2016 final rule ''untethered the salary level test from its historical justification[,]'' 84 FR 10901, and that this resulted in its invalidation by the district court. For this reason, the Department declines to return to the 2016 methodology or to set an even higher salary level. In contrast, as noted in the NPRM, the methodology in the 2004 final rule, which the Department is applying in this rule, ''has withstood the test of time, is familiar to employees and employers, and can be used without causing significant hardship or disruption to employers or the economy, while ensuring overtime-eligible workers continue to receive the protections intended by Congress.'' *Id.* at 10903.

The Department also believes that the number of workers affected by the salary level set in this final rule confirms that the level is appropriate. The Department estimates that the final rule will result in 1.2 million workers who will be newly overtime-eligible in the first year as a result of the increased salary level. The number of affected workers is very similar to the 1.3 million workers affected by the 2004 rule's salary level increase. *Id.* at 10911 (citing 69 FR 22213, 22253). This similarity to the 2004 rule, which has never been challenged in court, is consistent with the Department's view that the salary level set in this final rule is reasonable and legally sound.

Moreover, as the Department explained in the NPRM, because the 2016 final rule set the salary level ''at the low end of the historical salary range of short test salary levels,'' 81 FR 32414, it failed to account for the absence of a long test that historically exempted white collar workers with lower salaries but whose duties confirmed they were bona fide EAP employees. Thus, the impact of the 2016 final rule would have been the inverse of the ''mismatch'' the Department sought to correct. It would have resulted in employees who, due to the nature of their duties, have historically been classified as exempt suddenly becoming nonexempt simply because of their salaries.

As a result, the 2016 final rule was in tension with the salary level's limited role in defining the EAP exemption, as it conflicted with the Department's longtime practice of setting a salary level that did not ''disqualify[ ] any substantial number of'' bona fide executive, administrative, and professional employees from exemption, Kantor Report at 5, leading directly to the district court's invalidation of the rule. While the Department has long recognized that it is inevitable that some employees will be incorrectly excluded from exemption since the salary level is ''a dividing line [that] cannot be drawn with great precision but can at best be only approximate[,]'' Weiss Report at 11, the Department may not disregard Congress's express directive to exempt bona fide EAP employees. Conversely, the 1.2 million lower-income workers who will become nonexempt as a result of this rule's increase to the standard salary level will not include a substantial number of workers whose duties have historically qualified them as bona fide EAP employees.

Thus, while employee representatives criticized the narrower scope of this rule compared to the 2016 final rule, the fact that this final rule affects considerably fewer employees than the 2016 final rule confirms, rather than undermines, its appropriateness. Given that the 2016 final rule was invalidated due to its overbreadth, that rule is not a reasonable benchmark for concluding that the number of affected employees under this rule is too low.

As noted above, employee commenters also objected to the Department's reliance on the *Nevada* district court's decision invalidating the 2016 final rule. The Department believes that its reliance on the reasoning of the district court is well-founded.

Such reliance is reasonable and prudent as it reduces the vulnerability of new rules to legal challenges or injunctions, and maximizes the likelihood that a new rule can be implemented immediately. Notably, it has been over three years since the 2016 rule was published, and nearly three years since its stated effective date. Because of the rule's invalidation, however, the currently enforced salary level remains at $455 per week, which the Department and nearly all commenters agree must be updated. Adoption of a salary level that reduces, to the extent possible, the likelihood that the rule will be enjoined is the best way to ensure that workers can reap the rule's benefits as soon as possible rather than waiting for the outcome of potentially lengthy litigation. The Department believes that the salary level in this final rule accomplishes that objective, particularly given the district court's implicit endorsement of the 2004 methodology. *See* 275 F. Supp. 3d at

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[73] *See* Kantor Report at 3 (''Employees who do not meet the salary test are generally also found not to meet the other requirements of the regulations.''); Weiss Report at 8 (''In an overwhelming majority of cases, it has been found by careful inspection that personnel who did not meet the salary requirements would also not qualify under other sections of the regulations as the Divisions and the courts have interpreted them.'').

[74] As noted in the NRPM, 84 FR 10908 n.76, the Department explained in the 2016 final rule that at the time of its analysis, 12.2 million salaried white collar workers earned more than $455 per week but were overtime eligible because they failed the duties test, while 838,000 salaried white collar workers were overtime eligible because even though they passed the standard duties test they earned below $455 per week. The Department then estimated that a $913-per-week salary level would result in 6.5 million salaried white collar workers who failed only the duties test, and increase to 5.0 million the number of salaried white collar workers who passed the duties test but would be overtime eligible because they failed the salary level test. *See* 81 FR 32464–65; *see also id.* at 32413. As the Department noted, however, it ''has never compared the number of employees who are nonexempt based exclusively on the salary or duties test, respectively, to determine the effectiveness of the salary level.'' 84 FR 10908.

807 n.6 (noting the court's earlier observation that an updated 2004 salary level likely would have not prompted the litigation that invalidated the 2016 final rule because it ''would still be operating . . . as more of a floor'') (internal quotation marks and citation omitted).

Additionally, the Department is mindful of the concerns the district court cited. As articulated in the NPRM and above, the 2016 final rule was, at minimum, in tension with the FLSA because it resulted in 4.2 million employees, including employees who were historically exempt under the long test, becoming nonexempt based on their salaries alone, even though the Act directs that the EAP exemption be based on ''capacity.'' This threatened to make ''salary rather than an employee's duties determinative'' of an employee's status under the EAP exemption.[75] While the 2016 final rule naturally contains language disagreeing with these propositions, for the reasons explained above, the Department has reexamined the 2016 final rule in light of the district court's decision and the public comments it has received in response to the RFI and the NPRM, and ultimately finds that the concerns voiced by the district court and by many public commenters warrant adopting a lower salary level.

The Department disagrees with the employee commenters who asserted that the 2004 methodology created a ''mismatch'' that must be corrected by a salary level comparable to the one from the 2016 final rule or a restoration of the long duties test. *See, e.g.,* EPI (''The methodology for setting the standard salary threshold in the 2004 rule was fundamentally flawed.''); NELP. The 2004 final rule explained that it was difficult to coherently apply the long duties test's requirement that an EAP employee perform no more than 20 percent nonexempt work.[76] Consequently, the Department switched from the long and short duties tests to a single duties test that, like the previous short duties test, did not include a quantitative limit on the percentage of time performing nonexempt work. And the Department set a standard salary level that was similar to that of the long test.

The commenters relying on the ''mismatch'' theory appear to assert that the 2004 final rule should have paired the single duties test with a higher salary threshold such as the short test because the Department was obligated to preserve the previous structure of pairing a more rigorous duties test with a lower salary level test, or a less rigorous duties test with a higher salary level. *See, e.g.,* AFL–CIO, EPI. But the previous structure had been created by the Department as one among many permissible policy choices. It was not required by the statutory text. Indeed, the statutory text does not require the Department to determine any salary level. As such, the Department was under no legal obligation to preserve the previous salary/duties structure in the 2004 final rule.

Moreover, the Department believes it would have been inappropriate to adopt the higher short test salary level after removing the long duties test in the 2004 final rule. *See* 84 FR 10908. The long duties test ensured that white collar employees would not become nonexempt simply because their salaries fell below the short test's higher threshold, if their duties clearly indicated bona fide EAP status. If the 2004 final rule had adopted the short test's higher salary threshold after eliminating the long duties test, such employees would have been reclassified as nonexempt solely because of their salary level. This approach would have departed from the historical role of using the salary level to screen out only obviously nonexempt employees, and would have risked violating the statutory requirement to base EAP status on the ''capacity'' in which the employee is employed. 29 U.S.C. 213(a)(1). Therefore, the Department believes that its' decision in 2004 not to pair the higher short test salary level with the standard duties test was a necessary measure to maintain policy consistency and follow statutory requirements.

Indeed, the 2016 final rule's attempt to correct the ''mismatch'' by setting the salary level ''at the low end of the historical range of short test salary levels,'' 81 FR 32409, created the precise legal risks that the 2004 final rule attempted to avoid. While the Department previously relied on the mismatch theory in defending the 2016 final rule in litigation, the district court, in declaring the 2016 final rule invalid for the reasons set forth above, implicitly rejected application of the mismatch theory in reaching its conclusion. As explained above, the district court found that the salary level set by the 2016 final rule improperly substituted employee salaries for an analysis of employees' duties.[77] 275 F. Supp. 3d at 806. In contrast, the 2004 methodology has never even been challenged in court—let alone invalidated—during the 15 years it has been enforced by the Department.

Additionally, as noted in the NPRM, the mismatch rationale failed to account for the substantial number of years during which the long duties test was effectively dormant. 84 FR 10908–09; *see also* 69 FR 22126 (explaining that ''the 'long' duties test [had], as a practical matter, become effectively dormant'' due to outdated salary levels, and quoting commenters who described the long duties test as ''inoperative,'' ''rarely, if ever, used,'' ''largely . . . dormant,'' and ''lack[ing] current relevance''). The long test salary levels set in 1975 were equaled or surpassed by the minimum wage in 1991.[78] Thus, since at least 1991, the short duties test and salary level determined whether workers qualified for the EAP exemption. Employers and employees alike have effectively operated for 28 years under a single-test system. Thus, although, as noted above, some employee commenters asserted that the 2004 methodology exempts certain historically nonexempt employees (*i.e.,* those who had passed the long salary test and failed the long duties test), any of these employees who were nonexempt in the years leading up to 2004 were nonexempt because their salaries fell below the short test's salary threshold. It therefore appears that these commenters are requesting that the Department set the salary threshold at the historical short test level. The Department attempted to do this in the 2016 final rule, but as explained above, this approach created legal risks, as evidenced by the district court's conclusion.

The Department continues to believe that the post-1991 landscape is ''highly relevant'' to its approach here, 84 FR 10909, and disagrees with the employee representatives contending otherwise. The one-test system effectively in place for the nearly three decades has created significant reliance interests and

[75] 275 F. Supp. 3d at 807.

[76] 69 FR 22127 (''When employers, employees, as well as Wage and Hour Division investigators applied the 'long' test exemption criteria in the past, distinguishing which specific activities were inherently a part of an employee's exempt work proved to be a subjective and difficult evaluative task that prompted contentious disputes.'').

[77] Some commenters contend that the district court's decision was flawed because it did not address the ''mismatch'' theory in its opinion, even though it was the central theory behind the 2016 final rule. *See* AFL–CIO; NELP. However, as noted above, the district court implicitly rejected the mismatch theory.

[78] In 1975, the Department set a long test salary level of $155 per week for executive and administrative employees, and of $170 per week for professional employees. *See* 40 FR 7092. On April 1, 1991, the federal minimum wage increased to $4.25 per hour, which equals $170 for a 40-hour workweek. *See* Sec. 2, Public Law 101–157, 103 Stat. 938 (Nov. 17, 1989).

understandings in the workplace under which employees and employers alike recognize certain positions as exempt. As the *Nevada* district court recognized, a salary level that deviates substantially from recent practice would result in ''entire categories of previously exempt employees who perform 'bona fide executive, administrative, or professional capacity' duties'' becoming nonexempt. 275 F. Supp. 3d at 806 (quoting 29 U.S.C. 213(a)(1)). Numerous employers indicated that they anticipated significant adverse effects from the 2016 final rule as a result of this widespread reclassification, including not only increased compliance costs but decreased employee flexibility, reduced morale, and increased employee turnover. *See* Independent Electrical Contractors; National Association of Truck Stop Operators; National Multifamily Housing Council and the National Apartment Association; PPWO; SBA Advocacy; Seyfarth Shaw.

Regarding EPI's request that the Department ''include the value of the Kantor long test in the final rule,'' as explained below and as described in more detail in the economic analysis, the Department has considered the Kantor long test methodology as an alternative. But as the 2004 final rule explained, the Kantor method, which uses the lowest 10 percent of exempt salaried employees in low-wage regions and industries, requires ''uncertain assumptions regarding which employees are actually exempt[.]'' 69 FR 22167. It is also more complex to model and thus is less accessible and transparent. And it presents a circularity problem: The Kantor method would determine the population of exempt salaried employees, while being determined by the make-up of that population. The 2004 methodology of setting the minimum salary level based on the lowest 20 percent of *all* salaried employees in the South and retail industry avoids these problems. *See id.* Additionally, as discussed in the economic analysis below, upon consideration of the Kantor method, the Department found that it would result in a salary threshold that differs from the level set in this final rule by $40 per week. EPI similarly estimated that the Kantor method would result in a salary threshold that deviates from the level proposed in the NPRM by $33 per week. The Department does not believe this fairly small difference justifies reverting back to the Kantor method, particularly because the 2004 methodology is familiar to employers and employees, does not require uncertain and circular assumptions, and has never been challenged in court.

The Department also disagrees with commenters who stated that a significantly higher salary level is justified in order to reduce further the risk of employee misclassification. The Department recognizes that, in addition to conferring minimum wage and overtime protections on newly nonexempt employees, an updated salary level clarifies and strengthens the nonexempt status of employees who fail the duties test and earn between the previous salary level and the new one (*i.e.,* those who are and will remain nonexempt), and thereby reduces the risk that those employees will be misclassified as exempt. Indeed, this final rule clarifies and strengthens the nonexempt status of 2.2 million salaried white collar workers and 1.9 million salaried blue collar workers earning between $455 and $684 per week. *See infra* §§ VI.A.iii, VI.D.iii.3.

But the laudable goal of reducing misclassification cannot overtake the statutory text, which grounds an analysis of exemption status in the ''capacity'' in which someone is employed—*i.e.,* that employee's duties. Accordingly, the salary level test's limited purpose is to screen out only those employees who are not performing bona fide EAP duties. *See* Weiss Report at 8 (noting that the salary levels ''have amply proved their effectiveness in preventing the misclassification by employers of *obviously nonexempt* employees'') (emphasis added). As explained at length above, if the salary level is too high, as was the case in the 2016 final rule, it results in a substantial number of historically *exempt* bona fide EAP employees being classified as *nonexempt* without any examination of their duties. Such action is inconsistent with the section 13(a)(1) exemption. The Department believes that potential misclassification of nonexempt employees as exempt is most appropriately addressed through compliance assistance and, if necessary, enforcement by the Department or private parties, rather than through an artificial increase to the salary level.[79]

The Department also declines to adopt a lower salary level than the one proposed in the NPRM, as some employer representatives suggested. As explained above, by setting the salary level at the low end—the 20th percentile—of the earnings of full-time salaried employees in the South and/or retail industry, the Department, consistent with its historical practice, has tailored the salary level to the needs of the lowest-wage regions and industries. While some employer representatives stated that the Department could use an even narrower subset of data by eliminating from consideration higher-wage states, the Department believes that using the entire South—the lowest-wage Census Region—in addition to the retail industry nationwide strikes the appropriate balance by setting a salary level that is based on low-wage areas but can still serve as a meaningful dividing line in higher-wage areas as well.[80]

In sum, after considering the comments received, the Department has decided to update the salary level by applying the 2004 methodology to current data. As noted in the NPRM, using this methodology ''promotes familiarity and stability for the workplace, ensures workers the important wage protections contained in the Act, . . . minimizes the uncertainty and potential legal vulnerabilities that could accompany a novel and untested approach,'' ''avoids new regulatory burdens,'' and sets a salary level that ''accounts for nationwide differences in employee earnings and . . . work[s] appropriately with the standard duties test.'' 84 FR 10909.

The Department declines to make any changes to the duties test, such as adopting a duties test similar to the long duties test, which some employee representatives advocated as an alternative or complement to a higher salary level. As explained above, the standard duties test has been in effect for 15 years, and the short duties test, to which it is similar, was functionally the predominant test in use for the preceding 13 years. This approach has never been challenged. As a result, both employees and employers are accustomed to these tests. Moreover, a large body of jurisprudence interprets these duties tests, and so changing these tests could increase regulatory uncertainty and result in costly litigation. The Department also remains

[79] Regarding the view of the state attorneys general that the new salary level does not do enough to prevent misclassification under their states' wage-and-hour laws that track FLSA exemptions, nothing in this rule prevents any state from enacting a higher salary level, or a more restrictive duties test, than the FLSA if it believes it is necessary to prevent misclassification under state law.

[80] The Chamber stated that the 2004 rule and the Department's application of that rule (in the NPRM) used different groups of states, and that the 2004 rule used only a subset of states in the South Census Region. The Chamber's characterization of the data set used in the 2004 rule is incorrect, as both this rule and the 2004 final rule used the entire South Census Region in setting the salary level.

mindful of employer concerns that reinstating the long test's cap on nonexempt work could introduce new compliance burdens. *See, e.g.,* National Association of Truck Stop Operators; NRF; *see also* 81 FR 32446; 69 FR 22127. Finally, the Department did not propose any changes to the duties test in the NPRM and does not believe that it would be appropriate to institute such a significant change to the part 541 exemptions in this final rule.

Accordingly, the Department declines to return to the more complicated long duties test. The Department believes that the standard duties test, which focuses on whether an employee's ''primary duty'' consists of EAP tasks, can appropriately distinguish bona fide EAP employees from nonexempt workers.

The Department considered a number of alternatives to the salary level in this final rule.[81] First, the Department considered not changing the salary level from the currently enforced level of $455 per week. The Department rejected this option because, as discussed above, the Department concluded that the $455 salary level set fifteen years ago no longer reflects current earnings and must be updated to serve as a meaningful dividing line between nonexempt and potentially exempt employees. The Department also considered maintaining the average minimum wage protection in place since 2004 by using the weighted average of hours at minimum wage and overtime pay represented by the minimum salary level (*i.e.,* the $455 weekly threshold represented 72.2 hours at minimum wage and overtime pay at the minimum wage in 2004; currently, that salary level represents 55.2 hours at minimum wage and overtime pay; the weighted average is 59.5 hours, which yields a salary of $502 per week). The Department rejected this option because it would not adequately address wage growth since 2004.

In light of comments from some employer representatives, the Department also considered using the 2004 methodology but eliminating the District of Columbia, Maryland, and Virginia from the data set used to determine the salary level due to their higher levels of employee earnings. However, as discussed above, the Department believes that using the entire South and the retail industry nationwide results in an appropriate nationwide salary level that is based on low-wage regions but can still serve as a meaningful dividing line in higher-wage regions. Using the entire South is also consistent with the methodology used in the 2004 final rule.

In response to a comment from EPI, the Department also considered adopting the methodology that was used to derive the long test salary level prior to 2004 (the Kantor long test method), which used the lowest 10 percent of exempt salaried employees in low-wage regions and industries. However, as explained in greater detail above, the Department declined to do so because while the Kantor methodology produces a salary level that differs from the level set in this final rule by less than 6 percent, it depends on uncertain and circular assumptions, and is more complex to model and thus less accessible and transparent.

Finally, the Department considered using the methodology from the 2016 final rule to set the salary level, as suggested by many employee representatives. However, as explained at length above, the Department believes that methodology was inappropriate because it resulted in too many employees being newly classified as nonexempt based on their salaries alone, thus supplanting the role of the duties test. Moreover, the district court invalidated the 2016 final rule. Therefore, the Department has chosen to use the 2004 methodology, which, as noted above, screens out obviously nonexempt workers, works well with the standard duties test, and has never been challenged during the fifteen years in which it has been enforced by the Department.

3. Proposed Inflation to January 2020

The Department proposed to inflate the salary level to reflect anticipated wage growth to January 2020, the final rule's estimated effective date. Most commenters did not address this aspect of the proposal, but some employer representatives opposed it. A few stated that the proposed approach was inconsistent with the Department's past practice of setting the salary level using the most recent available data on actual salaries paid to employees, rather than inflationary metrics. *See, e.g.,* Center for Workplace Compliance; Chamber; FMI.

In the final rule, instead of projecting the salary level to January 2020, the Department has set the salary level using the most recent data available at the time the Department has drafted the final rule. The Department is using pooled CPS MORG data from July 2016 to June 2019, adjusted to reflect 2018/2019. As some commenters noted, using recent actual wage data is consistent with the approach the Department has taken in prior rulemakings. *See* 81 FR 32403 (noting regulatory history reveals that in most prior rulemakings ''the Department examined a broad set of data on actual wages paid to salaried employees'' to set the salary level), *id.* at 32051 (''In keeping with our practice, the Department relies on the most up-to-date data available to derive the final salary level[.]'').

It is also consistent with the Department's historical practice (with only one exception, in 1975) of declining to use inflation to adjust the salary level for the part 541 exemption. *See* 69 FR 12167 (noting the Department's ''long-standing tradition of avoiding the use of inflation indicators for automatic adjustments to these salary requirements''). Additionally, the gap between the latest month covered by the data set—June 2019—and the rule's effective date—January 2020—is only six months. This is a shorter gap than was the case in the 2016 rule, which had an effective date of December 1, 2016 and relied on salary data from the fourth quarter of 2015, and a significantly shorter gap than the 2004 rule, which had an effective date of August 23, 2004 and relied on 2002 CPS data. 81 FR 32391, 32405; 69 FR 22122, 22168. Using a data set that includes such recent earnings data enables the Department to avoid the uncertainty and speculation that would accompany projecting earnings data.

4. Rescission of the 2016 Final Rule

Many employer representatives who commented on the issue supported the NPRM's independent proposal to rescind the 2016 final rule. *See, e.g.,* ASTA; Center for Workplace Compliance; NAHB; NFIB; Wage and Hour Defense Institute; Worldwide Cleaning Industry Association. These employers generally maintained that the 2016 final rule, unlike the proposed rule, was inconsistent with how the Department has previously set the salary level, and some highlighted that the 2016 final rule excluded many workers performing EAP duties. As noted above, employer representatives also asserted that the 2016 final rule salary level would have a number of adverse effects, including reductions in staffing levels, hours, and employee benefits; less flexibility in scheduling; and decreased employee morale. In contrast, other commenters, including the tens of thousands who submitted comments as part of a campaign, maintained that the 2016 final rule was appropriate and would have benefited more employees than the salary level proposed in the NPRM, and urged the Department to defend the 2016 final rule in the

[81] The salary levels that would result from each of the alternatives are set forth in section VI.C.

currently stayed litigation. *See, e.g.,* AFL–CIO; Campaign Comments; Senator Patty Murray; The Leadership Conference on Civil and Human Rights.

The Department is finalizing the formal rescission of the 2016 final rule as proposed. Thus, in addition to replacing the 2016 final rule functionally by revising the part 541 regulatory text in the Code of Federal Regulations, this final rule also formally rescinds the 2016 final rule. This rescission operates independently of the new content in this final rule, as the Department intends it to be severable from the substantive rule for revising part 541. Thus, even if the substantive provisions of this final rule revising part 541 are invalidated, enjoined, or otherwise not put into effect, the Department intends the 2004 final rule to remain operative, not the enjoined 2016 final rule that it is rescinding.

Particularly given the recent history of litigation in this area, the rescission of the 2016 final rule is necessary to provide certainty and clarity to employees and employers about what salary level will be effective if this final rule were to be invalidated, enjoined, or otherwise not put into effect. As explained at length above, the Department believes that the salary level set in the 2016 final rule was inappropriate. Moreover, given the district court's invalidation of the 2016 final rule, the 2004 final rule, which has never been challenged in court, is the logical framework to take the place of this rule if this rule were to be struck down.

B. Special Salary Tests

i. Puerto Rico, Virgin Islands, Guam, and the Commonwealth of the Northern Mariana Islands [82]

The Department has applied the standard salary level to Puerto Rico since 2004.[83] In 2016, Congress passed the Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA).[84] Section 404 of PROMESA states that ''any final regulations issued related to'' the Department's 2015 overtime rule NPRM—*i.e.,* the 2016 final rule—''shall have no force or effect'' in Puerto Rico until the Comptroller General of the Unites States completes and transmits a report to Congress assessing the impact of applying the final regulations to Puerto Rico, and the Secretary of Labor, ''taking into account the assessment and report of the Comptroller General, provides a written determination to Congress that applying such rule to Puerto Rico would not have a negative impact on the economy of Puerto Rico.'' [85]

It is the Department's belief that PROMESA does not apply to this final rule as it is a new rulemaking, and thus not ''related to'' the 2015 overtime rule NPRM within the meaning of PROMESA. Section 404, however, reflected Congress's apprehension with increasing the salary level in Puerto Rico, and given the current economic climate there, the Department proposed to set a special salary level in Puerto Rico of $455 per week—the level that currently applies under PROMESA.

The Department also currently applies the standard salary level to the Virgin Islands, Guam, and the Commonwealth of the Northern Mariana Islands (CNMI).[86] The Department understands that U.S. territories face their own economic challenges and that an increase in the salary level affects them differently than the States. In recognition of these challenges, and to promote special salary level consistency across U.S. territories, the Department proposed setting a special salary level of $455 per week for the Virgin Islands, Guam, and the CNMI.

Few commenters addressed this issue, but those who did all supported the Department's proposal. The Saipan Chamber of Commerce, for example, stated that ''U.S. territories face economic challenges not experienced by businesses and employers on the U.S. mainland,'' and the World Floor Covering Association (WFCA) similarly cited the ''unique economies'' in these territories. The Hotel Association of the Northern Mariana Islands referenced several CNMI-specific concerns, including that ''[w]ages across all industries in the CNMI, including the hospitality industry, have been historically lower than their stateside counterparts.'' The CNMI chapter of SHRM expressed similar concerns.

After reviewing the comments received, the Department is finalizing this aspect of the NPRM as proposed. As such, in this final rule the Department will set a special salary level of $455 per week for Puerto Rico, the Virgin Islands, Guam, and the CNMI.

ii. American Samoa

As discussed in the NPRM, the Department has historically applied a special salary level test to employees in American Samoa because minimum wage rates there have remained lower than the federal minimum wage.[87] The Fair Minimum Wage Act of 2007, as amended, provides that industry-specific minimum wage rates in American Samoa will increase every three years until each equals the federal minimum wage.[88] The disparity with the federal minimum wage is expected to remain for the foreseeable future.

The special salary level test for employees in American Samoa has historically equaled approximately 84 percent of the standard salary level.[89] The Department proposed to maintain this percentage and considered whether to set the special salary level in American Samoa equal to 84 percent of the proposed standard salary level ($679 per week)—resulting in a special salary level of $570 per week—or to set it equal to approximately 84 percent of the proposed special salary level applicable to the other U.S. territories ($455 per week)—resulting in a special salary level of $380 per week. The Department proposed a special salary level of $380 per week in American Samoa. It explained that this approach would not only maintain the special salary level that the Department is currently enforcing in American Samoa, but would also ensure that American Samoa, which has a lower minimum wage than the other U.S. territories, would not have a higher special salary level.[90]

The Department received no comments on this proposal and will adopt the methodology set forth in the NPRM. Accordingly, in this final rule the Department will set a special salary level of $380 per week for employees in American Samoa.

iii. Motion Picture Producing Industry

The Department has permitted employers to classify as exempt employees in the motion picture producing industry who are paid a specified base rate per week (or a proportionate amount based on the number of days worked), so long as they meet the duties tests for the EAP exemption.[91] This exception from the

[82] The special salary tests do not apply to employees of the Federal government employed in Puerto Rico, the U.S. Virgin Islands, Guam, the Commonwealth of the Northern Mariana Islands, or American Samoa.

[83] *See* 69 FR 22172.

[84] *See* Public Law 114–187, 130 Stat. 549 (June 30, 2016).

[85] *See* 48 U.S.C. 2193(a)–(b). The Comptroller General's report was published on June 29, 2018 and is available at: *https://www.gao.gov/products/GAO-18-483.*

[86] In Guam and the CNMI, the Department has applied the salary level test(s) applicable to the States. In the Virgin Islands, the Department applied a special salary level test prior to 2004, but applied the standard salary level beginning in 2004.

[87] *See* 69 FR 22172.

[88] *See* Sec. 1, Public Law 114–61, 129 Stat. 545 (Oct. 7, 2015).

[89] *See, e.g.,* 69 FR 22172.

[90] *See* 84 FR 10912.

[91] *See* § 541.709.

''salary basis'' requirement was created in 1953 to address the ''peculiar employment conditions existing in the [motion picture producing] industry,'' and applies, for example, when a motion picture producing industry employee works less than a full workweek and is paid a daily base rate that would yield the weekly base rate if 6 days were worked.[92] Consistent with its practice since the 2004 final rule, the Department proposed to increase the required base rate proportionally to the proposed increase in the standard salary level test, resulting in a proposed base rate of $1,036 per week.

The Department did not receive any comments on the proposed base rate for motion picture employees. The final rule adopts the methodology set forth in our proposal, which using the new standard salary level ($684 per week) results in a base rate of $1,043 per week (or a proportionate amount based on the number of days worked).[93]

C. Inclusion of Nondiscretionary Bonuses, Incentive Payments, and Commissions in the Salary Level Requirement

In the 2016 final rule, the Department for the first time allowed employers to count nondiscretionary bonuses and incentive payments toward the standard or special salary levels.[94] Under that rule, such bonuses must be paid quarterly or more frequently and may satisfy up to 10 percent of the standard or special salary level. In the NPRM, the Department again proposed to permit nondiscretionary bonuses and incentive payments (including commissions) to satisfy up to 10 percent of the standard or special salary level tests for the EAP exemption. However, unlike the 2016 final rule's requirement that such payments must be paid on a quarterly or more frequent basis, the Department proposed to allow the crediting of payments made on an annual or more frequent basis. Additionally, the Department proposed to permit employers to make a final ''catch-up'' payment within one pay period after the end of each 52-week period to bring an employee's compensation up to the required level. *See* 84 FR 10912–13.

Most commenters representing employers supported allowing nondiscretionary bonuses and incentive payments to count towards the standard salary level requirement. Employer representatives supporting the bonuses proposal (or an expanded version of it) asserted that nondiscretionary bonuses and incentive payments constitute a large and important part of the total compensation package for many exempt employees. Several commenters, including the Chamber, FMI, IFA, and NRA, noted that, in light of commenter feedback, the Department has previously acknowledged this point in the NPRM and in the 2016 final rule. *See* 81 FR 32423–24; 84 FR 10912. The Chamber additionally cited a survey from 2018 showing that 80 percent of non-profit and government employers surveyed use some type of ''short-term incentive plan.'' The National Association of Truck Stop Operators and PPWO asserted that the majority of employees who receive bonuses and incentive payments otherwise qualify for exempt status, while SIGMA and WFCA asserted that bonuses and incentive payments tied to an employer's success ''foster a sense of ownership'' among the managerial employees who receive them. Many employer representatives specifically approved of the Department's proposal to allow the crediting of nondiscretionary bonuses and incentive payments paid on an annual basis (rather than quarterly, as provided by the 2016 final rule), agreeing that annual bonuses are a common form of compensation for many EAP employees. *See* PPWO; SIGMA.

Although several employer representatives supported the proposal without reservation, a larger number objected to the proposal's restriction that nondiscretionary bonuses and incentive payments could only satisfy up to 10 percent of the standard salary level. Some of these commenters urged the Department to allow bonuses to satisfy more than 10 percent of the standard salary level, but declined to specify an exact amount. *See* Center for Workplace Compliance; National Association of Federally-Insured Credit Unions; NGA. Others specifically proposed a higher percentage limit, including: WFCA (suggesting 20 percent); Small Business Legislative Council and TechServe Alliance (25 percent); ASTA (30 percent); National Independent Automobile Dealers Association (30 or 40 percent); and HR Policy Association and the Kentucky Retail Federation (50 percent). Finally, many employer representatives urged the Department not to impose any limit. *See, e.g.,* American Network of Community Options and Resources; American Staffing Association; IFA; Mortgage Bankers Association; NRF; PPWO; Seyfarth Shaw.

Some commenters critical of the proposed 10 percent limit asserted that it is not reflective of the compensation practices in their industry, where bonuses and incentive payments often exceed 10 percent of an employee's fixed salary. *See, e.g.,* ASTA; NGA; WFCA. Others contended that to ''harmonize'' the respective regulations, any non-hourly payments that count toward an employee's ''regular rate of pay'' when calculating overtime pay, *see* 29 CFR 778.211(c), should count towards the salary threshold as well. *See, e.g.,* AGC; HR Policy Association; PPWO; Worldwide Cleaning Industry Association.[95] The Chamber, IFA, and the National Lumber and Building Material Dealers Association criticized the NPRM's rationale that the 10 percent limit was necessary to help maintain parity between sectors that use such pay methods and those that traditionally have not done so,[96] while ASTA and TechServe Alliance asserted that the 10 percent limit would have a negative impact on employers in industries that rely on incentive pay.

Although few organizations representing employees commented on the bonuses proposal, those who did were unanimous in voicing their opposition. NELA, Nichols Kaster, Rudy Exelrod, and Smith Summerset & Associates LLC (Smith Summerset) asserted that allowing annual bonuses and incentive payments to satisfy any portion of the salary level test would undermine the premise that only workers with a minimum level of dependable and predictable pay should be exempt from the FLSA's overtime protections. Relatedly, the AFL–CIO expressed concern that the proposal would ''provide a means for employers to manipulate employees' salaries to

[92] 18 FR 2881 (May 19, 1953).

[93] The Department calculated this figure by dividing the weekly salary level ($684) by $455, and then multiplying this result (rounded to the nearest hundredth) by the base rate set in the 2004 final rule ($695 per week). This produced a new base rate of $1,043 (per week), when rounded to the nearest whole dollar.

[94] Although a federal district court subsequently invalidated the 2016 final rule, the court's summary judgment decision did not address the bonuses provision. 275 F. Supp. 3d 795.

[95] For the same reason, some commenters specifically requested the Department allow employers to credit the value of board and lodging towards the standard salary level. See AHLA (''If an employer must include a non-hourly payment in the regular rate, that payment should likewise count towards the salary threshold.''); *see also* CUPA–HR; PPWO; Seyfarth Shaw. AHLA and CUPA–HR asserted that board and lodging benefits are especially common for exempt employees in hospitality and higher education, respectively.

[96] The Chamber stated that such a consideration is ''beyond the Department's proper purview.'' The Chamber and IFA additionally stated that government and non-profit employers do not typically compete with for-profit employers over the same employee, and that the proposal would not alter any existing competitive imbalance in any event.

avoid paying overtime[.]'' *See also* NELA. Given these concerns, some employee representatives asserted that the proposal would be particularly inappropriately paired with a salary level substantially lower than the figure adopted in the 2016 final rule. *See, e.g.,* NELA; Smith Summerset.

Several commenters disputed that nondiscretionary bonuses and incentive payments are indicative of exempt status. For example, NELA and TELA emphasized that such payments do not convey ownership interests in the business, and asserted that their members ''have represented many categories of employees who receive various nondiscretionary bonuses, including middle management and lower level employees[.]'' By contrast, Smith Summerset asserted that nondiscretionary bonuses and incentive payments ''are not an important pay component for the relatively lowly paid employees who would be affected by the [proposal],'' who the firm described as ''most in need of the certainty and regularity of a salary'' (emphasis in original).

Finally, employee representatives worried that the proposal would undermine the clarity and effectiveness of the salary level test. For example, AFL–CIO stated that ''[i]ncluding bonuses in the calculation could create confusion as to whether employees meet the salary threshold test and are overtime eligible.'' *See also* Nichols Kaster. Several commenters, including NELA, Rudy Exelrod, and TELA, asserted that the proposal would increase monitoring and compliance costs. Smith Summerset asserted that employers would have to keep new payroll and timekeeping records for their exempt staff, including for some individuals no longer employed by the company who might be awaiting a deferred compensation payment. Several employee representatives predicted that the proposal would result in increased litigation, particularly over the distinction between discretionary and nondiscretionary bonuses.[97] Smith Summerset emphasized that the back wage claims in such disputes would be substantial, and could pose ''a surprising and unexpected liability to those unsophisticated employers who might stumble into the violation simply by reason of administrative oversight.''

After carefully considering commenter feedback, the Department has decided to adopt the proposal without modification—*i.e.,* allowing employers to satisfy up to 10 percent of the standard or special salary levels [98] with nondiscretionary bonuses and incentive payments (including commissions), provided that such payments are paid no less frequently than on an annual basis.[99] This provision appropriately modernizes the regulations to account for EAP compensation practices in a growing number of workplaces, while at the same time preserving the important role of the salary basis and salary level tests in identifying EAP employees, simplifying compliance, and preventing abuse.

Feedback from employer representatives responding to the NPRM has reinforced the Department's view in the previous rulemaking that the provision of nondiscretionary bonus and incentive payments has become sufficiently correlated with EAP status. At the same time, the Department acknowledges that nonexempt employees may receive nondiscretionary bonuses and incentive payments, and that the part 541 regulations have historically looked only to payments made on a salary or fee basis to satisfy the minimum salary level. The Department believes that allowing employers to credit nondiscretionary bonuses towards up to 10 percent of the standard or special salary levels strikes an appropriate balance between accommodating legitimate pay practices for a growing number of bona fide EAP employees, while not undermining the salary basis requirement.

The Department has decided against raising or eliminating the proposal's 10 percent limitation. The Department continues to believe in the basic logic of the salary requirement. Capping the crediting of nondiscretionary bonuses and incentive payments at 10 percent of the standard salary level ensures that the salary level test remains predominantly a test of *salaried* earnings, requiring that EAP employees subject to the salary criteria must earn at least 90 percent of the standard salary level on a salaried basis. Additionally, while several employer commenters asserted that nondiscretionary bonuses and incentive pay often comprise more than 10 percent of the total compensation paid to EAP employees, few specifically asserted that any significant number of EAP employees earn salaries of less than 90 percent of the proposed salary threshold (*i.e.,* $614.70 per week, or $31,964.40 per year). Thus, the Department disagrees that the cumulative effect of raising the standard salary level while limiting the amount that can be satisfied through nondiscretionary bonuses and incentive pay will result in a significant reduction in such payments. The regulations do not limit the amount of bonuses EAP employees may earn; it only limits the amount that can count toward the standard salary level.

For similar reasons, the Department has decided against expanding the proposal to allow additional kinds of payments to count towards the standard salary level, such as discretionary bonuses, employer benefit contributions, or the value of board, lodging, and facilities. The Department has never allowed such payments to count towards any of the earning thresholds required for the EAP exemption, including under the HCE test created in 2004. *See* 541.601(b)(1). The Department did not propose to allow such payments to count towards the salary level test, and declines commenter suggestions to do so in this final rule.

NELA, Smith Summerset, and other commenters questioned how the proposed rule would treat employees affected by the proposal whose employment ends before the end of a 52-week period. Here, consistent with the treatment of employees under the existing HCE test, *see* § 541.601(b)(3), the Department has amended the proposed regulatory text at § 541.602(a)(3) to clarify that employers may pay employees a prorated amount for a designated 52-week period where an employee does not work for the entire period, because the employee either is newly hired after the period's start or ends employment before the period's end. Determining an employer's payment obligation to such employees to maintain their exempt status depends on the number of workweeks that the employee works within the 52-week period. Where employment ends before the end of the 52-week period, employers must ensure that the employee receives enough in pay to satisfy the standard salary level by the end of the next pay period

[97] NELA and other commenters asserted that ''[d]etermining whether bonuses are discretionary or nondiscretionary already generates considerable litigation in the context of whether certain kinds of bonuses must be included in the regular rate for purposes of calculating the overtime rate.'' *See also* Nichols Kaster; Rudy Exelrod; TELA.

[98] Specifically, this rule permits employers to use nondiscretionary bonuses and incentive payments to satisfy up to 10 percent of the standard salary level or any of the special salary levels applicable to U.S. territories. As discussed in greater detail below, however, HCEs must receive at least the standard salary amount each pay period on a salary or fee basis without regard to the payment of nondiscretionary bonuses and incentive payments.

[99] The employer may use any 52-week period, such as a calendar year, a fiscal year, or an anniversary of the hire year.

following the employee's end of employment.

The final rule permits employers to meet the salary level requirement by making a catch-up payment within one pay period of the end of the 52-week period.[100] In plain terms, each pay period an employer must pay the EAP employee on a salary basis at least 90 percent of the standard salary level and, if at the end of the 52-week period the sum of the salary paid plus the nondiscretionary bonuses and incentive payments (including commissions) paid does not equal the standard salary level for the 52-week period, the employer has one pay period to make up for the shortfall (up to 10 percent of the required salary level). Any such catch-up payment will count only toward the previous 52-week period's salary amount and not toward the salary amount in the 52-week period in which it was paid.

The Department is sensitive to concerns raised by employee representatives and some employer commenters that the bonuses provision may increase compliance costs and litigation. These effects, however, are mitigated by the fact that crediting nondiscretionary bonuses and incentive pay towards the standard salary level is purely optional. Employers, who would predominantly bear the cost of compliance and litigation expenses, are presumably best positioned to evaluate whether the potential costs of such crediting would outweigh the potential benefits. While the AFL–CIO contends that the bonuses proposal could theoretically ''lead to anomalous results, where employees working side by side performing the same job would be exempt and nonexempt, simply because inclusion of the bonus would raise one employee over the salary threshold[,]'' this has always been true of the salary level test, given that employees performing identical job duties may receive different salaries.

The Department emphasizes that this rulemaking does not change the requirement in § 541.601(b)(1) that highly compensated employees must receive at least the standard salary amount each pay period on a salary or fee basis without regard to the payment of nondiscretionary bonuses and incentive payments. While nondiscretionary bonuses and incentive payments (including commissions) may be counted toward the HCE total annual compensation requirement, the HCE test does not allow employers to credit these types of payments toward the standard salary requirement. The Department continues to believe that permitting employers to use nondiscretionary bonuses and incentive payments to satisfy the standard salary portion of the HCE test is not appropriate because employers are already permitted to fulfill more than three quarters of the HCE total annual compensation requirement with commissions, nondiscretionary bonuses, and other forms of nondiscretionary deferred compensation (paid at least annually). Thus, when conducting the HCE analysis, employers must remain mindful that HCEs must receive the full standard salary amount each pay period on a salary or fee basis.

Finally, nothing adopted in this final rule alters the Department's longstanding position that employers may pay their exempt EAP employees additional compensation of any form beyond the minimum amount needed to satisfy the salary basis and salary level tests. *See* § 541.604(a). Similarly, the Department emphasizes that nonexempt employees may continue to receive bonuses and incentive payments. Where nondiscretionary bonuses or incentive payments are made to nonexempt employees, the payments must be included in the regular rate when calculating overtime pay. The Department's regulations at §§ 778.208–.210 explain how to include nondiscretionary bonuses in the regular rate calculation.

D. Highly Compensated Employees

As noted in the NPRM, the Department's 2004 final rule created a new test under the EAP exemption, known as the highly compensated employee (HCE) test, based on the rationale that it is unnecessary to apply the standard duties test in its entirety to employees who earn at least a certain amount annually—an amount substantially higher than the annual equivalent of the weekly standard salary level—because such employees ''have almost invariably been found to meet all the other requirements of the regulations for exemption.'' [101] The HCE test combines a high compensation requirement with a less-stringent duties test.

To meet the HCE test, an employee must earn at least the amount specified in the regulation in total annual compensation and must customarily and regularly perform any one or more of the exempt duties or responsibilities of an executive, administrative, or professional employee.[102] This test applies ''only to employees whose primary duty includes performing office or non-manual work.'' [103] Such an employee must receive at least the standard salary level each pay period on a salary or fee basis, while the remainder of the employee's total annual compensation may include commissions, nondiscretionary bonuses, and other nondiscretionary compensation.[104] An employee is permitted to make a final ''catch-up'' payment ''during the last pay period or within one month after the end of the 52-week period'' to bring an employee's compensation up to the required level.[105] If an employee works for less than a full year, either because the employee is newly hired after the beginning of the 52-week period or ends the employment before the end of this period, the employee may still qualify for exemption under the HCE test if the employee receives a pro rata portion of the required annual compensation, based upon the number of weeks of employment.[106]

The Department stated in the NPRM that it continues to believe that the HCE test is a useful alternative to the standard salary level and duties tests for highly compensated employees.[107] At the time this level was initially set in 2004 at $100,000, the Department concluded that ''white collar'' employees who earn above this threshold would nearly always satisfy any duties test.[108] The Department proposed updating the HCE threshold to ensure that it remains a meaningful and appropriate standard when paired with the more-lenient HCE duties test. Specifically, the Department proposed setting the HCE threshold at the 90th percentile of all full-time salaried workers nationally using 2017 CPS data, then inflated to January 2020, resulting

[100] FMI, IFA, and other employer representatives requested giving employers more than one pay period to make any necessary catch-up payments, pointing out that the HCE test permits employers to make catch-up payments within one month after the end of the 52-week period used for that test. *See* 29 CFR 541.601(b)(2). The Department declines this request because this new provision specifically affects the standard salary level requirement, not additional income received on top of that threshold by highly compensated employees.

[101] 69 FR 22174 (quoting Weiss Report at 22).

[102] § 541.601(a).

[103] § 541.601(d).

[104] § 541.601(b)(1). However, total annual compensation does not include board, lodging, and other facilities, or payments for medical insurance, life insurance, retirement plans, or other fringe benefits. *Id.*

[105] § 541.601(b)(2).

[106] § 541.601(b)(3).

[107] 84 FR 10913.

[108] *Id.* The Department concluded that ''in the rare instances when these employees do not meet all other requirements of the regulations, a determination that such employees are exempt would not defeat the objectives of section 13(a)(1) of the Act.'' 69 FR 22174 (quoting Weiss Report at 22–23).

in a proposed HCE threshold of $147,414, of which $679 would have to be paid weekly on a salary or fee basis.[109]

The Department received fewer comments addressing the HCE proposal than on many other issues in the NPRM, and those who addressed the HCE proposal often did not provide detailed feedback. Nearly all the commenters on the HCE proposal were employer representatives, most of whom opposed the Department's proposal to increase the HCE compensation level to a level equal to the 90th percentile of all full-time salaried workers ($147,414). These commenters instead supported keeping the HCE level at $100,000, *see, e.g.,* HR Policy Association; National Association of Manufacturers; NRF, or increasing the HCE level but by a lower amount (resulting in a threshold between $100,000 and $147,414), *see, e.g.,* Chamber; National Lumber and Building Material Dealers Association; WFCA. For example, some commenters suggested lowering the percentile from 90 percent to 80 percent of full-time salaried employees nationwide. *See, e.g.,* Center for Workplace Compliance; WorldatWork. A few employer representatives noted that they did not object to the proposed HCE salary level. *See* ASTA; Credit Human Federal Credit Union. By and large, employee representatives did not specifically address the HCE proposal.[110]

Commenters who favored keeping the HCE threshold at $100,000 or increasing it by a lower amount expressed concern that the proposed level was so high as to put the HCE test for the EAP exemption out of reach for employers in lower-wage regions and industries. For example, the Chamber stated that such employers would not be able to access the HCE test ''on equal terms,'' because ''[w]hether an employee qualifies for exemption under the highly compensated test would depend more on where the employee works than how much the employer values the employee's duties.'' Some of these commenters suggested that the Department should calculate the HCE threshold using data from a lower-wage region of the country, such as the South Census Region or a subset thereof, which would result in a lower threshold than using a national data set. *See, e.g.,* Chamber; NRA. Others suggested that the Department should continue to use national data, but should lower the threshold by pegging the HCE threshold at the 80th percentile of full-time salaried workers, rather than the 90th percentile proposed in the NPRM. *See* Center for Workforce Opportunity; WorldatWork. WorldatWork asserted that this approach would ''result in a far more workable standard, given the fluctuation in weekly earnings in different parts of the country and in different industries'' and would still ''identify[ ] those individuals who should be eligible for a more relaxed duties test.''

Other commenters objected to the Department's proposed HCE threshold on the ground that it would require employers to reassess the exempt status of many employees using the standard duties test, rather than the simpler HCE test. The HR Policy Association and PPWO explained that ''[a] significant amount of administrative effort will be needed to determine that an employee who had been classified as exempt through application of the HCE test remains exempt under application of the standard duties test.'' The National Association of Manufacturers explained that this process ''is certain to be lengthy'' as ''employers will need to survey managers, conduct follow-up interviews, hold new budget discussions, and plan and implement changes to each individual employee's duties or status.''

The Department has considered the comments regarding the HCE test for exemption and decided to lower the percentile at which to set the HCE threshold from that proposed in the NPRM. The Department agrees with commenters that increasing the HCE threshold so dramatically would result in significant administrative burdens and compliance costs, including costs associated with reassessing the exempt status of many highly paid white collar workers under the standard duties test. Yet while employers would incur these burdens and costs, the vast majority of currently exempt HCE employees would remain exempt (under the standard test).[111] In short, the Department would be imposing significant administrative costs on employers for a limited effect. Additionally, the Department agrees with commenters that the proposed level was so high that it would have excluded employees who should be exempt under the provision, particularly those in lower-wage regions and industries. However, the Department disagrees with commenters who oppose any increase in the HCE threshold beyond the currently enforced level. The number of full-time salaried workers who earn above $100,000 per year has increased significantly.[112] The Department believes that some increase to the HCE threshold is necessary to ensure that the HCE threshold continues to provide a meaningful and appropriate complement to the more lenient HCE duties test.

Accordingly, the Department is setting the HCE total annual compensation level at the 80th percentile of full-time salaried workers nationally using pooled 2018/2019 CPS data.[113] This results in a level of $107,432, of which $684 must be paid weekly on a salary or fee basis.[114] The Department believes this threshold is sufficiently high to ensure that it provides a meaningful and appropriate complement to the more lenient HCE duties test, and that nearly all of the highly-paid white collar workers earning above this threshold ''would satisfy any duties test.'' Additionally, to be consistent with the methodology for setting the standard salary level, the Department now uses three-year pooled data to estimate the HCE compensation level. The Department further believes that this straightforward approach will lower administrative costs, as compared to the initial proposal, while still ensuring that nearly all of the highly paid white collar workers earning above this threshold ''would satisfy any duties test.'' [115]

E. Future Updates to the Earnings Thresholds

As the Department noted in the NPRM, even a well-calibrated salary

[109] 84 FR 10913–14. Consistent with the 2016 final rule, the Department's proposal did not permit employers to use nondiscretionary bonuses to satisfy the weekly standard salary level requirement for HCE workers. *Id.* at 10914 n.129. As previously stated, the Department believes that permitting employers to use nondiscretionary bonuses and incentive payments to satisfy the standard salary portion of the HCE test is not appropriate because employers are already permitted to fulfill the majority of the HCE total annual compensation requirement with commissions, nondiscretionary bonuses, and other forms of nondiscretionary deferred compensation (paid at least annually).

[110] At least one individual commenter supported the proposed increase in the HCE compensation level.

[111] In the economic analysis below in section VI.B.v, the Department estimated that, under the baseline scenario in which the HCE threshold remains at $100,000, approximately 9.3 million workers will pass both the standard and HCE tests and 343,000 will pass only the HCE test. Stated differently, of those workers who will earn at least $100,000, approximately 96.4 percent would pass the standard duties test.

[112] 84 FR 10913 n.123.

[113] In the NPRM, the Department used 2017 CPS data to set the HCE compensation level. *See id.* at 10913. To be consistent with the methodology for setting the standard salary level, in the final rule the Department is setting the HCE compensation level using pooled CPS data for July 2016 to June 2019, adjusted to reflect 2018/2019.

[114] The Department notes that no regional adjustment has been made to the HCE threshold in this final rule, just as this was not part of the determination of the HCE threshold in either the 2004 or 2016 final rules.

[115] 84 FR 10914 (internal citation omitted).

level that is fixed becomes obsolete as wages for nonexempt workers increase over time. Long lapses between rulemakings have resulted in EAP salary levels based on outdated salary data. Such levels are ill-equipped to help employers assess which employees are unlikely to meet the duties tests for the part 541 exemptions. As the Department noted in 2004, outdated regulations ''allow unscrupulous employers to avoid their overtime obligations and can serve as a trap for the unwary but well-intentioned employer;'' they can also lead increasing numbers of nonexempt employees to ''resort to lengthy court battles to receive their overtime pay.'' 69 FR 22212.

Throughout the years, various stakeholders have submitted comments asking the Department to establish a mechanism to update the thresholds automatically. The Department has twice declined such requests, once in 1970, when it concluded that ''such a proposal [would] require further study,'' 35 FR 884, and once in 2004, 69 FR 22171–72. However, in the 2016 final rule, the Department for the first time adopted a mechanism to automatically update the earnings thresholds every three years, applying the same methodology used to initially set each threshold in that rulemaking. 81 FR 32430. The district court's summary judgment decision invalidating the 2016 final rule stated that because the standard salary level established by the 2016 final rule was unlawful, the mechanism to automatically update that standard salary level was ''similarly . . . unlawful.''[116]

In the NPRM, the Department expressed its intent to evaluate the part 541 earnings thresholds more frequently through rulemaking. 84 FR 10914–15. Specifically, the Department stated in the NPRM that it intended to propose updates to the standard salary level and HCE total compensation threshold on a quadrennial basis (*i.e.,* once every four years) through notice-and-comment rulemaking, and that each proposal would use the same methodology as the most recently published final rule. The Secretary, however, could forestall proposed updates if economic or other factors so indicated. The Department also described how it could revise the part 541 regulations if it were to codify this intention in a final rule. *Id.* at 10915 n.140.

Some commenters supported the Department's proposal to propose updates to the earnings thresholds every four years unless unwarranted due to economic or other factors. *See* National Association of Convenience Stores; National Association of Landscape Professionals; NGA; National Multifamily Housing Council and the National Apartment Association; SBA Advocacy. These commenters generally agreed that the Department's proposal would help the salary level keep pace with earnings growth, thus preventing dramatic increases after long gaps between updates. *See, e.g.,* Credit Union National Association; Joint Comment from Golf Industry Representatives. Many of these commenters specifically expressed support for the Department's proposal to use notice-and-comment rulemaking to set future salary thresholds; such as NAHB, which commented that ''[b]y continuing its current practice of engaging the regulated community . . . DOL will receive timely and important information as it moves forward with proposed updates in the future.'' Commenters who supported the Department's proposal generally characterized this reliance on notice-and-comment rulemaking as preferable to the 2016 final rule's automatic updating provision, *see, e.g.,* Job Creators Network; Joint Comment of 5 Senators, with some asserting that automatic updating, without notice-and-comment rulemaking, would be unlawful, *see, e.g.,* Joint Comment by International Public Management Association for Human Resources and others; SIGMA.

Other commenters did not support the Department's commitment to evaluate the thresholds regularly. Many commenters felt that there was no need to adhere to a fixed schedule, with some asserting that doing so could deprive the Department of flexibility to adapt to unanticipated circumstances. These commenters advocated for the Department to continue its practice of updating the salary whenever it deems such updates appropriate. *See, e.g.,* AGC; Argentum and American Seniors Housing Association; HR Policy Association; Independent Bakers Association. A few commenters questioned the Department's authority to bind itself to conducting regular evaluations of the salary level. *See* AHLA; PPWO. Others felt that the proposed updating framework could expose the Department to legal risk because parties might challenge a decision by the Department not to engage in the anticipated rulemaking. *See* Associated Builders and Contractors; FMI. Some commenters who opposed the updating proposal asserted that it was unnecessary since the Department can engage in rulemaking at any time. *See* Associated Builders and Contractors, FMI, NRA.

Other commenters, including employee representatives, took the opposite tack, requesting that the Department automatically update the salary thresholds. *See, e.g.,* Center for Popular Democracy; Demos; Oxfam America. Some of these commenters asserted that past experience, including the long gaps between the most recent updates, has demonstrated that in the absence of regular updates, the salary level becomes obsolete, and that an announced intent to propose updates does not sufficiently ensure that the levels will, in fact, be updated. *See, e.g.,* AARP; Joint Comment from 77 Members of Congress; Nichols Kaster. Many commenters who favored automatic updating specifically supported the updating provision that was included in the 2016 final rule. *See* AARP; NELA; NELP; NWLC; State AGs; The Leadership Conference on Civil and Human Rights. Some maintained that the lack of automatic updating would result in decreased earnings for workers, citing EPI's estimates that the gap in projected earnings transfers to workers between the 2016 final rule and the proposal would increase from $1.2 billion to $1.6 billion due to the lack of automatic updates. *See, e.g.,* EPI; NELP; UAW. NELP further stated that ''[i]ndexing would ensure predictability for workers and employers alike and eliminate the need for time-consuming federal regulations.''

A number of commenters generally supported regular updates to the earnings thresholds, but suggested a frequency other than every four years. For instance, ASTA suggested that a six-year gap ''would strike a better balance in recognizing [its] and [its] member employers' legitimate concerns . . . than the four-year interval included in the NPRM.'' The Pennsylvania Credit Union Association wrote in support of updating the thresholds no less frequently than every three years, while Representative Daniel Lipinski ''urge[d] the Department to review the [standard salary] threshold more frequently than once every four years.'' AFSCME supported annual updates.

In this final rule, the Department reaffirms its intent to update the standard salary level and HCE total annual compensation threshold more regularly in the future using notice-and-comment rulemaking. The Department agrees with those commenters who stated that long periods without updates serve neither employee nor employer interests, since they diminish the usefulness of the salary level test and cause future increases to be larger and

[116] 275 F. Supp. 3d at 808.

more challenging for businesses to absorb. Regular updates, on the other hand, ensure that the salary level test is based on the best available data (and thus remains a meaningful, bright-line test), produce more predictable and incremental changes in the salary level, and therefore provide certainty to employers and promote government efficiency.

After reviewing the comments received on this issue, however, the Department declines to finalize its proposal to propose updates to the part 541 regulations quadrennially. The Department agrees with commenters who stated that this commitment could deprive the Department of flexibility to adapt to unanticipated circumstances, and believes that prevailing economic conditions, rather than fixed timelines, should drive future updates. While some commenters supported the Department's updating proposal, the reasons often underlying that support—*e.g.,* the benefits of notice-and-comment rulemaking and of salary levels that keep pace with earnings growth—are not necessarily tied to updates occurring on a predetermined schedule, and would be met by the Department updating the salary thresholds more regularly. In addition, that many commenters who supported regular updates nonetheless disagreed on the optimal updating frequency reaffirms the Department's approach, as does the fact that few, if any, commenters supported the Department codifying its intent to propose updates quadrennially.

The Department's intention to update the part 541 regulations more regularly using notice-and-comment rulemaking will also ensure ample opportunity for public input, and provide the Department with the flexibility to update the earnings thresholds in a manner that is tailored to wages and economic conditions at the time of the update. Because the Department believes that it is important to preserve the Department's flexibility to adapt to different types of circumstances, the Department declines the suggestions by employee representatives to adopt an automatic updating mechanism as in the 2016 final rule. Lastly, while the Department understands commenter concerns regarding the lengthy time periods between recent rulemakings, in this final rule the Department is reaffirming its commitment to better implement Congress's instruction to define and delimit the EAP exemptions ''from time to time'' [117] through regulations. Regular updates ensure that the salary level test continues to screen from exemption obviously nonexempt employees who are unlikely to be performing the duties of bona fide executive, administrative, or professional employees.

[117] 29 U.S.C. 213(a)(1).

V. Paperwork Reduction Act

The Paperwork Reduction Act of 1995 (PRA), 44 U.S.C. 3501 *et seq.,* and its attendant regulations, 5 CFR part 1320, require that the Department consider the impact of paperwork and other information collection burdens imposed on the public. Under the PRA an agency may not collect or sponsor the collection of information, nor may it impose an information collection requirement, unless it displays a currently valid Office of Management and Budget (OMB) control number. *See* 5 CFR 1320.8(b)(3)(vi). OMB has assigned control number 1235–0018 to the Fair Labor Standards Act (FLSA) information collections. OMB has assigned control number 1235–0021 to Employment Information Form collections, which the Department uses to obtain information from complainants regarding FLSA violations.

In accordance with the PRA, the Department solicited comments on the FLSA information collections and the Employment Information Form collections in the NPRM published March 22, 2019, *see* 84 FR 10900, as the NPRM was expected to impact these collections. 44 U.S.C. 3506(c)(2). The Department also submitted a contemporaneous request for OMB review of the proposed revisions to the FLSA information collections, in accordance with 44 U.S.C. 3507(d). On May 20, 2019, OMB issued a notice for each collection (1235–0018 and 1235–0021) that continued the previous approval of the FLSA information collections and the Employment Information Form collections under the existing terms of clearance. OMB asked the Department to resubmit the information collection request upon promulgation of the final rule and after considering public comments on the proposed rule.

Circumstances Necessitating Collection: The FLSA, 29 U.S.C. 201 *et seq.,* sets the federal minimum wage, overtime pay, recordkeeping, and youth employment standards of most general application. Section 11(c) of the FLSA requires all employers covered by the FLSA to make, keep, and preserve records of employees and of wages, hours, and other conditions and practices of employment. An FLSA covered employer must maintain the records for such period of time and make such reports as prescribed by regulations issued by the Secretary of Labor. The Department has promulgated regulations at part 516 to establish the basic FLSA recordkeeping requirements, which are approved under OMB control number 1235–0018.

FLSA section 11(a) provides that the Secretary of Labor may investigate and gather data regarding the wages, hours, or other conditions and practices of employment in any industry subject to the FLSA, and may enter and inspect such places and such records (and make such transcriptions thereof), question such employees, and investigate such facts, conditions, practices, or matters deemed necessary or appropriate to determine whether any person has violated any provision of the FLSA. 29 U.S.C. 211(a). The information collection approved under OMB control number 1235–0021 provides a method for the Wage and Hour Division of the U.S. Department of Labor to obtain information from complainants regarding alleged violations of the labor standards the agency administers and enforces. This final rule revises the existing information collections previously approved under OMB control number 1235–0018 (Records to be Kept by Employers—Fair Labor Standards Act) and OMB control number 1235–0021 (Employment Information Form).

This final rule does not impose new information collection requirements; rather, burdens under existing requirements are expected to increase as more employees receive minimum wage and overtime protections due to the proposed increase in the salary level requirement. More specifically, the changes adopted in this final rule may cause an increase in burden on the regulated community because employers will have additional employees to whom certain long-established recordkeeping requirements apply (*e.g.,* maintaining daily records of hours worked by employees who are not exempt from both the minimum wage and overtime provisions). Additionally, the changes adopted in this final rule may cause an initial increase in burden if more employees file complaints with WHD to collect back wages under the overtime pay requirements.

Public Comments: The Department sought public comments regarding the burdens imposed by information collections contained in the proposed rule. The Department received few comments relevant to the PRA. A few commenters stated that employers would need to maintain records of hours worked for more employees as a result of an increase to the salary level.

See, International Bancshares Corporation; Washington Nonprofits. A few individual commenters expressed concerns surrounding costs associated with additional recordkeeping. A CEO of a professional placement firm indicated that tracking of hours would produce increased human resources paperwork and technology costs. Smith Summerset commented that those employers who take advantage of the allowance for up to ten percent of nondiscretionary bonuses and incentive payments to meet the standard salary level will have to maintain records documenting the applicable annual periods and detailing earnings and all payments (including catch-up payments) for each affected worker, including records such employers were not previously required to maintain.

In response to these comments, the Department notes that most employers currently have both exempt and nonexempt workers and therefore have systems already in place for employers to track hours. The Department also notes that commenters did not offer alternatives for estimates or make suggestions regarding the methodology for calculating the PRA burdens. The actual recordkeeping requirements are not changing in the final rule. However, the pool of workers for whom employers will be required to make and maintain records has increased under the final rule, and as a result the burden hours have increased. Included in this PRA section are the regulatory familiarization costs for this final rule. We note, however, that this is a duplication of the regulatory familiarization costs contained in the economic impact analysis, *see* section VI.

An agency may not conduct an information collection unless it has a currently valid OMB approval, and the Department has submitted the identified information collection contained in the proposed rule to OMB for review under the PRA under the Control Numbers 1235–0018 and 1235–0021. *See* 44 U.S.C. 3507(d); 5 CFR 1320.11. The Department has resubmitted the revised FLSA information collections to OMB for approval, and intends to publish a notice announcing OMB's decision regarding this information collection request. A copy of the information collection request can be obtained at *http://www.Reginfo.gov* or by contacting the Wage and Hour Division as shown in the **FOR FURTHER INFORMATION CONTACT** section of this preamble.

Total annual burden estimates, which reflect both the existing and new responses for the recordkeeping and complaint process information collections, are summarized as follows:

Type of Review: Revisions to currently approved information collections.

Agency: Wage and Hour Division, Department of Labor.

Title: Records to be Kept by Employers—Fair Labor Standards Act.

OMB Control Number: 1235–0018.

Affected Public: Private sector businesses or other for-profits, farms, not-for-profit institutions, state, local and tribal governments, and individuals or households.

Estimated Number of Respondents: 5,621,961 (2,616,667 by this rulemaking).

Estimated Number of Responses: 46,959,856 (2,616,667 added by this rulemaking).

Estimated Burden Hours: 3,625,986 hours (2,616,667 added by this rulemaking).

Estimated Time per Response: Various (unaffected by this rulemaking).

Frequency: Various (unaffected by this rulemaking).

Other Burden Cost: 0.

Title: Employment Information Form.

OMB Control Number: 1235–0021.

Affected Public: Businesses or other for-profit, farms, not-for-profit institutions, state, local and tribal governments, and individuals or households.

Total Respondents: 36,278 (651 added by this rulemaking).

Estimated Number of Responses: 36,278 (651 added by this rulemaking).

Estimated Burden Hours: 12,155 (217 hours added by this rulemaking).

Estimated Time per Response: 20 minutes (unaffected by this rulemaking).

Frequency: Once.

Other Burden Cost: 0.

VI. Analysis Conducted in Accordance With Executive Order 12866, Regulatory Planning and Review, and Executive Order 13563, Improving Regulation and Regulatory Review

Executive Orders 12866 and 13563 direct agencies to assess the costs and benefits of a regulation and to adopt a regulation only upon a reasoned determination that the regulation's net benefits (including potential economic, environmental, public health and safety effects, distributive impacts, and equity) justify its costs. Executive Order 13563 emphasizes the importance of quantifying both costs and benefits, reducing costs, harmonizing rules, and promoting flexibility.

Under Executive Order 12866, the Office of Management and Budget (OMB) determines whether a regulatory action is a ''significant regulatory action,'' which includes an economically significant action that has an annual effect of $100 million or more on the economy. Significant regulatory actions are subject to review by OMB. As described below, this final rule is economically significant.

When the Department uses a perpetual time horizon to allow for cost comparisons under Executive Order 13771,[118] the annualized cost savings of the final rule is $534.8 million with 7 percent discounting. This final rule is accordingly expected to be an Executive Order 13771 deregulatory action.

A. Introduction

i. Background

The FLSA requires covered employers to: (1) Pay employees who are covered and not exempt from the Act's requirements not less than the federal minimum wage for all hours worked and overtime premium pay at a rate of not less than one and one-half times the employee's regular rate of pay for all hours worked over 40 in a workweek, and (2) make, keep, and preserve records of their employees and of the wages, hours, and other conditions and practices of employment.

The FLSA provides a number of exemptions from the Act's minimum wage and overtime pay provisions, including one for bona fide executive, administrative, and professional (EAP) employees. The exemption applies to employees employed in a bona fide executive, administrative, or professional capacity and to outside sales employees, as those terms are ''defined and delimited'' by the Department.[119] The Department's regulations implementing these ''white collar'' exemptions are codified at 29 CFR part 541.

In 2004, the Department determined that two earnings level tests should be used to help employers distinguish nonexempt employees from exempt employees: The standard salary test, which it set at $455 a week, and the highly compensated employee (HCE) total-compensation test, which it set at $100,000 per year (see section II.C for further discussion). In 2016, the Department published a final rule setting the standard salary level at $913 per week and the HCE annual compensation level at $134,004. As previously discussed, the U.S. District Court for Eastern District of Texas declared the 2016 final rule invalid.

ii. Need for Rulemaking

The Department has updated the salary level test many times since its implementation in 1938. Table 1 presents the weekly salary levels

[118] 82 FR 9339 (Feb. 3, 2017).

[119] 29 U.S.C. 213(a)(1).

associated with the EAP exemptions since 1938, organized by exemption and long/short/standard duties tests.[120] In the 37 years between 1938 and 1975, the Department increased salary test levels approximately every five to nine years. In subsequent years, the Department revised the levels less frequently, and it is currently enforcing the levels set in 2004.[121]

TABLE 1—HISTORICAL SALARY LEVELS FOR THE EAP EXEMPTIONS

Date enacted	Long test			Short test (all)
	Executive	Administrative	Professional	
1938	$30	$30		
1940	30	50	$50	
1949	55	75	75	$100
1958	80	95	95	125
1963	100	100	115	150
1970	125	125	140	200
1975	155	155	170	250
	Standard test			
2004	$455			

To restore the value of the standard salary level as a line of demarcation between those workers for whom Congress clearly intended to provide minimum wage and overtime protections and other workers who may be bona fide EAPs, and to maintain the salary level's continued validity, the Department is updating the standard salary level by applying the 2004 methodology to current Current Population Survey (CPS) data.[122] Using pooled CPS Merged Outgoing Rotation Group (MORG) [123] data to represent the July 2018 through June 2019 period (hereafter referred to as 2019), the salary level of $684 ($35,568 annually) set in this final rule corresponds to the 20th percentile of earnings for full-time salaried workers in the South Census Region and/or in the retail industry.[124] [125] Similarly, the Department used the pooled 2018/19 CPS MORG data to set the updated HCE total annual compensation requirement at $107,432, which is the earnings for the 80th percentile of all full-time salaried workers nationally.

iii. Summary of Affected Workers, Costs, Benefits, and Transfers

The Department estimated the number of affected workers and quantified costs and transfer payments associated with this final rule, using the currently-enforced 2004 salary level as the baseline. To produce these estimates, the Department used pooled CPS MORG data. *See* section VI.B.ii. Most critically, the Department estimates that 1.2 million workers who would otherwise be exempt under the currently-enforced standard salary level of $455 per week will either become eligible for overtime or have their salary increased to at least $684 per week, and that 4.1 million employees paid between $455 and $684 per week who fail the standard duties test (*i.e.,* that are and will remain nonexempt) will have their overtime eligibility made clearer because their salary will fall below the specified threshold (Table 2).[126] Additionally, an estimated 101,800 workers will be affected by the increase in the HCE compensation test from $100,000 per year to $107,432 per year using the pooled 2018/19 CPS MORG data. By Year 10, the Department estimates that 723,000 workers will be affected by the change in the standard salary level test and 154,000 workers will be affected by the change in the HCE total annual compensation test, compared to a baseline assuming the currently-enforced earnings thresholds (*i.e.,* $455 per week and $100,000 per year) remain unchanged.[127]

This analysis quantifies three direct costs to employers: (1) Regulatory familiarization costs; (2) adjustment costs; and (3) managerial costs (*see* section VI.D.iii for further discussion on costs). The costs presented here are the combined costs for both the change in the standard salary level test and the HCE total annual compensation level (these will be disaggregated in section VI.D.iii). Total annualized direct employer costs over the first 10 years

[120] From 1949 until 2004 the regulations contained two different tests for exemption—a long test for employees paid a lower salary that included a more rigorous examination of employees' duties, and a short test for employees paid at a higher salary level that included a more flexible duties test. The standard duties test is used in conjunction with the standard salary level test, as set in 2004 and applied to date, to determine eligibility for the EAP exemptions. It replaced the short and long tests in effect from 1949 to 2004.

[121] In 2016, the Department issued a final rule revising the EAP salary levels; however, on August 31, 2017, the U.S. District Court for Eastern District of Texas held that the 2016 final rule's standard salary level exceeded the Department's authority and was therefore invalid. *See Nevada* v. *U.S. Dep't of Labor,* 275 F. Supp. 3d 795 (E.D. Tex. 2017). Until the Department issues a new final rule, it is enforcing the part 541 regulations in effect on November 30, 2016, including the $455 per week standard salary level set in the 2004 final rule.

[122] The Department also notes that the terms *employee* and *worker* are used interchangeably throughout this analysis.

[123] The Merged Outgoing Rotation Group is a supplement to the CPS and is conducted on approximately one-fourth of the CPS sample monthly to obtain information on weekly hours worked and earnings.

[124] Excluding workers who are not subject to the FLSA, not subject to the salary level test, or in agriculture or transportation.

[125] As previously explained, in the 2004 final rule, the Department looked to the 20th percentile of full-time salaried workers in the South and in the retail industry nationally to validate the standard salary level set in the final rule. In this final rule, the Department set the standard salary level at the 20th percentile of the combined subpopulations of full-time salaried employees in the South and full-time salaried employees in the retail industry nationwide. Accordingly, the use of ''and/or'' when describing the salary level methodology in this final rule reflects that this data set includes full-time salaried workers who work: (1) In the South but not in the retail industry; (2) in the retail industry but not in the South; and (3) in the south in the retail industry.

[126] Here and elsewhere in this analysis, numbers are reported at varying levels of aggregation, and are generally rounded to a single decimal point. However, calculations are performed using exact numbers. Therefore, some numbers may not match the reported totals or the calculations shown due to rounding of components.

[127] In later years, earnings growth will cause some workers to no longer be affected because their earnings will exceed the new salary threshold. Additionally, some workers will become newly affected because their earnings will exceed $455 per week, and in the absence of this final rule would have lost their overtime protections. To estimate the total number of affected workers over time, the Department accounts for both of these effects.

were estimated to be $173.3 million, assuming a 7 percent discount rate (Table 2).[128]

In addition to the costs described above, this rule will also transfer income from employers to employees in the form of wages. The Department estimated annualized transfers will be $298.8 million. The majority of these transfers will be attributable to the FLSA's overtime provision; a smaller share will be attributable to the FLSA's minimum wage requirement. Transfers also include salary increases for some affected EAP workers [129] to preserve their exempt status. Employers may incur additional costs, such as hiring new workers. These other potential costs are discussed in section VI.D.iii. Potential benefits of this rule could not be quantified due to data limitations, requiring the Department to discuss such benefits qualitatively. *See* § VI.D.v.

TABLE 2—SUMMARY OF REGULATORY COSTS AND TRANSFERS, STANDARD AND HCE SALARY LEVELS

[Millions in 2019$]

Impact	Year 1	Future years [a]		Annualized value	
		Year 2	Year 10	3% real discount rate	7% real discount rate
Affected Workers (1,000s)					
Standard	1,156	1,069	723		
HCE	101.8	114	154		
Total	1,257	1,183	877		
Costs and Transfers (Millions in 2019$) [b]					
Direct employer costs	$543.0	$134.3	$99.1	$164.0	$173.3
Transfersthnsp;[c]	396.4	307.7	247.4	295.0	298.8

[a] These cost and transfer figures represent a range over the nine-year span.
[b] Costs and transfers for affected workers passing the standard and HCE tests are combined.
[c] This is the net transfer from employers to workers. There may also be transfers of hours and income from some workers to others.

B. Methodology To Determine the Number of Potentially Affected EAP Workers

i. Overview

This section explains the methodology used to estimate the number of workers who are subject to the part 541 regulations and the number of potentially affected EAP workers. In this final rule, as in the 2004 final rule, the Department estimated the number of EAP exempt workers because there is no data source that identifies workers as EAP exempt. Employers are not required to report EAP exempt workers to any central agency or as part of any employee or establishment survey.[130] The methodology described here is largely based on the approach the Department used in the 2004 and 2016 final rules.[131]

ii. Data

The estimates of EAP exempt workers were based on data drawn from the CPS MORG, which is sponsored jointly by the U.S. Census Bureau and BLS. The CPS is a large, nationally representative sample of the labor force. Households are surveyed for four months, excluded from the survey for eight months, surveyed for an additional four months, then permanently dropped from the sample. During the last month of each rotation in the sample (month 4 and month 16), employed respondents complete a supplementary questionnaire in addition to the regular survey.[132] This supplement contains the detailed information on earnings necessary to estimate a worker's exemption status. Responses are based on the reference week, which is always the week that includes the 12th day of the month.

Although the CPS MORG is a large scale survey, administered to approximately 15,000 households monthly representing the entire nation, it is still possible to have relatively few observations when looking at subsets of employees, such as exempt workers in a specific occupation employed in a specific industry, or workers in a specific geographic location. To increase the sample size, the Department pooled together three years of CPS MORG data (July 2016 through June 2019) to represent the single year from July 2018 through June 2019. Earnings for each observation from the last six months of 2016, 2017, and the first six months of 2018 were inflated to 2018/19 dollars using the Consumer Price Index for All Urban Consumers (CPI–U). For ease of presentation and because inflation is low enough for this to be trivial, these will be referred to as 2019 dollars throughout this analysis. The weight of each observation was adjusted so that the total number of potentially affected EAP workers in the pooled sample remained the same as the number for the July 2018 through June 2019 CPS MORG. Thus, the pooled CPS MORG sample uses roughly three times as many observations to represent the same total number of workers in 2018/19. The additional observations allow the Department to better characterize certain attributes of the potentially affected labor force. This pooled dataset

[128] Hereafter, unless otherwise specified, annualized values will be presented using the 7 percent real discount rate.

[129] The term affected EAP workers refers to the population of potentially affected EAP workers who either pass the standard duties test and earn at least $455 but less than the new salary level of $684, or pass only the HCE duties test and earn at least $100,000 but less than the new HCE compensation level of $107,432. This was estimated to be 1.3 million workers.

[130] In 2015, RAND released results from a survey conducted to estimate EAP exempt workers. However, this survey does not have the variables or sample size necessary for the Department to base the RIA on this analysis. Rohwedder, S. and Wenger, J.B. (2015). The Fair Labor Standards Act: Worker Misclassification and the Hours and Earnings Effects of Expanded Coverage. RAND Labor and Population.

[131] *See* 69 FR 22196–209; 81 FR 32453–60. Where the proposal follows the methodology used to determine affected workers in both the 2004 and 2016 final rules citations to both rules are not always included.

[132] This is the outgoing rotation group (ORG); however, this analysis uses the data merged over twelve months and thus will be referred to as MORG.

is used to estimate all impacts of the final rulemaking.[133]

Some assumptions were necessary to use these data as the basis for the analysis. For example, the Department eliminated workers who reported that their weekly hours vary and provided no additional information on hours worked. This was done because the Department cannot estimate effects for these workers since it is unknown whether they work overtime and therefore unknown whether there would be any need to pay for overtime if their status changed from exempt to nonexempt. The Department reweighted the rest of the sample to account for this change (*i.e.,* to keep the same total employment estimates).[134] This adjustment assumes that the distribution of hours worked by workers whose hours do not vary is representative of hours worked by workers whose hours do vary. The Department believes that without more information this is an appropriate assumption.[135]

iii. Number of Workers Covered by the Department's Part 541 Regulations

To estimate the number of workers covered by the FLSA and subject to the Department's part 541 regulations, the Department excluded workers who are not subject to its regulations or whom the FLSA does not cover. This may happen, for instance, if a worker is not an employee under the FLSA. Excluded workers include military personnel, unpaid volunteers, self-employed individuals, clergy and other religious workers, and federal employees (with a few exceptions described below).

Many of these workers are excluded from the CPS MORG, including members of the military on active duty and unpaid volunteers. Self-employed and unpaid workers are included in the CPS MORG, but have no earnings data reported and thus are excluded from the analysis. The analysis excluded religious workers identified by their occupation codes: 'clergy' (Census occupational code 2040), 'directors, religious activities and education' (2050), and 'religious workers, all other' (2060). Most employees of the federal government are covered by the FLSA but not the Department's part 541 regulations because the Office of Personnel Management (OPM) regulates their entitlement to minimum wage and overtime pay.[136] Exceptions exist for U.S. Postal Service employees, Tennessee Valley Authority employees, and Library of Congress employees.[137] The analysis identified and included these covered federal workers using occupation and/or industry codes.[138] The FLSA also does not cover employees of firms that have annual revenue of less than $500,000 and who are not engaged in interstate commerce. The Department does not exclude them from the analysis, however, because there is no data set that would adequately inform an estimate of the size of this worker population, although the Department believes it is a small percentage of workers. The 2004 final rule analysis similarly did not adjust for these workers.

The Department estimated that in Year 1 there will be 164.5 million wage and salary workers in the United States (Figure 1). Of these, 139.4 million will be covered by the FLSA and subject to the Department's regulations (84.7 percent). The remaining 25.1 million workers will be excluded from FLSA coverage for the reasons described above. Figure 1 illustrates how the Department analyzed the U.S. civilian workforce through successive stages to estimate the number of potentially affected EAP workers.

[133] A few commenters commented on the Department's use of CPS data to calculate the salary level. EPI and NELP asked the Department to set the salary thresholds using a data series that BLS publishes on a regular basis, while the Chamber asked the Department to publish the data sets used to set the salary thresholds. The Department calculated the standard salary level and the HCE total annual compensation level using publicly-available CPS microdata (compiled by the U.S. Census Bureau). The Department has frequently set the salary level using its own enforcement data and/or data that is not publicly available, and believes that using publicly available CPS data to calculate the salary level in this final rule is appropriate.

[134] The Department also reweighted for workers reporting zero earnings. In addition, the Department eliminated, without reweighting, workers who both reported usually working zero hours and working zero hours in the past week.

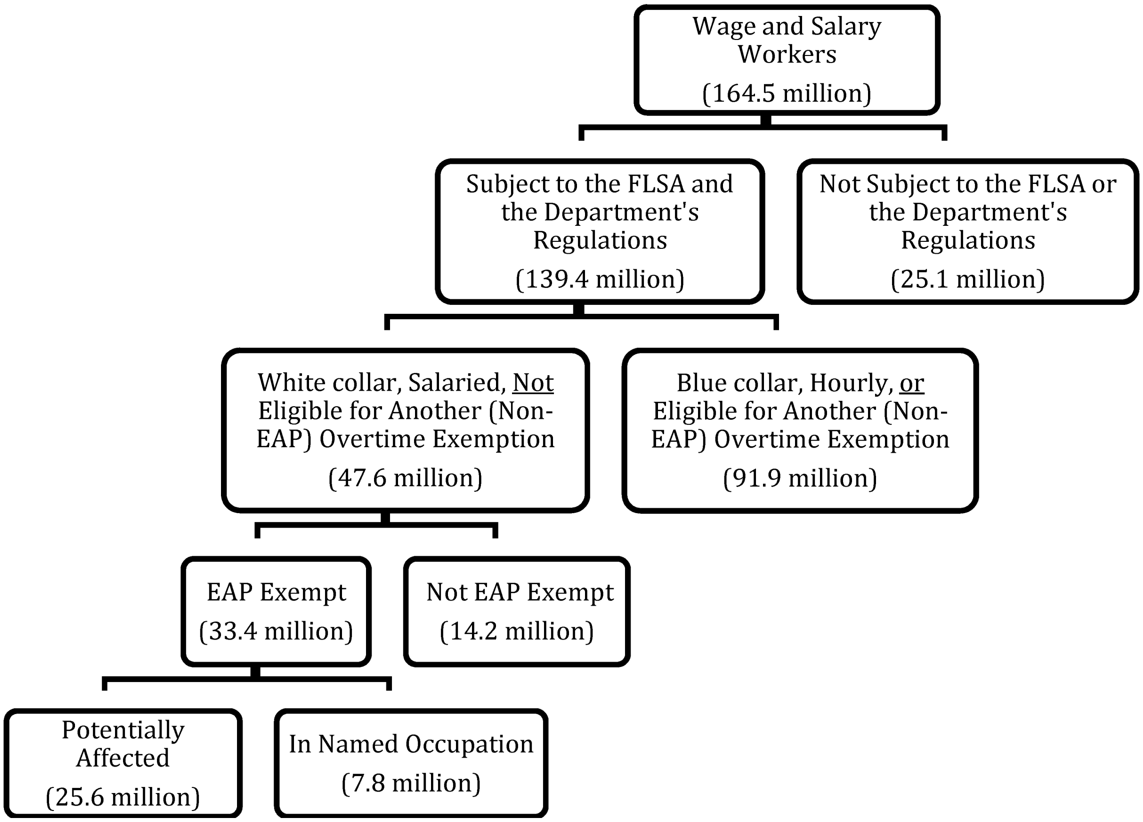
[135] This is justifiable because demographic and employment characteristics are similar across these two populations (*e.g.,* age, gender, education, distribution across industries, share paid nonhourly). The share of all workers who stated that their hours vary (but provided no additional information) is 5.0 percent. To the extent these excluded workers are exempt, if they tend to work more overtime than other workers, then transfer payments and costs may be underestimated. Conversely, if they work fewer overtime hours, then transfer payments and costs may be overestimated.

[136] *See* 29 U.S.C. 204(f). Federal workers are identified in the CPS MORG with the class of worker variable PEIO1COW.

[137] *See id.*

[138] Postal Service employees were identified with the Census industry classification for postal service (6370). Tennessee Valley Authority employees were identified as federal workers employed in the electric power generation, transmission, and distribution industry (570) and in Kentucky, Tennessee, Mississippi, Alabama, Georgia, North Carolina, or Virginia. Library of Congress employees were identified as federal workers under Census industry 'libraries and archives' (6770) and residing in Washington DC

Figure 1: Flow Chart of FLSA Exemptions and Estimated Number of Potentially Affected Workers



iv. Number of Workers in the Analysis

After limiting the analysis to workers covered by the FLSA and subject to the Department's part 541 regulations, several other groups of workers were identified and excluded from further analysis since this final rule is unlikely to affect them. These include blue collar workers, workers paid on an hourly basis, and workers who are exempt under certain other (non-EAP) exemptions.

The Department excluded a total of 91.9 million workers from the analysis for one or more of these reasons, which often overlapped (*e.g.,* many blue collar workers are also paid hourly). The Department estimated that in 2018/19 there were 50.0 million blue collar workers. These workers were identified in the CPS MORG data following the methodology from the U.S. Government Accountability Office's (GAO) 1999 white collar exemptions report [139] and the Department's 2004 regulatory impact analysis. *See* 69 FR 22240–44. Supervisors in traditionally blue collar industries were classified as white collar workers because their duties are generally managerial or administrative, and therefore they were not excluded as blue collar workers. Using the CPS variable indicating a respondent's hourly wage status, the Department determined that 81.9 million workers were paid on an hourly basis in 2018/19.[140]

Also excluded from further analysis were workers who were exempt under certain other (non-EAP) exemptions. Although some of these workers may also be exempt under the EAP exemptions, they would independently remain exempt from the minimum wage and/or overtime pay provisions based on the non-EAP exemptions. The Department excluded an estimated 5.0 million workers, including some agricultural and transportation workers, from further analysis because they would be subject to another (non-EAP) overtime exemption. *See* Appendix A: Methodology for Estimating Exemption Status, contained in the rulemaking docket, for details on how this population was identified.

Agricultural and transportation workers are two of the largest groups of workers excluded from the population of potentially affected EAP workers in the current analysis, and with some exceptions, they were similarly excluded in 2004. The 2004 final rule excluded all workers in agricultural industries from the analysis,[141] while the current analysis, similar to the 2016 analysis, only excludes agricultural workers from specified occupational-industry combinations since not all workers in agricultural industries qualify for the agricultural overtime pay exemptions. The exclusion of transportation workers matched the method for the 2004 final rule. Transportation workers were defined as those who are subject to the following FLSA exemptions: Section 13(b)(1), section 13(b)(2), section 13(b)(3), section 13(b)(6), or section 13(b)(10). The Department excluded 1.1 million agricultural workers and 2.1 million transportation workers from the analysis. In addition, the Department excluded another 1.9 million workers who fall within one or more other FLSA minimum wage and overtime

[139] GAO/HEHS. (1999). Fair Labor Standards Act: White Collar Exemptions in the Modern Work Place. GAO/HEHS–99–164, 40–41, *https://www.gao.gov/assets/230/228036.pdf.*

[140] CPS MORG variable PEERNHRY.

[141] 69 FR 22197.

exemptions. The criteria for determining exempt status for agricultural and transportation workers are detailed in Appendix A. However, of these 1.9 million workers, all but 20,000 are either blue collar or hourly, and thus the effect of excluding these workers is negligible.

v. Number of Potentially Affected EAP Workers

After excluding workers not subject to the Department's FLSA regulations and workers who are unlikely to be affected by this final rule (*i.e.,* blue collar workers, workers paid hourly, workers who are subject to another (non-EAP) overtime exemption), the Department estimated there will be 47.6 million salaried white collar workers for whom employers might claim either the standard EAP exemption or the HCE exemption. To be exempt under the standard EAP test, the employee must:

• Be paid a predetermined and fixed salary that is not subject to reduction because of variations in the quality or quantity of work performed (the salary basis test); [142]

• earn at least a designated salary amount (the 2004 final rule set the salary level at $455 per week (the standard salary level test)); and

• primarily perform exempt work, as defined by the regulations (the standard duties test).

The 2004 final rule's HCE test allows certain highly-paid employees to qualify for exemption as long as they customarily and regularly perform one or more exempt job duties. The HCE annual compensation level set in the 2004 final rule was $100,000, including at least $455 per week paid on a salary or fee basis. The CPS annual earnings variable is topcoded at $150,000 (*i.e.,* workers earning above $2,884.61 ($150,000/52 weeks) per week are reported as earning $2,884.61 per week). The Department imputed earnings for topcoded workers in the CPS data to adequately estimate the cost savings of this rule in comparison to the 2016 final rule under E.O. 13771.[143] [144]

Salary Basis

The Department included only nonhourly workers in the analysis based on CPS data.[145] For this rulemaking, the Department considered data representing compensation paid to nonhourly workers to be an appropriate proxy for compensation paid to salaried workers. The Department notes that it made the same assumption regarding nonhourly workers in the 2004 final rule.[146]

The CPS population of ''nonhourly'' workers includes workers who are paid on a piece-rate, a day-rate, or largely on bonuses or commissions. Data in the CPS are not available to distinguish between salaried workers and these other nonhourly workers. However, the Panel Study of Income Dynamics (PSID) provides additional information on how nonhourly workers are paid. In the PSID, respondents are asked how they are paid on their main job and are also asked for more detail if their response is other than salaried or hourly. Possible responses include piecework, commission, self-employed/farmer/profits, and by the job/day/mile. The Department analyzed the PSID data and found that relatively few nonhourly workers were paid by methods other than salaried. The Department is not aware of any statistically robust source that more closely reflects salary as defined in its regulations.

Salary Level

Weekly earnings are available in the CPS MORG data, which allowed the Department to estimate how many nonhourly workers pass the salary level tests.[147] However, the CPS earnings variable does not perfectly reflect the Department's definition of earnings. First, the CPS includes all nondiscretionary bonuses and commissions, which may be used to satisfy up to 10 percent of the new standard salary level under this final rule. This discrepancy between the earnings variable used and the FLSA definition of salary may cause a slight overestimation of the number of workers estimated to meet the standard salary level test. Second, CPS earnings data includes overtime pay, commissions, and tips. The Department notes that employers may factor into an employee's salary a premium for expected overtime hours worked. To the extent they do so, that premium would be reflected in the data. Similarly, the Department believes tips will be an uncommon form of payment for these workers since tips are uncommon for white collar workers. The Department also believes that commissions make up a relatively small share of earnings among nonhourly employees.[148]

Duties

The CPS MORG data do not capture information about job duties; therefore, the Department used occupational titles, combined with probability estimates of passing the duties test by occupational title, to estimate the number of workers passing the duties test. This methodology is very similar to the methodology used in the 2004 rulemaking, and the Department believes it is the best available methodology. In 2004, to determine whether a worker met the duties test, the Department used an analysis performed by WHD in 1998 in response to a request from the GAO. Because WHD enforces the FLSA's overtime requirements and regularly assesses workers' exempt status, WHD was uniquely qualified to provide the analysis. The analysis was used in both the GAO's 1999 white collar exemptions report [149] and the Department's 2004 regulatory impact analysis.[150]

WHD examined 499 occupational codes, excluding nine that were not relevant to the analysis for various reasons (one code was assigned to unemployed persons whose last job was in the Armed Forces, some codes were assigned to workers who are not FLSA covered, others had no observations). Of the remaining occupational codes, WHD

[142] Some computer employees may be exempt even if they are not paid on a salary basis. Hourly computer employees who earn at least $27.63 per hour and perform certain duties are exempt under section 13(a)(17) of the FLSA. These workers are considered part of the EAP exemptions but were excluded from the analysis because they are paid hourly and will not be affected by this final rule (these workers were similarly excluded in the 2004 analysis). Salaried computer workers are exempt if they meet the salary and duties tests applicable to the EAP exemptions, and are included in the analysis since they will be impacted by this final rule. Additionally, administrative and professional employees may be paid on a fee basis, as opposed to a salary basis. § 541.605(a). Although the CPS MORG does not identify workers paid on a fee basis, they are considered nonhourly workers in the CPS and consequently are correctly classified as ''salaried'' (as was done in the 2004 final rule).

[143] We used the standard Pareto distribution approach to impute earnings above the topcoded value as described in Armour, P. and Burkhauser, R (2013). Using the Pareto Distribution to Improve Estimates of Topcoded Earnings. Center for Economic Studies (CES).

[144] As a result of the 2016 final rule's automatic updating provision, the HCE compensation level in Year 7 following the 2016 final rule would exceed $150,000. Imputing earnings improves the impact estimates and consequently the estimates of cost savings of this final rule.

[145] The CPS variable PEERNHRY identifies workers as either hourly or nonhourly.

[146] *See* 69 FR 22197.

[147] The CPS MORG variable PRERNWA, which measures weekly earnings, is used to identify weekly salary.

[148] In the PSID, relatively few nonhourly workers were paid by commission. Additionally, according to the BLS ECI, about 5 percent of the private workforce is incentive-paid workers (incentive pay is defined as payment that relates earnings to actual individual or group production). *See* William J. Wiatrowski, Bureau of Labor Statistics, The Effect of Incentive Pay on Rates of Change in Wages and Salaries (November 24, 2009), *http://www.bls.gov/opub/mlr/cwc/the-effect-of-incentive-pay-on-rates-of-change-in-wages-and-salaries.pdf,* at 1.

[149] Fair Labor Standards Act: White Collar Exemptions in the Modern Work Place, *supra note* 139, at 40–41.

[150] *See* 69 FR 22198.

determined that 251 occupational codes likely included EAP exempt workers and assigned one of four probability codes reflecting the estimated likelihood, expressed as ranges, that a worker in a specific occupation would perform duties required to meet the EAP duties tests. The Department supplemented this analysis in the 2004 final rule regulatory impact analysis when the HCE exemption was introduced. The Department modified the four probability codes for highly paid workers based upon its analysis of the provisions of the highly compensated test relative to the standard duties test (Table 3). To illustrate, WHD assigned exempt probability code 4 to the occupation ''first-line supervisors/managers of construction trades and extraction workers'' (Census code 6200), which indicates that a worker in this occupation has a 0 to 10 percent likelihood of meeting the standard EAP duties test. However, if that worker earned at least $100,000 annually, he or she was assigned a 15 percent probability of passing the more lenient HCE duties test.[151]

The occupations identified in GAO's 1999 report and used by the Department in the 2004 final rule map to an earlier occupational classification scheme (the 1990 Census occupational codes). For this final rule, the Department used occupational crosswalks to map the previous occupational codes to the 2002 Census occupational codes and then to the 2010 Census occupational codes, which are used in the CPS MORG 2016 through 2019 data.[152] If a new occupation comprises more than one previous occupation, then the new occupation's probability code is the weighted average of the previous occupations' probability codes, rounded to the closest probability code.

TABLE 3—PROBABILITY WORKER IN CATEGORY PASSES THE DUTIES TEST

Probability code	The standard EAP test		The HCE test	
	Lower bound %	Upper bound %	Lower bound %	Upper bound %
0	0	0	0	0
1	90	100	100	100
2	50	90	94	96
3	10	50	58.4	60
4	0	10	15	15

These codes provide information on the likelihood that an employee in a category met the duties test but they do not identify the workers in the CPS MORG who actually passed the test. Therefore, the Department designated workers as exempt or nonexempt based on the probabilities. For example, for every ten public relations managers, between five and nine were estimated to pass the standard duties test (based on probability category 2). However, it is unknown which of these ten workers are exempt; therefore, the Department must determine the status for these workers. Exemption status could be randomly assigned with equal probability, but this would ignore the earnings of the worker as a factor in determining the probability of exemption. The probability of qualifying for the exemption increases with earnings because higher paid workers are more likely to perform the required duties, an assumption to which both the Department in the 2004 final rule and the GAO in its 1999 Report adhered.[153]

The Department estimated the probability of exemption for each worker as a function of both earnings and the occupation's exempt probability category using a gamma distribution.[154] Based on these revised probabilities, each worker was assigned exempt or nonexempt status based on a random draw from a binomial distribution using the worker's revised probability as the probability of success. Thus, if this method is applied to ten workers who each have a 60 percent probability of being exempt, six workers would be expected to be designated as exempt.[155] However, which particular workers are designated as exempt may vary with each set of ten random draws. For details, see Appendix A (in the rulemaking docket).

The Department acknowledges that the probability codes used to determine the share of workers in an occupation who are EAP exempt are 21 years old. However, the Department believes the probability codes continue to estimate exemption status accurately given the fact that the standard duties test is not substantively different from the former short duties tests reflected in the codes. For the 2016 rulemaking, the Department looked at O*NET[156] to determine the extent to which the 1998 probability codes reflected current occupational duties. The Department's review of O*NET verified the continued appropriateness of the 1998 probability codes.[157]

Potentially Affected Exempt EAP Workers

The Department estimated that of the 47.6 million salaried white collar workers considered in the analysis, 33.4 million qualified for the EAP exemption under the currently-enforced regulations. Some of these workers were

[151] The HCE duties test is used in conjunction with the HCE total annual compensation requirement, as set in 2004 and applied to date, to determine eligibility for the HCE exemption. It is much less stringent than the standard and short duties tests to reflect that very highly paid employees are much more likely to be properly classified as exempt.

[152] References to occupational codes in this analysis refer to the 2002 Census occupational codes. Crosswalks and methodology available at: *https://www.census.gov/topics/employment/industry-occupation/guidance/code-lists.html.*

[153] For the standard exemption, the relationship between earnings and exemption status is not linear and is better represented with a gamma distribution. For the HCE exemption, the relationship between earnings and exemption can be well represented with a linear function because the relationship is linear at high salary levels (as determined by the Department in the 2004 final rule). Therefore, the gamma model and the linear model would produce similar results. *See* 69 FR 22204–08, 22215–16.

[154] The gamma distribution was chosen because, during the 2004 revision, this non-linear distribution best fit the data compared to the other non-linear distributions considered (*i.e.,* normal and lognormal). A gamma distribution is a general type of statistical distribution that is based on two parameters that control the scale (alpha) and shape (in this context, called the rate parameter, beta).

[155] A binominal distribution is frequently used for a dichotomous variable where there are two possible outcomes; for example, whether one owns a home (outcome of 1) or does not own a home (outcome of 0). Taking a random draw from a binomial distribution results in either a zero or a one based on a probability of ''success'' (outcome of 1). This methodology assigns exempt status to the appropriate share of workers without biasing the results with manual assignment.

[156] The O*NET database contains hundreds of standardized and occupation-specific descriptions. *See http://www.onetcenter.org.*

[157] 81 FR 32459.

excluded from further analysis because the final rule will not affect them. This excluded group contains workers in named occupations who are not required to pass the salary requirements (although they must still pass a duties test) and therefore whose exemption status does not depend on their earnings. These occupations include physicians (identified with Census occupation codes 3010, 3040, 3060, 3120), lawyers (2100), teachers (occupations 2200–2550 and industries 7860 or 7870), academic administrative personnel (school counselors (occupation 2000 and industries 7860 or 7870) and educational administrators (occupation 0230 and industries 7860 or 7870)), and outside sales workers (a subset of occupation 4950). Out of the 33.4 million workers who were EAP exempt, 7.8 million, or 23.4 percent, were expected to be in named occupations. Thus, changes in the standard salary level and HCE compensation tests will not affect these workers. The 25.6 million EAP exempt workers remaining in the analysis are referred to in this final rule as ''potentially affected.''

Based on analysis of the occupational codes and CPS earnings data (described above), the Department has concluded that in Year 1, in the baseline scenario in which the rule does not take effect, of the 25.6 million potentially affected EAP workers, approximately 16.0 million will pass only the standard EAP test, 9.3 million will pass both the standard and the HCE tests, and approximately 343,000 will pass only the HCE test.

C. Determining the Revised Salary and Compensation Levels

For the reasons discussed in section IV.A, the Department has decided to update the 2004 standard salary level by reapplying the 2004 methodology. Using pooled 2018/19 CPS MORG data, the 20th percentile of earnings for full-time salaried workers in the South Census region and/or in the retail industry nationally roughly corresponds to a standard salary level of $684. For the HCE compensation level, the Department used the 80th percentile of all full-time salaried workers nationwide, calculated using the 2018/19 CPS MORG. This results in an HCE annual compensation level of $107,432.

i. The Policy Methodologies Chosen

This final rule uses the same methodology used in 2004 for the standard salary level, setting it at the 20th percentile of full-time salaried workers in the South and/or in the retail industry nationally. After considering public comments pertaining to the HCE total annual compensation requirement, as discussed in section IV.D, the Department has set this threshold so as to be equivalent to the earnings of the 80th percentile of all full-time salaried workers nationally, as opposed to the 90th percentile as proposed in the NPRM. Additionally, to be consistent with the methodology for setting the standard salary level, the Department now uses three-year pooled data to estimate the HCE compensation level. Lastly, the Department has chosen not to project the earnings levels to January 2020 as proposed in the NPRM.

ii. Alternative Methods for Setting the Standard Salary Level

For this final rule, the Department also considered several alternatives for setting the standard salary level. Table 4 presents alternative standard salary levels calculated using pooled 2018/19 CPS data for each alternative approach considered.

- *Alternative 1:* No change (*i.e.,* keep the salary level at the currently-enforced level of $455 per week).
- *Alternative 2:* Maintain the average minimum wage protection in place since 2004 by using the weighted average of hours at minimum wage and overtime pay represented by the minimum salary level.
- *Alternative 3:* Use the 2004 method but exclude the relatively high-wage areas from the South Census Region (Washington, DC, Maryland, and Virginia).
- *Alternative 4:* Use the Kantor method to determine the long test salary level, and set the salary level at that level. The Kantor method calculates a long test salary level by selecting the 10th percentile of earnings of likely exempt workers.
- *Alternative 5:* Use the 2016 method (*i.e.,* the 40th percentile of earnings of nonhourly full-time workers in the South Census Region).

Section VI.D details the transfers, costs, and benefits of the new salary level and the above alternatives.

TABLE 4—STANDARD SALARY LEVEL AND ALTERNATIVES IN 2018/19

Alternative	Salary level (weekly/annually)	Total increase [a]	
		$	%
Alt. #1: No change	$455/$23,660	$0	0.0
Alt. #2: Maintain average minimum wage protection since 2004 [b]	502/26,082	47	10.3
Alt. #3: 2004 Method, South (excluding Washington D.C., MD & VA) or Retail [c]	673/34,996	218	47.9
Final rule: 2004 method [c]	684/35,568	229	50.3
Alt. #4: Kantor long test [d]	724/37,648	269	59.1
Alt. #5: 2016 Method [e]	976/50,752	521	114.5

[a] Change between salary level or alternative and the salary level set in 2004 ($455 per week).

[b] When the $455 weekly threshold was established in 2004, the federal minimum wage was $5.15, so the salary threshold equated to minimum wage and overtime pay at time and one-half for hours over 40 for an employee working no more than 72.2 hours. That amount fell with increases in the minimum wage and is now 55.2 hours. The weighted average across the 15 years since the overtime threshold was last changed is 59.5 hours, and a threshold that would provide 59.5 hours of $7.25 minimum wage and overtime pay would be $502.

[c] Full-time salaried workers with various industry/region exclusions (excludes workers not subject to the FLSA, not subject to the salary level test, and in some workers in agriculture or transportation). Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.

[d] 10th percentile of likely exempt workers. Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.

[e] 40th percentile earnings of nonhourly full-time workers in the South Census region, provided by BLS. The salary level reflects the first automatic update that would have taken place under the 2016 final rule.

iii. Alternative Methods for Setting the HCE Total Annual Compensation Level

As described above, the Department is updating the HCE compensation level using earnings for the 80th percentile of all full-time salaried workers nationally, $107,432 per year. The Department also evaluated the following alternative HCE compensation levels:

- *HCE alternative 1:* No change (*i.e.,* leave the HCE compensation level at the currently-enforced level of $100,000 per year).

• *HCE alternative 2:* Use the methodology proposed in the NPRM (*i.e.,* use the 90th percentile earnings of full-time salaried workers nationally).[158]

Table 5 presents possible 2018/19 HCE levels as calculated using each alternative approach considered. Section VI.D details the transfers, costs, and benefits of the new HCE compensation level and the two alternatives.

TABLE 5—HCE COMPENSATION LEVELS AND ALTERNATIVES IN 2018/19

Alternative	Salary level (weekly/annually)	Total increase [a]	
		$	%
HCE alt. #1: No change	$1,923/$100,000	$0	0.0
Final rule: 80th percentile of full-time salaried workers [b]	2,066/107,432	7,432	7.4
HCE alt. #2: 90th percentile of full-time salaried workers [b]	2,807/145,964	45,964	46.0

[a] Change between updated/alternative compensation level and the compensation level set in 2004 ($100,000 annually).
[b] Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.

The Department believes that HCE alternative 1 is inappropriate because some increase to the HCE threshold is necessary to ensure that the HCE threshold continues to appropriately complement the more lenient HCE duties test. However, as explained in section IV.D, the Department does not believe the significantly higher threshold equal to the 90th percentile of full-time salaried workers nationally is necessary. Further, setting the HCE threshold at such a high level will result in significant administrative burdens, including the costs associated with the need to reassess, under the standard duties test, the exempt status of highly paid white collar workers, many of whom would remain exempt under that test. Accordingly, the Department rejected the second alternative because it believes that the HCE threshold set in this final rule is sufficiently high to ensure that those who meet that threshold will almost invariably pass the standard duties test.

D. Effects of Revised Salary and Compensation Levels

i. Overview and Summary of Quantified Effects

The economic effects of increasing the EAP salary and compensation levels will depend on how employers respond. Employer response is expected to vary by the characteristics of the affected EAP workers. Transfers from employers to employees and between employees, and direct employer costs, depend on how employers respond to the final rule.

The Department has derived the standard salary level using the 2004 methodology, and has set the HCE compensation level at the 80th percentile of all full-time salaried workers nationwide. In both cases we used pooled 2018/19 CPS data to calculate the levels. Given that at the time this analysis was performed data was available through June 2019, the Department believes that using current data to estimate the economic effects of the rule taking effect in January 2020 is appropriate.

Table 6 presents the estimated number of affected workers, costs, and transfers associated with increasing the salary and compensation levels. The Department estimated that the direct employer costs of this final rule will total $543.0 million in the first year, with 10-year annualized direct costs of $164.0 million per year using a 3 percent real discount rate and $173.3 million per year using a 7 percent real rate.

In addition to these direct costs, this final rule will transfer income from employers to employees. Estimated Year 1 transfers will equal $396.4 million, with annualized transfers estimated at $295.0 million and $298.8 million per year using the 3-percent and 7-percent real discount rates, respectively. Potential employer costs due to reduced profits and additional hiring were not quantified but are discussed in section VI.D.iii.5.

TABLE 6—SUMMARY OF AFFECTED WORKERS AND REGULATORY COSTS AND TRANSFERS, STANDARD AND HCE EARNINGS THRESHOLDS

Impact [a]	Year 1	Future years [b]		Annualized value	
		Year 2	Year 10	3% Real discount rate	7% Real discount rate
Affected Workers (1000s)					
Standard	1,156	1,069	723		
HCE	102	114	154		
Total	1,257	1,183	877		
Direct Employer Costs (Millions in 2019$)					
Regulatory familiarization	$340.4	$0.0	$0.0	$38.7	$45.3
Adjustment [c]	68.2	2.0	4.6	10.5	11.7
Managerial	134.4	132.3	94.5	114.8	116.3

[158] Because in the final rule the Department is using pooled CPS MORG data to set the HCE compensation level, it used the same data set to calculate this alternative compensation level. Thus, this method differs slightly from that proposed in the NPRM, which was calculated using the most recent year of data provided by BLS.

TABLE 6—SUMMARY OF AFFECTED WORKERS AND REGULATORY COSTS AND TRANSFERS, STANDARD AND HCE EARNINGS THRESHOLDS—Continued

Impact [a]	Year 1	Future years [b]		Annualized value	
		Year 2	Year 10	3% Real discount rate	7% Real discount rate
Total direct costs [d]	543.0	134.3	99.1	164.0	173.3
Transfers from Employers to Workers (Millions in 2019) [e]					
Due to minimum wage	75.4	42.8	26.1	36.9	38.1
Due to overtime pay	321.0	264.9	221.3	258.1	260.6
Total transfers [d]	396.4	307.7	247.4	295.0	298.8

[a] Additional costs and benefits of the rule that could not be quantified or monetized are discussed in the text.
[b] These costs/transfers represent a range over the nine-year span.
[c] Adjustment costs occur in all years when there are newly affected workers.
[d] Components may not add to total due to rounding.
[e] This is the net transfer from employers to workers. There may also be transfers between workers.

ii. Affected EAP Workers

1. Overview

The Department estimated there are 25.6 million potentially affected EAP workers—that is, EAP workers who either (1) passed the salary basis test, the standard salary level test, and the standard duties test, or (2) passed the salary basis test, the standard salary level test, the HCE total compensation level test, and the HCE duties test (but not the standard duties test). This number excluded workers in named occupations, who are not subject to the salary tests, or those who qualify for another (non-EAP) exemption.

Using the method described above, the Department estimated that the increase in the standard salary level from $455 per week to $684 per week will affect 1.2 million exempt workers in Year 1, while the increase in the HCE annual compensation level from $100,000 to $107,432 will impact 101,800 workers (Figure 2).[159] [160] In total, the Department expects that 1.3 million workers will be affected in Year 1 by the final rule earnings threshold increases, composing about 4.9 percent of the pool of potentially affected EAP workers.

Figure 2: Number of Affected Workers in Year 1

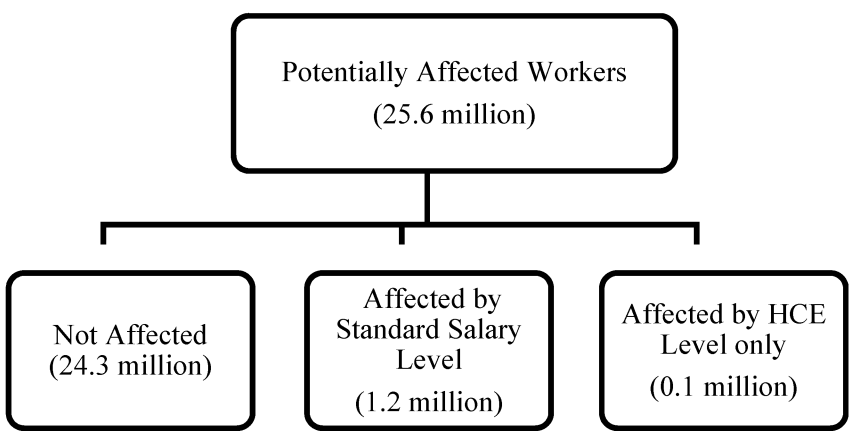


Table 7 presents the number of affected EAP workers, the mean number of overtime hours they work per week, and their average weekly earnings. The 1.2 million workers affected by the increase in the standard salary level work on average 1.6 usual hours of overtime per week and earn on average $581 per week.[161] However, the majority of these workers (about 86 percent) work zero usual hours of overtime. The 14 percent of affected workers who regularly work overtime average 11.7 hours of overtime per week. The 101,800 EAP workers affected by the change in the HCE compensation level average 4.2 hours of overtime per week and earn an average of $1,989 per week ($103,450 per year). About 65 percent of these workers work zero usual hours of overtime while the 35 percent who work usual hours of overtime average 11.9 hours of overtime per week.

Although most affected EAP workers who typically do not work overtime are unlikely to experience significant

[159] This group includes workers who may currently be nonexempt under more protective state EAP laws and regulations, such as some workers in Alaska, California, and New York.

[160] The 2016 final rule applied joint probabilities to estimate the number of affected HCE workers (*i.e.,* the number of HCE workers who pass the HCE duties test but fail the standard duties test). In order to provide a more accurate estimate, this final rule applies conditional probabilities to determine the number of affected HCE workers.

[161] CPS defines ''usual hours'' as hours worked 50 percent or more of the time.

changes in their daily work routine, those who regularly work overtime may experience significant changes. Moreover, affected EAP workers who routinely work overtime and earn less than the minimum wage are most likely to experience significant changes because of the revised standard salary level.[162] Employers might respond by paying overtime premiums; reducing or eliminating overtime hours; reducing employees' regular wage rates (provided that the reduced rates still exceed the minimum wage); increasing employees' salaries to the updated salary level to preserve their exempt status (although this will be less common for affected workers earning below the minimum wage); or using some combination of these responses.

TABLE 7—NUMBER OF AFFECTED EAP WORKERS, MEAN OVERTIME HOURS, AND MEAN WEEKLY EARNINGS, YEAR 1

Type of affected EAP worker	Affected EAP workers [a]		Mean overtime hours	Mean usual weekly earnings
	Number (1,000s)	% of Total		
Standard Salary Level				
All affected EAP workers	1,156	100%	1.6	$581
Earn less than the minimum wage [b].	22	1.9	21.4	524
Regularly work overtime	158	13.7	11.7	582
CPS occasionally work overtime [c].	42	3.7	8.3	581
HCE Compensation Level				
All affected EAP workers	102	100	4.2	1,989
Earn less than the minimum wage [b].				
Regularly work overtime	36	35.1	11.9	1,968
CPS occasionally work overtime [c].	4	3.5	9.7	1,995

Note: Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.
[a] Estimated number of workers exempt under the EAP exemptions who will be entitled to overtime protection under the updated salary levels (if their weekly earnings do not increase to the new salary levels).
[b] The applicable minimum wage is the higher of the federal minimum wage and the state minimum wage. HCE workers will not be affected by the minimum wage provision. These workers all regularly work overtime and are also included in that row.
[c] Workers who do not usually work overtime but did in the CPS reference week. Mean overtime hours are actual overtime hours in the reference week. Other workers may occasionally work overtime in other weeks. These workers are identified later.

The Department considered two types of overtime workers in this analysis: Regular overtime workers and occasional overtime workers.[163] Regular overtime workers typically worked more than 40 hours per week. Occasional overtime workers typically worked 40 hours or less per week, but they worked more than 40 hours in the week they were surveyed. The Department considered these two populations separately in the analysis because labor market responses to overtime pay requirements may differ for these two types of workers.

In a representative week, the increases in the standard salary level and the HCE compensation level affected an estimated 45,900 occasional overtime workers (3.7 percent of all affected EAP workers). They averaged 8.4 hours of overtime in the weeks they worked overtime. This group represents the number of workers with occasional overtime hours in the week the CPS MORG survey was conducted. Because the survey week is a representative week, the Department believes the prevalence of occasional overtime in the survey week, and the characteristics of these workers, is representative of other weeks (even though a different group of workers would be identified as occasional overtime workers in a different week).

2. Characteristics of Affected EAP Workers

In this section, the Department examined the characteristics of affected EAP workers. Table 8 presents the distribution of affected EAP workers by industry and occupation, using Census industry and occupation codes. The industry with the most affected EAP workers is education and health services (288,000), while the industry with the highest percentage of affected EAP workers is leisure and hospitality (about 10 percent). The occupation category with the most affected EAP workers is management, business, and financial (506,000), while the occupation category with the highest percentage of affected EAP workers is services (about 15 percent).

Finally, 6.1 percent of potentially affected workers in private nonprofits are affected compared with 4.6 percent in private for-profit firms. However, as discussed in section VI.B.iii, the estimates of workers subject to the FLSA include workers employed by enterprises that do not meet the enterprise coverage requirements because there is no data set that would adequately inform an estimate of the size of this worker population. Although failing to exclude workers who work for non-covered enterprises would only affect a small percentage of workers generally, it may have a larger effect (and result in a larger overestimate) for workers in nonprofits because when determining enterprise coverage only

[162] A small proportion (1.9 percent) of affected EAP workers earn implicit hourly wages that are less than the applicable minimum wage (the higher of the state or federal minimum wage). The implicit hourly wage is calculated as an affected EAP employee's total weekly earnings divided by total weekly hours worked. For example, workers earning the currently-enforced $455 per week standard salary level would earn less than the federal minimum wage if they work 63 or more hours in a week ($455/63 hours = $7.22 per hour).

[163] Regular overtime workers were identified in the CPS MORG with variable PEHRUSL1. Occasional overtime workers were identified with variables PEHRUSL1 and PEHRACT1.

revenue derived from business operations, not charitable activities, is included.

TABLE 8—ESTIMATED NUMBER OF EXEMPT WORKERS WITH THE CURRENT AND UPDATED SALARY LEVELS, BY INDUSTRY AND OCCUPATION, YEAR 1

Industry/occupation/nonprofit	Workers subject to FLSA (millions)	Potentially affected EAP workers (millions) [a]	Not-affected (millions) [b]	Affected (millions) [c]	Affected as share of potentially affected (%)
Total	139.43	25.59	24.33	1.26	4.9
By Industry [d]					
Agriculture, forestry, fishing, & hunting	1.33	0.04	0.04	0.00	5.4
Mining	0.73	0.19	0.18	0.00	2.6
Construction	8.49	1.02	0.97	0.05	5.0
Manufacturing	15.56	3.61	3.52	0.09	2.5
Wholesale & retail trade	19.08	2.60	2.44	0.17	6.4
Transportation & utilities	7.65	0.92	0.88	0.04	4.1
Information	2.73	1.01	0.97	0.04	4.2
Financial activities	9.66	3.81	3.64	0.17	4.3
Professional & business services	15.80	5.75	5.53	0.21	3.7
Education & health services	34.24	4.15	3.86	0.288	6.9
Leisure & hospitality	13.13	0.92	0.83	0.09	9.8
Other services	5.62	0.64	0.59	0.05	8.3
Public administration	5.40	0.93	0.88	0.05	5.5
By Occupation [d]					
Management, business, & financial	21.12	12.76	12.25	0.51	4.0
Professional & related	32.96	9.02	8.61	0.41	4.6
Services	24.16	0.22	0.18	0.03	14.6
Sales and related	13.78	2.44	2.26	0.18	7.6
Office & administrative support	17.64	0.95	0.84	0.11	11.7
Farming, fishing, & forestry	1.01	0.00	0.00	0.00	0.0
Construction & extraction	6.75	0.02	0.02	0.00	3.2
Installation, maintenance, & repair	4.59	0.04	0.04	0.00	3.9
Production	8.48	0.11	0.10	0.00	3.9
Transportation & material moving	8.93	0.03	0.03	0.00	9.1
By Nonprofit and Government Status					
Nonprofit, private	9.65	2.04	1.91	0.12	6.1
For profit, private	111.04	21.52	20.52	1.00	4.6
Government (state, local, and federal)	18.73	2.03	1.90	0.13	6.5

Note: Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.
[a] Exempt workers who are white collar, salaried, not eligible for another (non-EAP) overtime exemption, and not in a named occupation.
[b] Workers who continue to be exempt after the increases in the salary levels (assuming affected workers' weekly earnings do not increase to the new salary level).
[c] Estimated number of workers exempt under the EAP exemptions who will be entitled to overtime protection under the updated salary levels (if their weekly earnings do not increase to the new salary levels).
[d] Census industry and occupation categories.

Table 9 presents the distribution of affected EAP workers based on Census Regions and Divisions, and metropolitan statistical area (MSA) status. The region with the most affected workers will be the South (544,000), but the South's percentage of potentially affected workers who are affected is still small (6.1 percent). Although 90 percent of affected EAP workers will reside in MSAs (1.13 of 1.26 million), so do a corresponding 88 percent of all workers subject to the FLSA.[164]

Employers in low-wage industries, regions, and in non-metropolitan areas may be more affected because they typically pay lower wages and salaries. However, the Department believes the salary level adopted in this final rule is appropriate for these lower-wage sectors because the methodology used in 2004, and applied for this rulemaking, used earnings data in the low-wage retail industry and the low-wage South Region. Effects by region and industry are considered in section VI.D.vi.

[164] Identified with CPS MORG variable GTMETSTA.

TABLE 9—ESTIMATED NUMBER OF POTENTIALLY AFFECTED EAP WORKERS WITH THE CURRENT AND UPDATED SALARY LEVELS, BY REGION, DIVISION, AND MSA STATUS, YEAR 1

Region/division/metropolitan status	Workers subject to FLSA (millions)	Potentially affected EAP workers (millions) [a]	Not-affected (millions) [b]	Affected (millions) [c]	Affected as share of potentially affected (%)
Total	139.43	25.59	24.33	1.26	4.9
By Region/Division					
Northeast	*25.38*	*5.30*	*5.07*	*0.23*	*4.4*
New England	7.03	1.56	1.50	0.06	3.7
Middle Atlantic	18.35	3.74	3.57	0.17	4.6
Midwest	*30.59*	*5.23*	*5.01*	*0.23*	*4.4*
East North Central	20.77	3.56	3.40	0.16	4.4
West North Central	9.82	1.67	1.60	0.07	4.4
South	*50.90*	*8.93*	*8.39*	*0.54*	*6.1*
South Atlantic	26.77	5.01	4.72	0.30	5.9
East South Central	7.59	1.09	1.01	0.08	7.7
West South Central	16.55	2.83	2.67	0.16	5.7
West	*32.56*	*6.12*	*5.87*	*0.25*	*4.1*
Mountain	10.30	1.74	1.66	0.08	4.7
Pacific	22.26	4.38	4.21	0.17	3.9
By Metropolitan Status					
Metropolitan	122.63	23.98	22.84	1.13	4.7
Non-metropolitan	15.85	1.51	1.39	0.12	7.7
Not identified	0.95	0.10	0.10	0.01	6.0

Note: Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.
[a] Exempt workers who are white collar, salaried, not eligible for another (non-EAP) overtime exemption, and not in a named occupation.
[b] Workers who continue to be exempt after the increases in the salary levels (assuming affected workers' weekly earnings do not increase to the new salary level).
[c] Estimated number of workers exempt under the EAP exemptions who will be entitled to overtime protection under the updated salary levels (if their weekly earnings do not increase to the new salary levels).

3. NPRM Comments on Affected Worker Calculation

EPI and a few other commenters asserted that the Department's use of pooled 2015–2017 data to calculate the number of affected workers ''leads to an underestimate because it doesn't account for employment growth and other changes in the three years between 2017 and 2020.'' The Department is using pooled CPS MORG data for July 2016 through June 2019, adjusted to reflect 2018/2019, in this final rule. The Department is not modeling employment growth between 2018/19 and the final rule's effective date because of uncertainty in the appropriate growth rates to project earnings and employment, and because of the relatively short period of time separating June 2019—the most recent CPS MORG data available at the time this impact analysis was developed—and January 1, 2020—the effective date of the final rule. However, as a sensitivity analysis undertaken in response to these comments, the Department used the BLS National Employment Matrix (NEM) for 2016 to 2026 to calculate growth rates for each occupation-industry category. Using these rates to adjust the number of affected employees in 2018/19 for one and a half years of employment growth increased the estimated number of affected workers by less than 1.8 percent.

iii. Costs

1. Summary

The Department quantified three direct costs to employers in this analysis: (1) Regulatory familiarization costs; (2) adjustment costs; and (3) managerial costs. The Department estimated that in Year 1 (2020), regulatory familiarization costs will be $340.4 million, adjustment costs will be $68.2 million, and managerial costs will be $134.4 million (Table 10). Total direct employer costs in Year 1 will be $543.0 million.

TABLE 10—SUMMARY OF YEAR 1 DIRECT EMPLOYER COSTS
[Millions]

Direct employer costs	Standard salary level	HCE compensation level	Total
Regulatory familiarization [a]	....	....	$340.4
Adjustment	$62.7	$5.5	68.2
Managerial	121.5	12.9	134.4
Total direct costs	184.1	18.4	543.0

[a] Regulatory familiarization costs are assessed jointly for the change in the standard salary level and the HCE compensation level.

Adjustment costs and managerial costs are recurring, so we also projected them for years 2 through 10 in section VI.D.viii. The Department discusses costs that are not quantified in section VI.D.iii.5.

2. Regulatory Familiarization Costs

This rule will impose direct costs on firms by requiring them to review the regulation. To estimate these ''regulatory familiarization costs,'' three pieces of information must be estimated: (1) The number of affected establishments; (2) a wage level for the employees reviewing the rule; and (3) the amount of time employees spend reviewing the rule.

It is unclear whether regulatory familiarization costs are a function of the number of establishments or the number of firms. To avoid underestimating these costs, the Department assumed that regulatory familiarization occurs at a decentralized level and used the number of establishments in its cost estimate; this results in a higher estimate than would result from using the number of firms. The most recent data on private sector establishments at the time this final rule was drafted are from the 2016 Statistics of U.S. Businesses (SUSB), which reports 7.76 million establishments with paid employees.[165] Additionally, there were an estimated 90,126 state and local governments in 2017, the most recent data available.[166] The Department thus estimated 7.85 million establishments altogether (for ease, the Department uses the term ''establishments'' to refer to the total of establishments and government entities) might incur regulatory familiarization costs.

The Department believes that all establishments will incur some regulatory familiarization costs, even if they do not employ exempt workers, because all establishments will need to confirm whether this rule includes any provisions that may affect their employees. Firms with more affected EAP workers will likely spend more time reviewing the regulation than firms with fewer or no affected EAP workers (since a careful reading of the regulation will probably follow the initial decision that the firm is affected). However, the Department did not know the distribution of affected EAP workers across firms, so it used an average cost per establishment.

The Department believes one hour per establishment is appropriate because the EAP exemptions have existed in one form or another since 1938. The most significant change in this rulemaking is setting a new standard salary level for exempt workers, and the changed regulatory text is only a few pages. The Department thus believes that one hour is an appropriate average estimate for the time each establishment will spend reviewing the changes made by this rulemaking. Time spent to implement the necessary changes was included in adjustment costs. The Department's analysis assumed that mid-level human resource workers with a median wage of $26.56 per hour will review the final rule.[167] The Department also assumed that benefits are paid at a rate of 46 percent of the base wage[168] and overhead costs are paid at a rate of 17 percent of the base wage,[169] resulting in an hourly rate of $43.38. The Department thus estimates regulatory familiarization costs in Year 1 will be $340.4 million ($43.38 per hour × 1 hour × 7.85 million establishments).[170]

Some commenters asserted these cost estimates are too low. For example, SBA Office of Advocacy (SBA Advocacy) wrote: ''we spoke to a small retail business in Alabama, who retained the services of an attorney for 10–15 hours to review the 2016 final rule.'' International Bancshares Corporation described the necessary hours for regulatory familiarization and adjustment costs as ''countless.'' An individual commenter stated that the Department's estimated costs are too low but did not provide any information on what costs should be.

The Department continues to believe that an average of one hour per establishment is appropriate. The EAP exemptions have been in existence in one form or another since 1938, and a final rule was published as recently as 2016. Furthermore, employers who use the exemptions must apply them every time they hire an employee whom they seek to classify as exempt. Thus, employers should be familiar with the exemptions. The most significant change promulgated in this rulemaking is setting new earnings thresholds for exempt workers. The Department believes that, on average, one hour is sufficient to time to read and understand, for example, the changes to these thresholds, and we note that the regulatory text changes comprise only a few pages. Additionally, the estimated one hour for regulatory familiarization represents an average for all establishments in the U.S., even those without any affected or exempt workers, which are unlikely to spend much time reviewing the rule. Some businesses, of course, will spend more than one hour, and some will spend less, but for the reasons stated above, the Department believes that an average of one hour is an appropriate estimate.

3. Adjustment Costs

This rule will also impose direct costs on firms by requiring them to evaluate the exemption status of employees, update and adapt overtime policies, notify employees of policy changes, and adjust their payroll systems.[171] The Department believes the size of these ''adjustment costs'' will depend on the number of affected EAP workers and will occur in any year when exemption status is changed for any workers. To estimate adjustment costs, three pieces of information must be estimated: (1) A wage level for the employees making the adjustments; (2) the amount of time spent making the adjustments; and (3) the estimated number of newly affected EAP workers. The Department again estimated that the average wage with benefits and overhead costs for a mid-level human resource worker will be $43.38 per hour (as explained above).

The Department estimated that it will take establishments an average of 75

[165] Statistics of U.S. Businesses 2016, *https://www.census.gov/programs-surveys/susb.html.*

[166] 2017 Census of Governments. Table 1, *https://www.census.gov/data/tables/2017/econ/gus/2017-governments.html.*

[167] The median wage in the pooled 2018/19 CPS data for workers with the Census 2010 occupations ''human resources workers'' (0630); ''compensation, benefits, and job analysis specialists'' (0640); and ''training and development specialists'' (0650). The Department determined these occupations include most of the workers who would conduct these tasks. *See* Bureau of Labor Statistics, U.S. Department of Labor, Occupational Outlook Handbook.

[168] The benefits-earnings ratio is derived from BLS's Employer Costs for Employee Compensation data using variables CMU1020000000000D and CMU1030000000000D. This fringe benefit rate includes some fixed costs such as health insurance.

[169] The Department believes that the overhead costs associated with this rule are small because existing systems maintained by employers to track currently hourly employees can be used for newly overtime-eligible workers. However, acknowledging that there might be additional overhead costs, we have included an overhead rate of 17 percent. Because the 2016 final rule did not include overhead costs in its cost and transfer estimates, estimated costs and transfers associated with the 2016 final rule have been recalculated for comparison purposes in section VI.D.ix.

[170] As previously noted, the Department used the number of establishments rather than the number of firms, which results in a higher estimate of the regulatory familiarization cost. Using the number of firms, 6.0 million, would result in a reduced regulatory familiarization cost estimate of $262.2 million in Year 1.

[171] While some companies may need to reconfigure information technology systems to include both exempt and overtime-protected workers, the Department notes that most organizations affected by the rule already employ overtime-eligible workers and have in place payroll systems and personnel practices (*e.g.,* requiring advance authorization for overtime hours) such that additional costs associated with the rule should be relatively small in the short run.

minutes per affected worker to make the necessary adjustments. Little applicable data were identified from which to estimate the amount of time required to make these adjustments.[172] Therefore, in the NPRM the Department used the estimate of 1.25 hours from the 2016 final rule after reviewing public comments on the 2015 NPRM, and it is again using this estimate in this final rule. The estimated number of affected EAP workers in Year 1 is 1.3 million (as discussed in section VI.D.ii). Therefore, total estimated Year 1 adjustment costs will be $68.2 million ($43.38 × 1.25 hours × 1.3 million workers).

A reduction in the cost to employers of determining employees' exempt status may partially offset adjustment costs. Currently, to determine whether an employee is exempt, employers must apply the duties test to salaried workers who earn at least $455 per week. However, when the rule takes effect, firms will no longer be required to apply the potentially time-consuming duties test to employees earning less than the new standard salary level. This will be a clear cost savings to employers for the approximately 4.1 million salaried employees (2.2 million in white collar occupations and 1.9 million in blue collar occupations) who do not pass the duties test and earn at least $455 per week but less than the updated salary level. The Department did not estimate the potential size of this cost savings.

A few commenters expressed concern that the time estimate is too low. For example, as noted above, International Bancshares Corporation described the necessary hours for regulatory familiarization and adjustment costs as ''countless.'' SBA Advocacy wrote: ''Small businesses have told Advocacy that it may take them many hours and several weeks to understand and implement this rule for their small businesses.'' Two commenters, the National Association of Manufacturers and the HR Policy Association, expressed particular concern with adjustment costs stemming from the proposed increase in the HCE compensation level, noting that for each worker earning between $100,000 and the new HCE compensation level, the employee's job duties will need to be reassessed to determine whether the worker remains exempt under the standard salary level exemption. The National Association of Manufacturers elaborated that ''across the manufacturing sector, the change in HCE threshold [proposed in the NPRM] may be even more difficult and consequential than updating the standard salary threshold.''

The Department is retaining its estimate of adjustment costs as 75 minutes per affected worker in the final rule. The Department notes that the vast majority of commenters, including employer representatives, did not contest this estimate. Additionally, this estimate is drawn from the 2016 final rule, and represents a 25 percent increase, in response to concerns from employer representatives, over the Department's original estimate of one hour per worker in the 2015 NPRM.[173] Moreover, SBA Advocacy's numbers are not necessarily inconsistent with the Department's estimates. For example, if a small business has 15 affected employees, then the Department estimated it will (on average) take 19.75 hours to make the appropriate adjustments, an amount of time that some small businesses might consider ''many hours'' and that could take place over ''several weeks.''

The Department also believes that the 75-minute-per-worker average time estimate appropriately takes into account adjustment time for HCE-affected workers (those passing only the HCE duties test and not the standard duties test). This estimate assumes that the average is concentrated in the subset of employees requiring more analysis to make a decision. For example, employers are likely to incur relatively low adjustment costs for some workers, such as those who work no overtime (described below as Type 1 workers). This leaves more time for employers to spend on adjustment costs for other workers, such as affected HCE employees who become newly subject to the more rigorous standard duties test. The Department further notes that in this final rule, the number of affected HCE employees has declined from the NPRM as a result of the Department's decision to decrease the HCE threshold from the proposed amount of $147,414 to $107,432. This adjustment also addresses concerns about the burdens that would have been associated, under the NPRM, with applying the standard duties test to a large number of formerly HCE exempt employees, many of whom would have remained exempt under the standard duties test. Thus, although some employers may spend more time adjusting for HCE-affected workers than for other workers, HCE workers will now comprise a smaller portion of the of the total number of affected workers, further affirming the Department belief that its estimate of 75 minutes per worker on average is appropriate.

4. Managerial Costs

If employers reclassify employees as overtime-eligible due to the changes in the salary levels, then firms may incur ongoing managerial costs because the employer may spend more time developing work schedules and closely monitoring an employee's hours to minimize or avoid overtime. For example, the manager of a reclassified worker may have to assess whether the marginal benefit of scheduling the worker for more than 40 hours exceeds the marginal cost of paying the overtime premium. Additionally, the manager may have to spend more time monitoring the employee's work and productivity since the marginal cost of employing the worker per hour has increased. Unlike regulatory familiarization and adjustment costs, which occur primarily in Year 1, managerial costs are incurred more uniformly every year. The Department applied managerial costs to workers who (1) are reclassified as nonexempt, overtime-protected and (2) either regularly work overtime or occasionally work overtime, but on a predictable basis—an estimated 304,500 workers (*see* Table 13 and accompanying explanation). The Department estimated these costs assuming that management spends an additional ten minutes per week scheduling and monitoring each affected worker expected to be reclassified as nonexempt, overtime-eligible as a result of this rule, and whose hours are adjusted. As discussed in detail below, most affected workers do not currently work overtime, and there is no reason to expect their hours worked to change when their status changes from exempt to nonexempt. For that group of workers, management will have little or no need to increase their monitoring of hours worked; therefore, these workers are not included in the managerial cost calculation. Under these assumptions, the additional managerial hours worked per week will be 50,751 hours ((10 minutes/60 minutes) × 304,500 workers).

The median hourly wage in 2018/19 for a manager was $31.18 and benefits were estimated to be paid at a rate of 46 percent of the base wage.[174] Together

[172] Costs from the 2004 final rule were considered, but because that revision included changes to the duties test, the cost estimates are not directly applicable; in addition, the 2004 final rule did not separately account for managerial costs. The 2015 NPRM separately accounted for managerial costs. Some commenters responded with higher time estimates, but these estimates were not substantiated with data.

[173] 81 FR at 32475.

[174] Calculated as the median wage in the pooled 2018/19 CPS MORG data for workers in management occupations (excluding chief

Continued

with the 17 percent overhead costs used for this analysis, this totals $50.92 per hour. Thus, the estimated Year 1 managerial costs total $134.4 million (50,751 hours/week × 52 weeks × $50.92/hour). Although the exact magnitude will vary with the number of affected EAP workers each year, the Department anticipates that employers will incur managerial costs annually.

There was little precedent or data to aid in evaluating managerial costs. With the exception of the 2016 rulemaking, prior part 541 rulemakings did not estimate managerial costs. The Department likewise found no estimates of managerial costs after reviewing the literature. Thus, in the NPRM, the Department used the same methodology as the 2016 final rule, which the Department adopted after considering comments on the 2015 NPRM. However, for this final rule, the Department has increased the time estimate from 5 minutes to 10 minutes.

A few commenters generally expressed concern about the managerial costs for businesses. For example, one commenter noted: ''There is no easy way to track hours for salaried folks easily, in most businesses. As a result, companies will be forced to begin this practice, adding more costs in administrative ways.'' Another individual wrote that the proposed rule ''would create a challenge by placing a burden on the employers to exaustively [sic] track these newly nonexempt employees' hours to ensure compliance with overtime pay and other requirements. This tracking of hours would also produce increased human resources paperwork and technology costs to our company.'' The Kentucky Retail Federation wrote: ''Reclassifying managers to hourly workers will require hours spent scheduling work hours to avoid overtime costs.'' SBA Advocacy, asserting that the Department underestimated compliance costs, wrote: ''Employers reclassifying managers to hourly staff may spend many hours a week scheduling and keeping track of employee work to avoid these extra overtime costs.''

The Department acknowledges that firms may incur costs monitoring and managing the hours of formerly exempt staff. In addition, the Department acknowledges that to the extent workers who lose their exempt status as a result of the change in the standard salary level telecommute, but hourly and other nonexempt salaried workers do not telecommute, it may be necessary to develop ways of tracking such work by newly nonexempt workers. However, the Department does not expect that such firms will spend ''many hours a week'' on such tasks, and believes an estimate of 10 minutes per worker per week is appropriate. First, the Department notes that EAP exempt employees account for less than 20 percent of the U.S. labor force; as such, the Department expects that the vast majority of employers of EAP exempt workers also employ nonexempt workers. Such employers already have in place recordkeeping systems and standard operating procedures for ensuring employees work overtime under only employer-prescribed circumstances. Thus, such systems generally do not need to be invented for managing formerly-exempt EAP employees. Second, the Department also notes that under the FLSA recordkeeping regulations in part 516, employers determine how to make and keep an accurate record of hours worked by employees; for example, employers may tell their workers to write their own time records and any timekeeping plan is acceptable as long as it is complete and accurate. Additionally, if the nonexempt employee works a fixed schedule, *e.g.,* 9:00 a.m.–5:30 p.m. Monday–Friday, the employer may keep a record showing the exact schedule of daily and weekly hours and merely indicate exceptions to that schedule. *See* Fact Sheet #21: Recordkeeping Requirements under the Fair Labor Standards Act (*https://www.dol.gov/whd/regs/compliance/whdfs21.pdf*). However, as previously noted, in response to concerns raised by commenters the Department has doubled the amount of time attributed to managerial costs.

5. Other Potential Costs

In addition to the costs discussed above, the final rule may impose additional costs that have not been quantified. These costs are discussed qualitatively below, but we note that in some cases (*e.g.,* schedule flexibility, salaried status) these costs may directly affect workers' wages because workers face a tradeoff in the labor market between cash wages and the nonpecuniary aspects of jobs.[175]

Reduced Scheduling Flexibility

Exempt workers may enjoy more scheduling flexibility because their hours are less likely to be monitored than nonexempt workers. If so, the final rule could impose costs on newly nonexempt, overtime-eligible workers by, for example, limiting their ability to adjust their schedules to meet personal and family obligations. But the rule does not require employers to reduce scheduling flexibility. Employers can continue to offer flexible schedules and require workers to monitor their own hours and to follow the employers' timekeeping rules. Additionally, some exempt workers already monitor their hours for billing purposes. For these reasons, and because there is little data or literature on these costs, the Department did not quantify potential costs regarding scheduling flexibility.

Preference for Salaried Status

Some of the workers who become nonexempt as a result of the final rule and whose pay is changed by their employer from salaried to hourly status may have preferred to remain salaried. Research has shown that salaried workers are more likely than hourly workers to receive benefits such as paid vacation time and health insurance,[176] and are more satisfied with their benefits.[177] Additionally, when employer demand for labor decreases, hourly workers tend to see their hours cut before salaried workers, making earnings for hourly workers less predictable.[178] However, this literature generally does not control for differences between salaried and hourly workers such as education, job title, or earnings; therefore, this correlation is not necessarily attributable to hourly status.

If workers are reclassified as hourly, and hourly workers have fewer benefits than salaried workers, reclassification could reduce workers' benefits. But the Department notes that this rule does not require such reclassification. These newly nonexempt workers may continue to be paid a salary, as long as that salary is equivalent to a base wage at least equal to the minimum wage rate for every hour worked, and the employee receives a 50 percent

executives). The adjustment ratio is derived from BLS' Employer Costs for Employee Compensation data using variables CMU1020000000000D and CMU1030000000000D.

[175] *See, e.g.,* Ashenfelter, O. & Layard, R. (1986). Handbook of Labor Economics. Volume 1 641–92. *https://www.sciencedirect.com/science/article/abs/pii/S1573446386010155.*

[176] Lambert, S.J. (2007). Making a Difference for Hourly Employees. In A. Booth, & A.C. Crouter, *Work-Life Policies that Make a Real Difference for Individuals, Families, and Communities.* Washington, DC: Urban Institute Press.

[177] Balkin, D.B., & Griffeth, R.W. (1993). The Determinants of Employee Benefits Satisfaction. *Journal of Business and Psychology,* 7(3), 323–339.

[178] Lambert, S.J., & Henly, J.R. (2009). *Scheduling in Hourly Jobs: Promising Practices for the Twenty-First Century Economy.* The Mobility Agenda. Lambert, S.J. (2007). Making a Difference for Hourly Employees. In A. Booth, & A.C. Crouter, *Work-Life Policies that Make a Real Difference for Individuals, Families, and Communities.* Washington, DC: Urban Institute Press.

premium on that base wage for any overtime hours each week.[179] Similarly, employers may continue to provide these workers with the same level of benefits as previously, whether paid on an hourly or salary basis.

Quality of Public Services

To the extent that employers respond to this rule by restricting employee work hours, this rulemaking could negatively affect the quality of public services provided by local governments and nonprofits. However, the Department believes the effect of the rule on public services will be small. The Department acknowledges that some employees who work overtime providing public services may see a reduction in hours as an effect of the rulemaking. But if the services are in demand, the Department believes additional workers may be hired, as funding availability allows, to make up some of these hours, and productivity increases may offset some reduction in services. In addition, the Department expects many employers will adjust base wages downward to some degree so that even after paying the overtime premium, overall pay and hours of work for many employees will be relatively minimally impacted. Additionally, as noted above, many nonprofits are non-covered enterprises because when determining enterprise coverage only revenue derived from business operations, not charitable activities, is included.

Increased Prices

Business firms may pass along increased labor costs to consumers through higher prices. The Department anticipates that some firms may offset part of the additional labor costs through charging higher prices for the firms' goods and services. However, because costs and transfers are, on average, small relative to payroll and revenues, the Department does not expect the final rule to have a significant effect on prices. The Department estimated that, on average, costs and transfers make up less than 0.02 percent of payroll and less than 0.003 percent of revenues, although for specific industries and firms this percentage may be larger. Therefore, any potential change in prices would be modest. Further, any significant price increases would not represent a separate category of effects from those estimated in this economic analysis; rather, such price increases (where they occur) would be the channel through which consumers, rather than employers or employees, bear rule-induced costs (including transfers).

International Bancshares Corporation commented that the increased salary level could lead to increased prices, if ''anticipated wage gains do not result in productivity increases.'' As noted above, however, costs and transfers make up less than 0.02 percent of payroll; furthermore, payroll comprises only a fraction of the costs of producing goods and services in the U.S. economy. Therefore, the Department concludes the final rule will add little upward pressure to prices. To the extent that EAP-exempt employees are concentrated in some industries more than others, and thus specific industries might experience more pressure on wages, the Department notes that even in the industry where costs and transfers compose the highest percentage of payroll (agriculture, forestry, fishing, and hunting), that percentage is only 0.038 percent.

Reduced Profits

The increase in workers' earnings resulting from the revised salary level is a transfer of income from firms to workers, not a cost. The Department acknowledges that the increased employer costs and transfer payments as a result of this final rule may reduce the profits of business firms, although (1) some firms may offset some of these costs and transfers by making payroll adjustments, and (2) some firms may mitigate their reduced profits due to these costs and transfers through increased prices. To the extent that the final rule reduces profits at some business firms after all these adjustments are made, these firms would have marginally lower after-tax returns on new investments in equipment, structures, and intellectual property and could therefore make fewer such investments going forward. All else equal, less business investment slows economic growth and reduces employment. However, the Department expects that any anti-growth effects of the final rule would be minimal.

Hiring Costs

To the extent that firms respond to an update to the salary level test by reducing overtime hours, they may do so by spreading hours to other workers, including current workers employed for less than 40 hours per week by that employer, current workers who retain their exempt status, and newly hired workers. If new workers are hired to absorb these transferred hours, then the associated hiring costs are a cost of this final rule.

Other Costs Raised by Commenters

Some commenters asserted that the proposed rule would entail additional costs not detailed above. A few believe that the rule will result in increased employee turnover. SBA Advocacy wrote: ''Small businesses that reclassified their salaried staff to hourly staff as a result of the 2016 final rule reported that their employee turnover increased by up to 50 percent,'' forcing them to incur costs to hire and train new workers. According to SBA Advocacy, small businesses attributed this turnover to previously-exempt managers feeling ''demoralized'' by having to ''clock in'' due to their changed status, and suggested that this rule may have similar effects. Similarly, International Bancshares Corporation predicted that the proposed rule would result in layoffs, asserting that costs associated with ''reviewing the final regulations and building a software system to implement and monitor their compliance with the regulations'' would make it ''extremely difficult for community and regional banks to . . . [avoid] laying off employees or curtailing their operations.''

The Department believes these concerns are overstated. First, this final rule's increases to the earnings thresholds are much more modest than the 2016 final rule's, and the associated impacts are correspondingly more moderate. Thus, the Department believes that any adverse effects, such as increased turnover, will be minimal. Therefore, the Department has not quantified the potential costs associated with increased turnover. Likewise, the Department does not believe that this final rule will cause a significant number of layoffs. As explained above, the vast majority of firms employ both exempt and nonexempt workers and therefore have systems in place for managing nonexempt employees, and affected employees comprise less than 4 percent of EAP exempt employees. As such, the Department does not believe that the increased earnings thresholds in this final rule will cause layoffs to any significant extent, and has not quantified such costs.

iv. Transfers

1. Overview

Transfer payments occur when income is redistributed from one party to another. The Department has quantified two transfers from employers to employees that will result from the final rule: (1) Transfers to ensure compliance with the FLSA minimum wage provision; and (2) transfers to ensure compliance with the FLSA

[179] §§ 778.113–.114.

overtime pay provision. Transfers in Year 1 due to the minimum wage provision were estimated to be $75.4 million. The increase in the HCE compensation level does not affect minimum wage transfers because workers eligible for the HCE exemption earn well above the minimum wage. The Department estimates that transfers due to the overtime pay provision will be $321.0 million: $220.7 million from the increased standard salary level and $100.3 million from the increased HCE compensation level. Total Year 1 transfers are estimated at $396.4 million (Table 11).

TABLE 11—SUMMARY OF YEAR 1 REGULATORY TRANSFERS

[Millions]

Transfer from employers to workers	Standard salary level	HCE compensation level	Total
Due to minimum wage	$75.4	$0.0	$75.4
Due to overtime pay	220.7	100.3	321.0
Total transfers	296.1	100.3	396.4

Because the overtime premium depends on the base wage, the estimates of minimum wage transfers and overtime transfers are linked. This can be considered a two-step approach. The Department first identified affected EAP workers with an implicit regular hourly wage lower than the minimum wage, and then calculated the wage increase necessary to reach the minimum wage.

2. Transfers Due to the Minimum Wage Provision

For purposes of this analysis, the hourly rate of pay was calculated as usual weekly earnings divided by usual weekly hours worked. To earn less than the federal or most state minimum wages, this set of workers must work many hours per week. For example, a worker paid $455 per week must work 62.8 hours to earn less than the federal minimum wage of $7.25 per hour ($455/$7.25 = 62.8).[180] The applicable minimum wage is the higher of the federal minimum wage and the state minimum wage as of July 1, 2018. Most affected EAP workers already receive at least the minimum wage; only an estimated 1.8 percent of them (22,200 in total) earn an implicit hourly rate of pay less than the minimum wage. The Department estimated transfers due to payment of the minimum wage by calculating the change in earnings if wages rose to the minimum wage for workers who become nonexempt.[181]

In response to an increase in the regular rate of pay to the minimum wage, employers may reduce the workers' hours. Since the quantity of labor hours demanded is inversely related to wages, a higher mandated wage will result in fewer hours of labor demanded. For the first year, the Department estimated the potential disemployment effects (*i.e.,* the estimated reduction in hours) of the transfer attributed to the minimum wage by multiplying the percent change in the regular rate of pay by a labor demand elasticity of −0.2 (years 2–10 use a long run elasticity of −0.4) [182] [183]

At the new standard salary level, the Department estimated that 22,200 affected EAP workers will, on average, see an hourly wage increase of $1.39, work 2.4 fewer hours per week, and receive an increase in weekly earnings of $65.29 as a result of coverage by the minimum wage provisions (Table 12). The total change in weekly earnings due to the payment of the minimum wage was estimated to be $1.4 million per week ($65.29 × 22,200) or $75.4 million in Year 1.

TABLE 12—MINIMUM WAGE ONLY: MEAN HOURLY WAGES, USUAL OVERTIME HOURS, AND WEEKLY EARNINGS FOR AFFECTED EAP WORKERS, YEAR 1

	Hourly wage [a]	Usual weekly hours	Usual weekly earnings	Total weekly transfer (1,000s)
Before Final Rule	$8.75	61.4	$524.37	
After Final Rule	10.14	59.0	589.66	
Change	1.39	−2.4	65.29	1,450

Note: Pooled data for 7/2016–6/2018 adjusted to reflect 2018/2019.
[a] The applicable minimum wage is the higher of the federal minimum wage and the state minimum wage.

[180] Workers in states with minimum wages higher than the federal minimum wage could earn less than the state minimum wage working fewer hours.

[181] Because these workers' hourly wages will be set at the minimum wage after this final rule, their employers will not be able to adjust their wages downward to offset part of the cost of paying the overtime pay premium (which will be discussed in the following section). Therefore, these workers will generally receive larger transfers attributed to the overtime pay provision than other workers.

[182] Labor demand elasticity is the percentage change in labor hours demanded in response to a one percent change in wages.

[183] This elasticity estimate represents a short run demand elasticity for general labor, and is based on the Department's analysis of Lichter, A., Peichl, A. & Siegloch, A. (2014). The Own-Wage Elasticity of Labor Demand: A Meta-Regression Analysis. IZA DP No. 7958. We selected a general labor demand elasticity because employers will adjust their demand based on the cumulative change in employees' earnings, not on a conceptual differentiation between increases attributable to the minimum wage and the overtime provisions of the FLSA.

3. Transfers Due to the Overtime Pay Provision

Introduction

The final rule will transfer income to affected workers who work in excess of 40 hours per week. Requiring an overtime premium increases the marginal cost of labor, which employers will likely try to offset by adjusting wages and/or hours of affected workers. The size of the transfer will depend largely on how employers respond to the updated salary levels. Employers may respond by: (1) Paying overtime premiums to affected workers; (2) reducing overtime hours of affected workers and potentially transferring some of these hours to other workers; (3) reducing the regular rate of pay for affected workers working overtime (provided that the reduced rates still exceed the minimum wage); (4) increasing affected workers' salaries to the updated salary or compensation level to preserve their exempt status; or (5) using some combination of these responses. How employers will respond depends on many factors, including the relative costs of each of these alternatives; in turn, the relative costs of each of these alternatives are a function of workers' earnings and hours worked.

Literature on Employer Adjustments

Two conceptual models are useful for thinking about how employers may respond to reclassifying certain employees as overtime-eligible: (1) The ''fixed-wage'' or ''labor demand'' model, and (2) the ''fixed-job'' or ''employment contract'' model.[184] These models make different assumptions about the demand for overtime hours and the structure of the employment agreement, which result in different implications for predicting employer responses. The fixed-wage model assumes that the standard hourly wage is independent of the statutory overtime premium. Under the fixed-wage model, a reclassification of workers from overtime exempt to overtime nonexempt would cause a reduction in overtime hours for affected workers, an increase in the prevalence of a 40-hour workweek among affected workers, and an increase in the earnings of affected workers who continue to work overtime.

In contrast, the fixed-job model assumes that the standard hourly wage is affected by the statutory overtime premium. Thus, employers can neutralize any reclassification of workers from overtime exempt to overtime nonexempt by reducing the standard hourly wage of affected workers so that their weekly earnings and hours worked are unchanged, except when minimum wage laws prevent employers from lowering the standard hourly wage below the minimum wage. Under the fixed-job model, a reclassification of workers from overtime exempt to overtime nonexempt would have different effects on minimum-wage workers and above-minimum-wage workers. Similar to the fixed-wage model, minimum-wage workers would experience a reduction in overtime hours, an increase in the prevalence of a 40-hour workweek at a given employer (though not necessarily overall), and an increase in earnings for the portion of minimum-wage workers who continue to work overtime for a given employer. Unlike the fixed-wage model, however, above-minimum-wage workers would experience no change.

The Department conducted a literature review to evaluate studies of how labor markets adjust to a change in the requirement to pay overtime. In general, these studies are supportive of the fixed-job model of labor market adjustment, in that wages adjust to offset the requirement to pay an overtime premium as predicted by the fixed-job model, but do not adjust enough to completely offset the overtime premium as predicted by the model.

The Department believes the two most important papers in this literature are the studies by Trejo (1991) and Barkume (2010). Analyzing the economic effects of the overtime pay provisions of the FLSA, Trejo (1991) found ''the data analyzed here suggest the wage adjustments occur to mitigate the purely demand-driven effects predicted by the fixed-wage model, but these adjustments are not large enough to neutralize the overtime pay regulations completely.'' Trejo noted, ''In accordance with the fixed job model, the overtime law appears to have a greater impact on minimum-wage workers.'' He also stated, ''[T]he finding that overtime pay coverage status systematically influences the hours-of-work distribution for non-minimum wage works is supportive of the fixed-wage model. No significant differences in weekly earnings were discovered between the covered and non-covered sectors, which is consistent with the fixed-job model.'' However, ''overtime pay compliance is higher for union than for nonunion workers, a result that is more easily reconciled with the fixed wage model.'' Trejo's findings are supportive of the fixed-wage model whose adjustment is incomplete largely due to the minimum-wage requirement.[185]

A second paper by Trejo (2003) took a different approach to testing the consistency of the fixed-wage adjustment models with overtime coverage and data on hours worked. In this paper, he examined time-series data on employee hours by industry. After controlling for underlying trends in hours worked over 20 years, he found changes in overtime coverage had no impact on the prevalence of overtime hours worked. This result supports the fixed-job model. Unlike the 1991 paper, however, he did not examine impacts of overtime coverage on employees' weekly or hourly earnings, so this finding in support of the fixed-job model only analyzes one implication of the model.[186]

Barkume (2010) built on the analytic method used in Trejo (1991).[187] However, Barkume observed that Trejo did not account for ''quasi-fixed'' employment costs (*e.g.,* benefits) that do not vary with hours worked, and therefore affect employers' decisions on overtime hours worked. After incorporating these quasi-fixed costs in the model, Barkume found results consistent with those of Trejo (1991): ''though wage rates in otherwise similar jobs declined with greater overtime hours, they were not enough to prevent the FLSA overtime provisions from increasing labor costs.'' Barkume also determined that the 1991 model did not account for evidence that in the absence of regulation some employers may voluntarily pay workers some overtime premium to entice them to work longer hours, to compensate workers for unexpected changes in their schedules, or as a result of collective bargaining.[188] Barkume found that how much wages and hours worked adjusted in response to the overtime pay requirement

[184] *See* Trejo, S.J. (1991). The Effects of Overtime Pay Regulation on Worker Compensation. *American Economic Review,* 81(4), 719–740, and Barkume, A. (2010). The Structure of Labor Costs with Overtime Work in U.S. Jobs. *Industrial and Labor Relations Review,* 64(1), 128–142.

[185] Trejo, S. J. (1991). The Effects of Overtime Pay Regulation on Worker Compensation. *American Economic Review,* 81(4), 719–740.

[186] Trejo, S. J. (2003). Does the Statutory Overtime Premium Discourage Long Workweeks? Industrial and Labor Relations Review, 56(3), 375–392.

[187] Barkume, A. (2010). The Structure of Labor Costs with Overtime Work in U.S. Jobs. *Industrial and Labor Relations Review,* 64(1), 128–142.

[188] Barzel, Y. (1973). The Determination of Daily Hours and Wages. *The Quarterly Journal of Economics,* 87(2), 220–238, demonstrated that modest fluctuations in labor demand could justify substantial overtime premiums in the employment contract model. Hart, R. A. and Yue, M. (2000). Why Do Firms Pay an Overtime Premium? IZA Discussion Paper No. 163, showed that establishing an overtime premium in an employment contract can reduce inefficiencies.

depended on what overtime pay would be in absence of regulation.

In addition, Bell and Hart (2003) examined the standard hourly wage, average hourly earnings (including overtime), the overtime premium, and overtime hours worked in Britain. Unlike the United States, Britain does not have national labor laws regulating overtime compensation. Bell and Hart found that after accounting for overtime, average hourly earnings are generally uniform in a given industry because firms paying below-market level straight-time wages tend to pay above-market overtime premiums and firms paying above-market level straight-time wages tend to pay below-market overtime premiums. Bell and Hart concluded ''this is consistent with a model in which workers and firms enter into an implicit contract that specifies total hours at a constant, market-determined, hourly wage rate.[189] Their research is also consistent with studies showing that employers may pay overtime premiums either in the absence of a regulatory mandate (*e.g.,* Britain), or when the mandate exists but the requirements are not met (*e.g.,* United States).[190]

Finally, Kuroda and Yamamoto (2009) examined ''name only managers'' in Japanese labor markets and found essentially 100 percent adjustment of implicit hourly wages to offset the overtime pay requirement.[191] [192] This study suggests that these affected workers are all employed under the pure fixed-job model, so the implicit wage adjusted so that workers received no additional pay, and had essentially no change to hours worked. If applied to this rulemaking, transfers from employers to employees would occur only in cases in which the implicit hourly rate is less than the minimum wage. The Department estimates transfers would be about $193.4 million in Year 1 with 100 percent adjustment to the fixed-job model (compared with the Department's estimate of $396.4 million using the substantial, but incomplete fixed-job model, described in further detail below).

However, there are some challenges in generalizing Kuroda and Yamamoto's results to U.S. labor markets. First, ''name-only-managers would not be exempt in the U.S. because they do not meet the duties test for exemption. ''Name-only-managers'' are essentially identical to their peers, have no managerial responsibilities, and are distinguished only by their job title. This is not directly analogous to the case of EAP exempt employees, who do have managerial responsibilities, and must pass the duties test while other similar (but nonexempt) employees do not. Second, Kuroda also found that the pure fixed-job model results may not hold under all conditions. For example, in a following paper he found that during a recession, the labor market for ''name-only-managers'' behaved more like the fixed-wage model than the fixed-job model.[193] Third, some commenters on the NPRM provided survey results supporting that, among other responses, employers planned to respond to this rule (or responded or planned to respond to the 2016 final rule) by increasing salaries of some exempt employees to maintain their exempt status (*see* section VI.D.iv.5). This is inconsistent with Kuroda and Yamamoto's findings.

On balance, the Department finds strong support for the fixed-job model as the best approximation for the likely effects of a reclassification of above-minimum-wage workers from overtime exempt to overtime nonexempt and the fixed-wage model as the best approximation of the likely effects of a reclassification of minimum-wage workers from overtime exempt to overtime nonexempt. In addition, the studies suggest that although observed wage adjustment patterns are consistent with the fixed-job model, this evidence also suggests that the actual wage adjustment might, especially in the short run, be less than 100 percent as predicted by the fixed-job model. Thus, the hybrid model used in this analysis may be described as a substantial, but incomplete fixed-job model.

To determine the magnitude of the adjustment, the Department accounted for the following findings. Earlier research had demonstrated that in the absence of regulation some employers may voluntarily pay workers some overtime premium to entice them to work longer hours, to compensate workers for unexpected changes in their schedules, or as a result of collective bargaining.[194] Barkume (2010) found that the measured adjustment of wages and hours to overtime premium requirements depended on what overtime premium might be paid in absence of any requirement to do so. Thus, when Barkume assumed that workers would receive an average voluntary overtime pay premium of 28 percent in the absence of an overtime pay regulation, which is the average overtime premium that Bell and Hart (2003) found British employers paid in the absence of any overtime regulations, the straight-time hourly wage adjusted downward by 80 percent of the amount that would occur with the fixed-job model.[195] When Barkume assumed workers would receive no voluntary overtime pay premium in the absence of an overtime pay regulation, the results were more consistent with Trejo's (1991) findings that the adjustment was a smaller percentage. The Department modeled an adjustment process between these two findings. Although it seemed reasonable that some premium was paid for overtime in the absence of regulation, Barkume's assumption of a 28 percent initial overtime premium is likely too high for the salaried workers potentially affected by a change in the salary and compensation level requirements for the EAP exemptions because this assumption is based on a study of workers in Britain. British workers were likely paid a larger voluntary overtime premium than American workers because Britain did not have a required overtime pay regulation and so collective bargaining played a larger role in implementing overtime pay.[196] If the Department were to use only Barkume's assumptions and results to model employer adjustment to the overtime wage premium requirement for affected workers, estimated Year 1 transfers would total $247.9 million; further estimates derived from Barkume's findings will be presented later in the analysis. However, in the sections that

[189] Bell, D. N. F. and Hart, R. A. (2003). Wages, Hours, and Overtime Premia: Evidence from the British Labor Market, *Industrial and Labor Relations Review,* 56(3), 470–480.

[190] Hart, R. A. and Yue, M. (2000). Why Do Firms Pay an Overtime Premium? IZA Discussion Paper No. 163.

[191] Kuroda, S. and Yamamoto, I. (2009). How Are Hours Worked and Wages Affected by Labor Regulations?: The White-Collar Exemption and 'Name-Only Managers' in Japan. University of Tokyo Institute of Social Science. *Discussion Paper Series* No. F–147.

[192] The implicit hourly wage is calculated by dividing reported weekly earnings by reported hours worked.

[193] Kuroda, S. and Yamamoto, I. (2012). Impact of Overtime Regulations on Wages and Work Hours, *Journal of the Japanese and International Economies,* 26(2), 249–262.

[194] Barzel, Y. (1973). The Determination of Daily Hours and Wages. *The Quarterly Journal of Economics,* 87(2), 220–238, demonstrated that modest fluctuations in labor demand could justify substantial overtime premiums in the employment contract model. Hart, R. A. and Yue, M. (2000). Why Do Firms Pay an Overtime Premium? IZA Discussion Paper No. 163, showed that establishing an overtime premium in an employment contract can reduce inefficiencies.

[195] Barkume, A. (2010). The Structure of Labor Costs with Overtime Work in U.S. Jobs. *Industrial and Labor Relations Review,* 64(1), 128–142.

[196] Bell, D. N. F. and Hart, R. A. (2003). Wages, Hours, and Overtime Premia: Evidence from the British Labor Market, *Industrial and Labor Relations Review,* 56(3), 470–480.

immediately follow, the Department uses both papers to model transfers.

Identifying Types of Affected Workers

The Department identified four types of workers whose work characteristics affect how it modeled employers' responses to the changes in both the standard and HCE salary levels:

- *Type 1:* Workers who do not work overtime.
- *Type 2:* Workers who do not regularly work overtime but occasionally work overtime.
- *Type 3:* Workers who regularly work overtime and become overtime eligible (nonexempt).
- *Type 4:* Workers who regularly work overtime and remain exempt, because it is less expensive for the employer to pay the updated salary level than to pay overtime and incur additional managerial costs.

The Department began by identifying the number of workers in each type. After modeling employer adjustments, it estimated transfer payments. Type 3 and 4 workers were identified as those who regularly work overtime (CPS variable PEHRUSL1 greater than 40). Distinguishing Type 3 workers from Type 4 workers involved a four-step process. First, the Department identified all workers who regularly work overtime. Then the Department estimated each worker's weekly earnings if they became nonexempt, to which it added weekly managerial costs for each affected worker of $8.49 ($50.92 per hour × (10 minutes/60 minutes)).[197] Last, the Department identified as Type 4 those workers whose expected nonexempt earnings plus weekly managerial costs exceeds the updated standard salary level, and, conversely, as Type 3 those whose expected nonexempt earnings plus weekly managerial costs are less than the new standard salary.[198] The Department assumed that firms will include incremental managerial costs in their determination of whether to treat an affected employee as a Type 3 or Type 4 worker because those costs are only incurred if the employee is a Type 3 worker.

Identifying Type 2 workers involved two steps. First, using CPS MORG data, the Department identified those who do not usually work overtime but did work overtime in the survey week (the week referred to in the CPS questionnaire, variable PEHRACT1 greater than 40). Next, the Department supplemented the CPS data with data from the Survey of Income and Program Participation (SIPP) to look at likelihood of working some overtime during the year. Based on 2012 data, the most recent available, the Department found that 39.4 percent of non-hourly workers worked overtime at some point in a year. Therefore, the Department classified a share of workers who reported they do not usually work overtime, and did not work overtime in the reference week (previously identified as Type 1 workers), as Type 2 workers such that a total of approximately 39.4 percent of affected workers were Type 2, 3, or 4.

Modeling Changes in Wages and Hours

The substantial, but incomplete fixed-job model (hereafter referred to as the incomplete fixed-job model) predicts that employers will adjust wages of regular overtime workers but not to the full extent indicated by fixed-job model, and thus some employees may receive a small increase in weekly earnings due to overtime pay coverage. When modeling employer responses with respect to the adjustment to the regular rate of pay, the Department used the incomplete fixed-job model.

In this portion of the analysis, the Department presents an estimate of the effect on the implicit hourly rate of pay for regular overtime workers should be determined using the average of two estimates of the incomplete fixed-job model adjustments: Trejo's (1991) estimate that the overtime-induced wage change is 40 percent of the adjustment toward the amount predicted by the fixed-job model, assuming an initial zero overtime pay premium, and Barkume's (2010) estimate that the wage change is 80 percent of the predicted adjustment assuming an initial 28 percent overtime pay premium.[199] This is approximately equivalent to assuming that salaried overtime workers implicitly receive the equivalent of a 14 percent overtime premium in the absence of regulation (the midpoint between 0 and 28 percent).

Modeling changes in wages, hours, and earnings for Type 1 and Type 4 workers was relatively straightforward. Type 1 affected EAP workers will become overtime-eligible, but because they do not work overtime, they will see no change in their weekly earnings. Type 4 workers will remain exempt because their earnings will be raised to at least the updated EAP level (either the standard salary level or HCE compensation level). These workers' earnings will increase by the difference between their current earnings and the amount necessary to satisfy the new salary or compensation level. It is possible employers will increase these workers' hours in response to paying them a higher salary, but the Department did not have enough information to model this potential change.[200]

Modeling changes in wages, hours, and earnings for Type 2 and Type 3 workers was more complex. The Department distinguished those who regularly work overtime (Type 3 workers) from those who occasionally work overtime (Type 2 workers) because employer adjustment to the final rule may differ accordingly. Employers are more likely to adjust hours worked and wages for regular overtime workers because their hours are predictable. However, in response to a transient, perhaps unpredicted, shift in market demand for the good or service such employers provide, employers are more likely to pay for occasional overtime rather than adjust hours worked and pay.

The Department treated Type 2 affected workers in two ways due to the uncertainty of the nature of these occasional overtime hours. The Department assumed that 50 percent of these occasional overtime workers worked *expected* overtime hours and the other 50 percent worked *unexpected* overtime. Workers were randomly assigned to these two groups. Workers with *expected* occasional overtime hours were treated like Type 3 affected workers (incomplete fixed-job model adjustments). Workers with *unexpected* occasional overtime hours were assumed to receive a 50 percent pay premium for the overtime hours worked and receive no change in base wage or hours (full overtime premium

[197] *See supra* § VI.D.iii.4 (managerial costs).

[198] When analyzing impacts of increasing the standard salary level, Rohwedder and Wenger conducted a similar analysis; however, they use straight-time pay rather than overtime pay to calculate earnings in the absence of a pay raise to remain exempt. Rohwedder, S. and Wenger, *supra* note 130.

[199] Both studies considered a population that included hourly workers. Evidence is not available on how the adjustment towards the employment contract model differs between salaried and hourly workers. The employment contract model may be more likely to hold for salaried workers than for hourly workers since salaried workers directly observe their weekly total earnings, not their implicit equivalent hourly wage. Thus, applying the partial adjustment to the employment contract model as estimated by these studies may overestimate the transfers from employers to salaried workers. We do not attempt to quantify the magnitude of this potential overestimate.

[200] Cherry, Monica, ''Are Salaried Workers Compensated for Overtime Hours?'' *Journal of Labor Research* 25(3): 485–494, September 2004, found that exempt full-time salaried employees earn more when they work more hours, but her results do not lend themselves to the quantification of the effect *on* hours of an increase in earnings.

model).[201] When modeling Type 2 workers' hour and wage adjustments, the Department treated those identified as Type 2 using the CPS data as representative of all Type 2 workers. The Department estimated employer adjustments and transfers assuming that the patterns observed in the CPS reference week are representative of an average week in the year. Thus, the Department assumes total transfers for the year are equal to 52 times the transfers estimated for the single representative week for which the Department has CPS data. However, these transfers are spread over a larger group including those who occasionally work overtime but did not do so in the CPS reference week.[202]

Since employers must now pay more for the same number of labor hours, for Type 2 and Type 3 EAP workers, the quantity of labor hours demanded by employers will decrease. It is the net effect of these two changes that will determine the final weekly earnings for affected EAP workers. The reduction in hours is calculated using the elasticity of labor demand with respect to wages. The Department used a short-term demand elasticity of -0.20 to estimate the percentage decrease in hours worked in Year 1 and a long-term elasticity of -0.4 to estimate the percentage decrease in hours worked in Years 2–10.[203]

For Type 3 affected workers, and the 50 percent of Type 2 affected workers who worked *expected* overtime, the Department estimated adjusted total hours worked after making wage adjustments using the incomplete fixed-job model. To estimate adjusted hours worked, the Department set the percent change in total hours worked equal to the percent change in average wages multiplied by the wage elasticity of labor demand.[204]

Figure 3 is a flow chart summarizing the four types of affected EAP workers. Also shown are the effects on exempt status, weekly earnings, and hours worked for each type of affected worker.

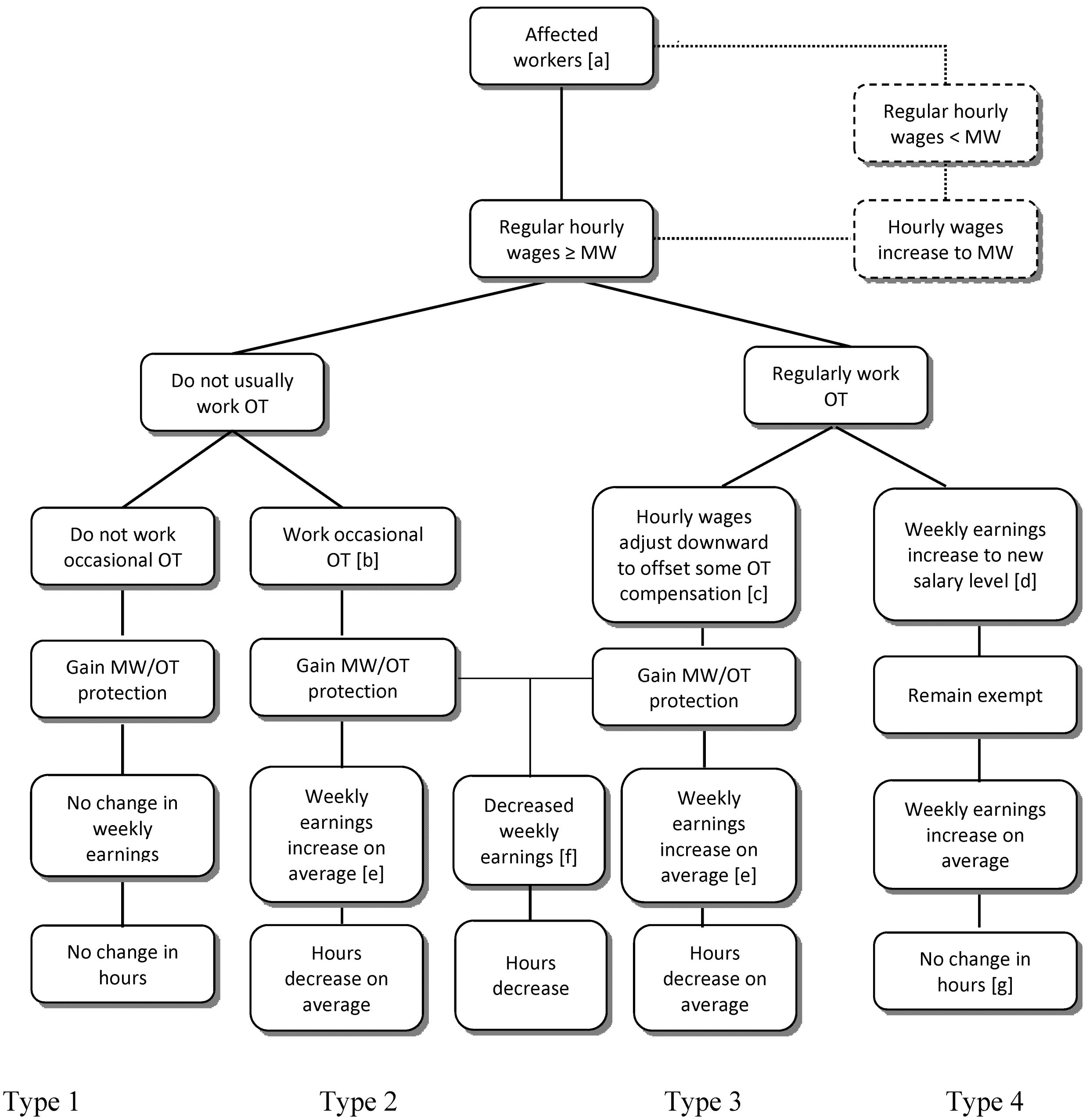
[201] We use the term ''full overtime premium'' to describe the adjustment process as modeled. The full overtime premium model is a special case of the general fixed-wage model in that the Department assumes the demand for labor under these circumstances is completely inelastic. That is, employers make no changes to employees' hours in response to these temporary, unanticipated changes in demand.

[202] If a different week was chosen as the survey week, then likely some of these workers would not have worked overtime. However, because the data are representative of both the population and all twelve months in a year, the Department believes the share of Type 2 workers identified in the CPS data in the given week is representative of an average week in the year.

[203] This elasticity estimate is based on the Department's analysis of Lichter, A., Peichl, A. & Siegloch, A. (2014). The Own-Wage Elasticity of Labor Demand: A Meta-Regression Analysis. IZA DP No. 7958. Some researchers have estimated larger impacts on the number of overtime hours worked (Hamermesh, D. and S. Trejo. (2000)). The Demand for Hours of Labor: Direct Evidence from California. *The Review of Economics and Statistics,* 82(1), 38–47 concludes the price elasticity of demand for overtime hours is at least -0.5. The Department decided to use a general measure of elasticity applied to the average change in wages since the increase in the overtime wage is somewhat offset by a decrease in the non-overtime wage as indicated in the fixed-job model.

[204] In this equation, the only unknown is adjusted total hours worked. Since adjusted total hours worked is in the denominator of the left side of the equation and is also in the numerator of the right side of the equation, solving for adjusted total hours worked requires solving a quadratic equation.

Figure 3: Flow Chart of Final Rule's Effect on Earnings and Hours Worked



[a] Affected EAP workers are those who are exempt under the current EAP exemptions and will gain minimum wage and overtime protection or receive a raise to the increased salary or compensation level.

[b] There are two methods the Department uses to identify occasional overtime workers. The first includes workers who report they usually work 40 hours or less per week (identified with variable PEHRUSL1 in CPS MORG) but in the reference week worked more than 40 hours (variable PEHRACT1 in CPS MORG). The second includes reclassifying some additional workers who usually work 40 hours or less per week, and in the reference week worked 40 hours

or less, to match the proportion of workers measured in other data sets who work overtime at any point in the year.
[c] The amount wages are adjusted downwards depends on whether the fixed-job model or the fixed-wage model holds. The Department's preferred method uses a combination of the two. Employers reduce the regular hourly wage rate somewhat in response to overtime pay requirements, but the wage is not reduced enough to keep total compensation constant.
[d] Based on hourly wage and weekly hours it is more cost efficient for the employer to increase the worker's weekly salary to the updated salary level than to pay overtime pay.
[e] On average, the Department expects employees' overall weekly earnings will increase despite a small decrease in average hours worked.
[f] In some cases, employers might decrease employees' hours enough to cause those employees' weekly earnings to decrease. If so, such employees may seek a second job to offset their lost weekly earnings. In extreme cases, some workers may become unemployed.
[g] The Department assumed hours would not change, due to lack of data and relevant literature; however, it is possible employers will increase these workers' hours in response to paying them a higher salary or to avoid paying overtime premiums to newly nonexempt coworkers.

Estimated Number of and Effects on Affected EAP Workers

The Department estimated the final rule will affect 1.3 million workers (Table 13), of which 762,200 were Type 1 workers (60.6 percent of all affected EAP workers), 300,900 were estimated to be Type 2 workers (23.9 percent of all affected EAP workers), 154,000 were Type 3 workers (12.3 percent of all affected EAP workers), and 40,100 were estimated to be Type 4 workers (3.2 percent of all affected workers). All Type 3 workers and half of Type 2 employees (304,500) are assumed to work predictable overtime.

TABLE 13—AFFECTED EAP WORKERS BY TYPE (1,000S), YEAR 1

	Total	No overtime (T1)	Occasional overtime (T2)	Regular overtime	
				Newly nonexempt (T3)	Remain exempt (T4)
Standard salary level	1,155.6	700.3	296.8	126.8	31.7
HCE compensation level	101.8	62.0	4.1	27.2	8.5
Total	1,257.3	762.2	300.9	154.0	40.1

Note: Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.
* *Type 1:* Workers without regular OT and without occasional OT and become overtime eligible.
* *Type 2:* Workers without regular OT but with occasional OT. These workers become overtime eligible.
* *Type 3:* Workers with regular OT who become overtime eligible.
* *Type 4:* Workers with regular OT who remain exempt (i.e., earnings increase to the updated salary level).

The final rule will affect some affected workers' hourly wages, hours, and weekly earnings. Predicted changes in implicit wage rates are outlined in Table 14, changes in hours in Table 15, and changes in weekly earnings in Table 16. How these will change depends on the type of worker, but on average the Department projects that weekly earnings will be unchanged or increase while hours worked will be unchanged or decrease.

Type 1 workers will have no change in wages, hours, or earnings.[205] Employers were assumed to be unable to adjust the hours or regular rate of pay for the occasional overtime workers whose overtime is irregularly scheduled and unpredictable. The Department used the incomplete fixed-job model to estimate changes in the regular rate of pay for Type 3 workers and the 50 percent of Type 2 workers who regularly work occasional overtime. As a group, Type 2 workers will see a decrease in their average regular hourly wage; however, because these workers will now receive a 50 percent premium on their regular hourly wage for each hour worked in excess of 40 hours per week, average weekly earnings for Type 2 workers will increase.[206]

Similarly, Type 3 workers will also receive decreases in their regular hourly wage as predicted by the incomplete fixed-job model but an increase in weekly earnings because these workers will now be eligible for the overtime premium. Type 4 workers' implicit hourly rates of pay will increase to meet the updated standard salary level or HCE annual compensation level.

[205] It is possible that these workers may experience an increase in hours and weekly earnings because of transfers of hours from other newly nonexempt workers who do usually work overtime. Due to the high level of uncertainty in employers' responses regarding the transfer of hours, the Department did not have credible evidence to support an estimation of the number of hours transferred to other workers.

[206] Type 2 workers do not see increases in regular earnings to the new salary level (as Type 4 workers do) even if their new earnings in this week exceed that new level. This is because the estimated new earnings only reflect their earnings in that week when overtime is worked; their earnings in typical weeks that they do not work overtime do not exceed the salary level.

TABLE 14—AVERAGE REGULAR RATE OF PAY BY TYPE OF AFFECTED EAP WORKER, YEAR 1

	Total	No overtime (T1)	Occasional overtime (T2)	Regular overtime	
				Newly nonexempt (T3)	Remain exempt (T4)
Standard Salary Level					
Before Final Rule	$15.85	$16.71	$16.15	$11.39	$11.91
After Final Rule	$15.81	$16.71	$16.09	$10.97	$12.51
Change ($)	−$0.04	$0.00	−$0.06	−$0.42	$0.60
Change (%)	−0.3%	0.0%	−0.4%	−3.7%	5.1%
HCE Compensation Level					
Before Final Rule	$46.94	$51.63	$49.81	$38.80	$37.46
After Final Rule	$46.32	$51.63	$47.53	$36.55	$38.27
Change ($)	−$0.63	$0.00	−$2.29	−$2.26	$0.81
Change (%)	−1.3%	0.0%	−4.6%	−5.8%	2.2%

Note: Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.
* *Type 1:* Workers without regular OT and without occasional OT and become overtime-eligible.
* *Type 2:* Workers without regular OT but with occasional OT. These workers become overtime eligible.
* *Type 3:* Workers with regular OT who become overtime eligible.
* *Type 4:* Workers with regular OT who remain exempt (i.e., earnings increase to the updated salary level).

Hours for Type 1 workers will not change. Similarly, hours will not change for the half of Type 2 workers who work irregular overtime. Half of Type 2 and all Type 3 workers will see a small decrease in their hours of overtime worked. This reduction in hours is relatively small and is due to the effect on labor demand from the increase in the average hourly wage as predicted by the incomplete fixed-job model (Table 15). Type 4 workers' hours may increase, but due to lack of data, the Department assumed hours would not change.

TABLE 15—AVERAGE WEEKLY HOURS FOR AFFECTED EAP WORKERS BY TYPE, YEAR 1

	Total	No overtime worked (T1)	Occasional OT (T2)	Regular OT	
				Newly nonexempt (T3)	Remain exempt (T4)
Standard Salary Level [a]					
Before Final Rule	39.9	37.5	39.2	50.4	56.6
After Final Rule	39.8	37.5	39.1	49.8	56.6
Change (hours)	−0.1	0.0	0.0	−0.6	0.0
Change (%)	−0.2%	0.0%	−0.1%	−1.2%	0.0%
HCE Compensation Level [a]					
Before Final Rule	44.2	39.4	48.4	51.0	54.9
After Final Rule	44.1	39.4	48.2	50.7	54.9
Change (hours)	−0.1	0.0	−0.3	−0.3	0.0
Change (%)	−0.2%	0.0%	−0.5%	−0.7%	0.0%

Note: Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.
[a] Usual hours for Types 1, 3, and 4 but actual hours for Type 2 workers identified in the CPS MORG.
* *Type 1:* Workers without regular OT and without occasional OT and become overtime eligible.
* *Type 2:* Workers without regular OT but with occasional OT. These workers become overtime eligible.
* *Type 3:* Workers with regular OT who become overtime eligible.
* *Type 4:* Workers with regular OT who remain exempt (i.e., earnings increase to the updated salary level).

Because most Type 1 workers will not experience a change in their regular rate of pay or hours, they will have no change in earnings due to the final rule (Table 16).[207] Although Type 2 and Type 3 workers will, on average, experience a decrease in both their regular rate of pay and hours worked, their weekly earnings will increase as a result of the overtime premium. Weekly earnings after the standard salary level increased were estimated using the new wage (*i.e.,* the incomplete fixed-job model wage) and the reduced number of overtime hours worked. Type 4 workers' salaries will increase to the new standard salary level or the HCE compensation level.

[207] The small increase in average weekly earnings for Type 1 workers is due to increasing the weekly earnings in the District of Columbia to the minimum wage ($13.25 per hour).

TABLE 16—AVERAGE WEEKLY EARNINGS FOR AFFECTED EAP WORKERS BY TYPE, YEAR 1

	Total	No overtime (T1)	Occasional overtime (T2)	Regular overtime	
				Newly nonexempt (T3)	Remain exempt (T4)
Standard Salary Level [a]					
Before Final Rule	$581.42	$575.71	$594.52	$566.67	$643.94
After Final Rule	$586.34	$575.72	$599.48	$589.91	$684.00
Change ($)	$4.93	$0.01	$4.96	$23.24	$40.06
Change (%)	0.8%	0.0%	0.8%	4.1%	6.2%
HCE Compensation Level [a]					
Before Final Rule	$1,989.41	$1,973.57	$2,415.63	$1,950.93	$2,021.82
After Final Rule	$2,008.37	$1,973.57	$2,467.78	$2,000.16	$2,066.00
Change ($)	$18.96	$0.00	$52.15	$49.24	$44.18
Change (%)	1.0%	0.0%	2.2%	2.5%	2.2%

Note: Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.
[a] The mean of the hourly wage multiplied by the mean of the hours does not necessarily equal the mean of the weekly earnings because the product of two averages is not necessarily equal to the average of the product.
* *Type 1:* Workers without regular OT and without occasional OT and become overtime eligible.
* *Type 2:* Workers without regular OT but with occasional OT. These workers become overtime eligible.
* *Type 3:* Workers with regular OT who become overtime eligible.
* *Type 4:* Workers with regular OT who remain exempt (i.e., earnings increase to the updated salary level).

At the new standard salary level, the average weekly earnings of affected workers will increase $4.93 (0.8 percent), from $581.42 to $586.34. Multiplying the average change of $4.93 by the 1.2 million EAP workers affected by the change in the standard salary level and 52 weeks equals an increase in earnings of $296.1 million in the first year (Table 17). For workers affected by the change in the HCE compensation level, average weekly earnings will increase by $18.96. When multiplied by 101,800 affected workers and 52 weeks, the national increase will be $100.3 million in the first year. Thus, total Year 1 transfer payments attributable to this final rule will total $396.4 million.

TABLE 17—TOTAL CHANGE IN WEEKLY AND ANNUAL EARNINGS FOR AFFECTED EAP WORKERS BY PROVISION, YEAR 1

Provision	Annual change in earnings (1,000s)
Total	$396,424
Standard salary level:	
Total	296,078
Minimum wage only	75,376
Overtime pay only [a]	220,702
HCE compensation level:	
Total	100,345
Minimum wage only	
Overtime pay only [a]	100,345

[a] Estimated by subtracting the minimum wage transfer from the total transfer.

Rohwedder and Wenger (2015) analyzed the effects of increasing the standard salary level.[208] They compared hourly and salaried workers in the CPS using quantile treatment effects. This methodology estimates the effect of a worker becoming nonexempt by comparing similar workers who are hourly and salaried. They found no statistically significant change in hours or wages on average. However, their point estimates, averaged across all affected workers, show small increases in earnings and decreases in hours, similar to our analysis. For example, using a salary level of $750, they estimated weekly earnings may increase between $2 and $22 and weekly hours may decrease by approximately 0.4 hours. The Department estimated weekly earnings for workers affected by the standard salary level will increase by $4.93 and hours will decrease by 0.1 hours.

4. Potential Transfers Not Quantified

There may be additional transfers attributable to this final rule; however, the magnitude of these other transfers could not be quantified and therefore are discussed only qualitatively.

Reduced Earnings for Some Workers

Holding regular rate of pay and work hours constant, payment of an overtime premium will increase weekly earnings for workers who work overtime. However, as discussed previously, employers may try to mitigate cost increases by reducing the number of overtime hours worked, either by transferring these hours to other workers or monitoring hours more closely. Depending on how hours are adjusted, a specific worker may earn less pay after this final rule.

Additional Work for Some Workers

Affected workers who remain exempt will see an increase in pay but may also see an increase in workload. The Department estimated the net changes in hours, but due to the data limitations as noted in section VI.D.iv.3, did not estimate changes in hours for affected workers whose salary is increased to the new threshold so they remain overtime exempt.

Reduction in Bonuses and Benefits for Some Workers

Employers may offset increased labor costs by reducing bonuses or benefits instead of reducing base wages or hours worked. Due to data limitations, the Department has not modeled this effect separately. The Department observes that any reductions in bonuses or benefits would be likely accompanied by smaller reductions in base wages or hours worked.

Several commenters stated that in order to pay for the higher payroll costs, they would decrease employee benefits. These comments were mostly general statements, often included in a list of changes the employer intends to make in response to the increased salary threshold. Others stated that employees would lose benefits due to being reclassified as hourly workers. However, as the Department previously noted, this regulation does not require that workers who become nonexempt must be

[208] Rohwedder and Wenger, *supra* note 130.

reclassified as hourly nor does it require that hourly workers receive fewer benefits than salaried workers. Additionally, some commenters stated that these employees would have reductions in their ability to earn commissions, bonuses, or other types of incentive payments, but these commenters generally did not discuss the net impact on these employees' earnings. These comments did not provide information that would allow the Department to estimate the purported impact of the final rule on employee benefits.

5. NPRM Comments on Transfer Calculations

In response to the NPRM, the Department's RFI, and at listening sessions, some commenters provided information concerning their proposed wage and hour adjustments in anticipation of an increase to the standard salary level and HCE total compensation level. In comments on the NPRM, Capital Associated Industries submitted the results from a survey of their members, which conveyed that employers plan to respond in different ways such as increasing salaries of exempt employees so that they remain exempt, or decreasing the hours or hourly rates of newly nonexempt employees. A survey of members of the International Public Management Association for Human Resources found ''an almost even split between those who would increase salaries of exempt employees to the new threshold and those who would shift currently exempt employees to nonexempt status'' in response to the proposed standard salary level.

In responses to the Department's RFI, commenters representing employer interests indicated that employers would respond to a new salary level by making a variety of adjustments to wages, hours worked, or both. Some commenters' feedback supports adoption of an incomplete fixed-job model. For example, Littler Mendelson and the U.S. Chamber of Commerce reported that, among surveyed employers with exempt employees who would become nonexempt under the 2016 final rule, 28.7 percent reported that they planned to ''allow [newly nonexempt employees] to work the same number of hours and earn overtime compensation without restriction,'' compared to just 18.6 percent who planned to reduce effective hourly rates ''so that their total pay remained the same.'' The Chamber's survey did not ask whether employers planned to adopt a combination of those two responses (*i.e.,* paying overtime premiums while partially reducing effective hourly rates).

In this final rule, the Department estimated that some workers will see their earnings increase to the new earnings levels and remain exempt. There is some evidence that employers will respond in this manner. For example, in response to the RFI, the Chamber reported that, of surveyed employers who had implemented or made plans to implement changes to comply with the 2016 final rule, 76.4 percent reported that they had increased or planned to increase the salaries of some exempt employees to retain their exempt status. Similarly, the American Hotel and Lodging Association reported that 43 percent of their members raised the salaries of at least one worker to a figure above the 2016 final rule's salary threshold. It is possible that employers will increase the salaries paid to some ''occasional'' overtime workers to maintain the exemption for those workers, but the Department has no way of identifying these workers.

Regarding the proposed transfer calculations, SBA Advocacy took issue with the Department's estimates that affected small business establishments would have, on average, $422 to $3,187 in additional payroll costs in the first year of the proposed rule. Rather, SBA Advocacy stated that ''[s]mall businesses have told Advocacy that their [additional] payroll costs will be in the thousands of dollars.'' This comment, however, does not explain what methodological approach the Department should use to estimate transfers; what error(s), if any, the Department's method contains; or how much, if at all, the Department's approach underestimated such transfers. Therefore, the Department has not made any changes to the methodology in response to this comment.

The National Association of Manufacturers (NAM), in its comment opposing the proposed rule's HCE total annual compensation threshold of $147,414, stated that such a threshold would impact many manufacturers who currently employ numerous exempt HCE employees. It contended that ''[i]n the representative case of one large manufacturer, approximately 1,200 individuals—nearly 11% of the company's workforce—are exempt employees earning between $100,000 and $147,414 annually. For this manufacturer, the difference between 'exempt' and 'almost exempt' is estimated to be between $8 million and $20 million in potential overtime exposure per year.'' Using the upper end of NAM's transfer cost range, this equates to $16,667 per affected worker. This single anecdote, however, does not provide a sufficient basis for the Department to change the methodology used to calculate transfers. Moreover, NAM's concerns are mitigated by the Department's decision to set the HCE total annual compensation level to $107,432 instead of to $147,414.

The Department further notes that its estimates of transfers are informed by its projection that employers will respond to the final rule in a number of ways. If, for example, an employer simply pays each affected employee the overtime premium for each hour worked in excess of 40 hours per week, without making any adjustments to wages, hours or duties, such an approach would maximize transfers from employers to employees. However, as discussed above, the Department believes that employers will respond to the final rule by adjusting wages, hours, and duties to minimize the cost of the rule. The Department's approach is supported by both the literature the Department reviewed examining employers' response to overtime premium pay requirements, as well as survey data and anecdotal evidence provided in response to the NPRM and RFI regarding employers' responses to the 2016 final rule and planned responses to this rulemaking. Accordingly, the actual amount of transfers will fall well short of the transfers that would result if employers simply paid each affected employee overtime premiums without adjusting wages, hours, or duties.

v. Benefits and Cost Savings

Potential Benefits and Effects Not Discussed Elsewhere

The Department has determined that the final rule will provide some benefits; however, these benefits could not be quantified due to data limitations, requiring the Department to discuss such benefits only qualitatively.

1. Reduce Employee Misclassification

The revised salary level reduces the likelihood of workers being misclassified as exempt from overtime pay, providing an additional measure of the effectiveness of the salary level as a bright-line test delineating exempt and nonexempt workers. The Department's analysis of misclassification drew on CPS data and looked at workers who are white collar, salaried, subject to the FLSA and covered by part 541 regulations, earn a weekly salary of at least $455 but less than $684, and fail the duties test. Because only workers who work overtime may receive overtime pay, when determining the share of workers who are misclassified the sample was limited to those who usually work overtime. Workers were considered misclassified if they did not receive overtime pay.[209] The Department estimated that 9.3 percent of workers in this analysis who usually worked overtime did not receive overtime compensation and are therefore misclassified as exempt. Applying this estimate to the sample of white collar salaried workers who fail the duties test and earn at least $455 but less than $684, the Department estimated that there are approximately 206,900 white collar salaried workers who are overtime-eligible but whose employers do not recognize them as such.[210] These employees' entitlement to overtime pay will now be abundantly evident.

RAND has conducted a survey to identify the number of workers who may be misclassified as EAP exempt. The survey, a special module to the American Life Panel, asks respondents: (1) Their hours worked, (2) whether they are paid on an hourly or salary basis, (3) their typical earnings, (4) whether they perform certain job responsibilities that are treated as proxies for whether they would justify exempt status, and (5) whether they receive any overtime pay. Using these data, Susann Rohwedder and Jeffrey B. Wenger[211] found that ''11.5 percent of salaried workers were classified as exempt by their employer although they did not meet the criteria for being so.'' Using RAND's estimate of the rate of misclassification (11.5 percent), the Department estimated that approximately 255,400 salaried workers earning between $455 and $684 per week who fail the standard duties test are currently misclassified as exempt.[212] By raising the salary level the final rule will increase the likelihood that these workers will be correctly classified as nonexempt.

2. Reduced Litigation

One result of enforcing the 2004 standard salary level for 15 years is that the established ''dividing line'' between EAP workers who are exempt and not exempt has gradually eroded and no longer holds the same relative position in the distribution of nominal wages and salaries. Therefore, as nominal wages and salaries for workers have increased over time, while the standard salary level has remained constant, more workers earn above the ''dividing line'' and have moved from nonexempt to potentially exempt. The Department's enforcement of the 2004 salary levels has burdened employers with performing duties tests to determine overtime exemption status of white collar workers for a larger proportion of workers than in 2004 and has created uncertainty regarding the correct classification of workers as nonexempt or exempt. This may have contributed to an increase in FLSA lawsuits since 2004,[213] much of which has involved cases regarding whether workers who satisfy the salary level test also meet the duties test for exemption.

Updating the standard salary level should restore the relative position of the standard salary level in the overall distribution of nominal wages and salaries as set forth in the 2004 rule. Increasing the standard salary level from $455 per week to the level set in this final rule of $684 per week will increase the number of white collar workers for whom the standard salary level test is determinative of their nonexempt status, and employers will no longer have to perform a duties analysis for these employees. This final rule's update to the standard salary level will reduce the burden on employers and may reduce legal challenges and the overall cost of litigation faced by employers in FLSA overtime lawsuits, specifically litigation that turns on whether workers earning above the current salary and earnings thresholds but below the levels set in this final rule pass the duties test. The size of the potential social benefit from fewer legal challenges and the corresponding decline in overall litigation costs is difficult to quantify, but a reduction in litigation costs would benefit employers and workers.

To provide a general estimate of the size of the potential benefits from reducing litigation, the Department used data from the federal courts' Public Access to Court Electronic Records (PACER) system and the CPS to estimate the number and percentage of FLSA cases that concern EAP exemptions and are likely to be affected by the final rule. For this step of the analysis, to avoid using data that could reflect changed behavior in anticipation of the 2016 final rule, the Department used the data gathered during the 2016 rulemaking. As explained in that rule, to determine the potential number of cases that will likely be affected by the final rule, the Department obtained a list of all FLSA cases closed in 2014 from PACER (8,256 cases).[214] From this list, the Department selected a random sample of 500 cases. The Department identified the cases within this sample that were associated with the EAP exemptions. The Department found that 12.0 percent of these FLSA cases (60 of 500) were related to the EAP exemptions. Next, the Department determined what share of these cases could potentially be avoided by an increase in the standard salary and HCE compensation levels.

The Department estimated the share of EAP cases that may be avoided due to the final rule by using data on the salaried earnings distribution from the 2018/19 CPS MORG to determine the share of EAP cases in which workers earn at least $455 but less than $684 per week or at least $100,000 but less than $107,432 annually. From CPS, the Department selected white collar, nonhourly workers as the appropriate reference group for defining the earnings distribution rather than exempt workers because if a worker is litigating his or her exempt status, then we do not know if that worker is exempt or not. Based on this analysis, the Department determined that 13.5 percent of white collar nonhourly workers had earnings within these ranges. Applying these findings to the 12 percent of cases associated with the EAP exemption yields an estimated 1.6 percent of FLSA cases, or about 133 cases, that may be avoidable. The assumption underlying this method is that workers who claim they are misclassified as EAP exempt have a similar earnings distribution as all white collar nonhourly workers.

After determining the potential number of EAP cases that the final rule may avoid, the Department examined a selection of 56 FLSA cases concluded between 2012 and 2015 that contained litigation cost information to estimate the average costs of litigation to assign

[209] Overtime pay status was based on worker responses to the CPS MORG question concerning whether they receive overtime pay, tips, or commissions at their job (''PEERNUOT'' variable).

[210] The Department applies the misclassification estimate derived here to both the group of workers who usually work more than 40 hours and to those who do not.

[211] Rohwedder and Wenger, *supra* note 130.

[212] The number of misclassified workers estimated based on the RAND research cannot be directly compared to the Department's estimates because of differences in data, methodology, and assumptions. Although it is impossible to reconcile the two different approaches without further information, by calculating misclassified workers as a percent of all salaried workers in its sample, RAND uses a larger denominator than the Department. If calculated on a more directly comparable basis, the Department expects the RAND estimate of the misclassification rate would still be higher than the Department's estimate.

[213] *See* Lydia DePillis, *Why wage and hour litigation is skyrocketing,* Washington Post (Nov. 25, 2015), *https://www.washingtonpost.com/news/wonk/wp/2015/11/25/people-are-suing-more-than-ever-over-wages-and-hours; Uptick in FLSA Litigation Expected to Continue in 2016,* BNA Daily Labor Report (Nov. 25, 2015), *https://bnanews.bna.com/daily-labor-report/uptick-in-flsa-litigation-expected-to-continue-in-2016.*

[214] *See* 81 FR 32501.

to the potentially avoided EAP cases.[215] To calculate average litigation costs associated with these cases, the Department looked at records of court filings in the Westlaw Case Evaluator tool and on PACER to ascertain how much plaintiffs in these cases were paid for attorney fees, administrative fees, and/or other costs, apart from any monetary damages attributable to the alleged FLSA violations. (The FLSA provides for successful plaintiffs to be awarded reasonable attorney's fees and costs, so this data is available in some FLSA cases.) After determining the plaintiff's total litigation costs for each case, the Department then doubled the figures to account for litigation costs that the defendant employers incurred.[216] According to this analysis, the average litigation cost for FLSA cases concluded between 2012 and 2015 was $654,182.[217] Applying this figure to the approximately 133 EAP cases that could be prevented as a consequence of this rulemaking, the Department estimated that avoided litigation costs resulting from the rule may total approximately $87.0 million per year. The Department believes these totals may underestimate total litigation costs because some FLSA overtime cases are heard in state court and thus were not captured by PACER; some FLSA overtime matters are resolved before litigation or by alternative dispute resolution; and some attorneys representing FLSA overtime plaintiffs may take a contingency fee atop their statutorily awarded fees and costs.

The Department did not receive any comments on the methodology it used to estimate potential reduced litigation costs.

[215] The 56 cases used for this analysis were retrieved from Westlaw's Case Evaluator database using a keyword search for case summaries between 2012 and 2015 mentioning the terms ''FLSA'' and ''fees.'' Although the initial search yielded 64 responsive cases, the Department excluded one duplicate case, one case resolving litigation costs through a confidential settlement agreement, and six cases where the defendant employer(s) ultimately prevailed. Because the FLSA only entitles prevailing plaintiffs to litigation cost awards, information about litigation costs was only available for the remaining 56 FLSA cases that ended in settlement agreements or court verdicts favoring the plaintiff employees.

[216] This is likely a conservative approach to estimate the total litigation costs for each FLSA lawsuit, as defendant employers tend to incur greater litigation costs than plaintiff employees because of, among other things, typically higher discovery costs.

[217] The median cost was $111,835 per lawsuit.

3. NPRM Comments on Benefits

Some commenters contended that the proposed salary level would not yield the benefits that a higher salary level would. They asserted that raising the salary level higher than the proposed level would result in less misclassification and less litigation. The law firm Winebrake & Santillo, LLC estimated that ''if the executive exemption carried a $50,000/year salary threshold, over 75% of the [lawsuits the firm litigated involving alleged misclassification under the executive exemption] would never have been filed.'' NELA provided an example of a misclassification case involving managers at a fast food chain earning $32,000-$40,000 whom a jury found had been misclassified, and stated that such litigation would have been unnecessary under a higher salary level such as the one in the 2016 final rule. EPI, a group of 14 State attorneys general and the Attorney General for the District of Columbia, and other commenters similarly stated that a higher salary level was necessary to further reduce the risk of employee misclassification and the costs of litigation.

While a higher salary level would likely result in fewer workers being misclassified as exempt, and potentially less litigation as a result, as explained above, the aim of reducing misclassification cannot be prioritized over the statutory text, which grounds an analysis of exemption status in the ''capacity'' in which someone is employed—*i.e.,* that employee's duties. The salary level test's limited purpose is therefore to screen out only those employees who are clearly nonexempt because they are not performing bona fide EAP duties.

Likewise, many commenters expressed concern that the proposed salary level is too low and thus does not do enough to address income inequality. Other commenters asserted that a higher salary level would create jobs and/or stimulate the economy. As explained in greater detail above, however, the Department declined to set a higher salary level because it believes that the salary level set in this final rule appropriately screens out obviously nonexempt workers and distinguishes between nonexempt and potentially exempt employees, without threatening to supplant the role of the duties test. Accordingly, the Department declines to change the salary level methodology in response to these comments.

vi. Sensitivity Analysis

This section includes estimated costs and transfers using either different assumptions or segments of the population. First, the Department presents bounds on transfer payments estimated using alternative assumptions. Second, the Department considers costs and transfers by region and by industry.

1. Bounds on Transfer Payments

Because the Department cannot predict employers' precise reactions to the final rule, the Department calculated bounds on the size of the estimated transfers from employers to workers. These bounds on transfers do not generate bounded estimates for costs.

For a reasonable upper bound on transfer payments, the Department assumed that all occasional overtime workers and half of regular overtime workers will receive the full overtime premium (*i.e.,* such workers will work the same number of hours but be paid 1.5 times their implicit initial hourly wage for all overtime hours) (Table 18). The full overtime premium model is a special case of the fixed-wage model where there is no change in hours. For the other half of regular overtime workers, the Department assumed in the upper-bound method that they will have their implicit hourly wage adjusted as predicted by the incomplete fixed-job model (wage rates fall and hours are reduced but total earnings continue to increase, as in the preferred method). In the preferred model, the Department assumed that only 50 percent of occasional overtime workers and no regular overtime workers will receive the full overtime premium.

The plausible lower-transfer bound also depends on whether employees work regular overtime or occasional overtime. For those who regularly work overtime hours and half of those who work occasional overtime, the Department assumes the employees' wages will fully adjust as predicted by the fixed-job model.[218] For the other half of employees with occasional overtime hours, the lower bound assumes they will be paid one and one-half times their implicit hourly wage for overtime hours worked (full overtime premium).

[218] The straight-time wage adjusts to a level that keeps weekly earnings constant when overtime hours are paid at 1.5 times the straight-time wage. In cases where adjusting the straight-time wage results in a wage less than the minimum wage, the straight-time wage is set to the minimum wage.

TABLE 18—SUMMARY OF THE ASSUMPTIONS USED TO CALCULATE THE LOWER ESTIMATE, PREFERRED ESTIMATE, AND UPPER ESTIMATE OF TRANSFERS

Lower transfer estimate	Preferred estimate	Upper transfer estimate
Occasional Overtime Workers (Type 2)		
50% fixed-job model 50% full overtime premium	50% incomplete fixed-job model 50% full overtime premium.	100% full overtime premium.
Regular Overtime Workers (Type 3)		
100% fixed-job model	100% incomplete fixed-job model	50% incomplete fixed-job model. 50% full overtime premium.

* Full overtime premium model: Regular rate of pay equals the implicit hourly wage prior to the regulation (with no adjustments); workers are paid 1.5 times this base wage for the same number of overtime hours worked prior to the regulation.
* Fixed-job model: Base wages are set at the higher of: (1) A rate such that total earnings and hours remain the same before and after the regulation; thus the base wage falls, and workers are paid 1.5 times the new base wage for overtime hours (the fixed-job model) or (2) the minimum wage.
* Incomplete fixed-job model: Regular rates of pay are partially adjusted to the wage implied by the fixed-job model.

The cost and transfer payment estimates associated with the bounds are presented in Table 19. Regulatory familiarization costs and adjustment costs do not vary across the scenarios. Managerial costs are lower under these alternative employer response assumptions because fewer workers' hours are adjusted by employers and thus managerial costs, which depend in part on the number of workers whose hours change, will be smaller.[219] Depending on how employers adjust the implicit regular hourly wage, estimated transfers may range from $233.7 million to $644.8 million, with the preferred estimate equal to $396.4 million.

TABLE 19—BOUNDS ON YEAR 1 COST AND TRANSFER PAYMENT ESTIMATES, YEAR 1

[Millions]

Cost/transfer	Lower transfer estimate	Preferred estimate	Upper transfer estimate
Direct employer costs	$413.5	$476.6	$422.9
Reg. familiarization	340.4	340.4	340.4
Adjustment costs	68.2	68.2	68.2
Managerial costs	9.8	134.4	27.7
Transfers	233.7	396.4	644.8

Note 1: Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.

2. Effects by Regions and Industries

This section presents estimates of the effects of this final rule by region and by industry. The Department compared the number of affected workers, costs, and transfers across the four Census Regions. The region with the largest number of affected workers will be the South (544,000). As a share of potentially affected workers in the region, the South has somewhat more affected workers relative to other regions (6.1 percent are affected compared with 4.1 to 4.4 percent in other regions). However, as a share of all workers in the region, the South will not be particularly affected relative to other regions (1.1 percent are affected compared with 0.7 to 0.9 percent in other regions).

TABLE 20—POTENTIALLY AFFECTED AND AFFECTED WORKERS, BY REGION, YEAR 1

Region	Workers subject to FLSA (millions)	Potentially affected workers (millions) [a]	Affected workers			
			Number (millions) [b]	Percent of total affected workers	Affected workers as a percent of potentially affected workers	Affected workers as a percent of all workers
All	139.4	25.6	1.257	100	4.9	0.9
Northeast	25.4	5.3	0.231	18.4	4.4	0.9
Midwest	30.6	5.2	0.229	18.2	4.4	0.7
South	50.9	8.9	0.544	43.2	6.1	1.1
West	32.6	6.1	0.253	20.2	4.1	0.8

Note: Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.
[a] EAP exempt workers who are white collar, salaried, not eligible for another (non-EAP) overtime exemption, and not in a named occupation.

[219] In the lower transfer estimate, managerial costs are for employees whose hours change because their hourly rate increased to the minimum wage.

[b] Currently EAP exempt workers who will be entitled to overtime protection under the updated earnings levels or whose weekly earnings will increase to the new earnings levels to remain exempt.

Total transfers in the first year were estimated to be $396.4 million (Table 21). As expected, the transfers in the South will be the largest portion because the largest number of affected workers will be in the South; however, transfers per affected worker will be the lowest in the South. Annual transfers per worker will be $255 in the South, and $317 to $436 in other regions.

TABLE 21—TRANSFERS BY REGION, YEAR 1

Region	Total change in earnings (millions)	Percent of total	Per affected worker
All	$396.4	100	$315.29
Northeast	73.3	18.5	317.35
Midwest	73.8	18.6	321.60
South	138.8	35.0	255.39
West	110.6	27.9	436.18

Note: Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.

Direct employer costs are composed of regulatory familiarization costs, adjustment costs, and managerial costs. The Department estimates that total direct employer costs will be the highest in the South ($208.3 million) and lowest in the Northeast ($100.4 million) (Table 22). Direct employer costs in each region, as a percentage of the total direct costs, will range from 18.5 percent in the Northeast to 38.4 percent in the South. These proportions are almost the same as the proportions of the total workforce in each region: 18.2 percent in the Northeast and 36.5 percent in the South.

TABLE 22—DIRECT EMPLOYER COSTS BY REGION, YEAR 1

Region	Regulatory familiarization	Adjustment	Managerial	Total direct costs
Costs (Millions)				
All	$340.4	$68.2	$134.4	$543.0
Northeast	65.7	12.5	22.2	100.4
Midwest	74.8	12.4	27.7	114.9
South	119.6	29.5	59.2	208.3
West	80.3	13.7	25.3	119.4
Percent of Total Costs by Region				
All	100.0	100.0	100.0	100.0
Northeast	19.3	18.4	16.5	18.5
Midwest	22.0	18.2	20.6	21.2
South	35.1	43.2	44.0	38.4
West	23.6	20.2	18.9	22.0

Note: Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.

Another way to compare the relative effects of this final rule by region is to consider the transfers and costs as a proportion of payroll and revenues (Table 23). Nationally, employer costs and transfers will be approximately 0.012 percent of payroll. By region, direct employer costs and transfers as a percent of payroll will be approximately the same (between 0.010 and 0.013 percent of payroll). Employer costs and transfers as a percent of revenue will be 0.002 percent nationally and in each region.

TABLE 23—ANNUAL TRANSFERS AND COSTS AS PERCENT OF PAYROLL AND OF REVENUE BY REGION, YEAR 1

Region	Payroll (billions)	Revenue (billions)	Costs and transfers	
			As percent of payroll	As percent of revenue
All	$7,867	$45,023	0.012	0.002
Northeast	1,733	9,048	0.010	0.002
Midwest	1,673	10,251	0.011	0.002
South	2,618	16,109	0.013	0.002

TABLE 23—ANNUAL TRANSFERS AND COSTS AS PERCENT OF PAYROLL AND OF REVENUE BY REGION, YEAR 1—Continued

Region	Payroll (billions)	Revenue (billions)	Costs and transfers	
			As percent of payroll	As percent of revenue
West	1,843	9,616	0.012	0.002

Notes: Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019. Payroll, revenue, costs, and transfers all exclude the federal government.

Sources: Private sector payroll and revenue data from 2012 SUSB. State and local payroll and revenue data from State and Local Government Finances Summary: FY2016. Inflated to 2018$ using GDP deflator.

In order to gauge the effect of the final rule on industries, the Department compared estimates of combined direct costs and transfers as a percent of payroll, profit, and revenue for the 13 major industry groups (Table 24).[220] This provides a common method of assessing the relative effects of the rule on different industries, and the magnitude of adjustments the rule may require on the part of enterprises in each industry. The relative costs and transfers expressed as a percentage of payroll are particularly useful measures of the relative size of adjustment faced by organizations in an industry because they benchmark against the cost category directly associated with the labor force. Measured in these terms, costs and transfers as a percent of payroll will be highest in agriculture, forestry, fishing, and hunting; leisure and hospitality; and other services. However, the magnitude of the relative shares will be small, representing less than 0.04 percent of payroll costs in all industries.

The Department also estimated transfers and costs as a percent of profits.[221] Benchmarking against profits is potentially helpful in the sense that it provides a measure of the final rule's effect against returns on investment. However, this metric must be interpreted carefully as it does not account for differences across industries in risk-adjusted rates of return, which are not readily available for this analysis. The ratio of costs and transfers to profits also does not reflect differences in the firm-level adjustment to changes in profits reflecting cross-industry variation in market structure.[222] Nonetheless, the magnitude of costs and transfers as a percentage of profits will be small, with total costs and transfers as a percent of profits will vary among industries, ranging from a low of 0.01 percent (financial activities and manufacturing) to a high of 0.18 percent (other services). However, because the share is not more than 0.2 percent, even for the industry with the largest impact, we believe this final rule will not disproportionately affect any industries.

Finally, the Department's estimates of transfers and costs as a percent of revenue by industry also indicated very small effects (Table 24) of less than 0.01 percent of revenues in any industry. The industry with the largest costs and transfers as a percent of revenue will be leisure and hospitality. However, the difference between this industry and the industry with the lowest costs and transfers as a percent of revenue (public administration) is only 0.008 percentage points. Table 24 illustrates that the differences in costs relative to revenues will be quite small across industry groupings.

TABLE 24—ANNUAL TRANSFERS, TOTAL COSTS, AND TRANSFERS AND COSTS AS PERCENT OF PAYROLL, REVENUE, AND PROFIT BY INDUSTRY, YEAR 1

Industry	Transfers (millions)	Direct costs (millions)	Costs and transfers		
			As percent of payroll	As percent of revenue	As percent of profit [a]
All	$396.3	$528.6	0.012	0.002	0.03
Agriculture, forestry, fishing, & hunting	1.5	1.4	0.038	0.007	0.16
Mining	2.0	2.1	0.005	0.001	0.02
Construction	20.1	37.4	0.017	0.003	0.10
Manufacturing	36.0	27.5	0.008	0.001	0.01
Wholesale & retail trade	64.5	97.2	0.017	0.001	0.04
Transportation & utilities	9.7	16.4	0.008	0.002	0.06
Information	22.8	13.5	0.011	0.002	0.03
Financial activities	38.6	60.4	0.013	0.002	0.01
Professional & business services	73.5	90.9	0.010	0.005	0.06
Education & health services	57.3	81.4	0.012	0.005	0.09
Leisure & hospitality	47.6	49.7	0.029	0.008	0.16
Other services	12.5	40.2	0.028	0.007	0.18

[220] Note that the totals in this table do not match the totals in other sections due to the exclusion of transfers to federal workers and costs to federal entities. Federal costs and transfers are excluded to be consistent with payroll and revenue which exclude the federal government.

[221] Internal Revenue Service. (2013). Corporation Income Tax Returns. Available at: *https://www.irs.gov/statistics/soi-tax-stats-corporation-complete-report*. Table 5 of the IRS report provides information on total receipts, net income, and deficits. The Department calculated the ratio of net income (column (7)) less any deficit (column (8)) to total receipts (column (3)) for all firms by major industry categories. Costs and transfers as a percent of revenues were divided by the profit to receipts ratios to calculate the costs and transfers as a percent of profit.

[222] In particular, a basic model of competitive product markets would predict that highly competitive industries with lower rates of return would adjust to increases in the marginal cost of labor arising from the rule through an overall, industry-level increase in prices and a reduction in quantity demanded based on the relative elasticities of supply and demand. Alternatively, more concentrated markets with higher rates of return would be more likely to adjust through some combination of price increases and profit reductions based on elasticities as well as interfirm pricing responses.

TABLE 24—ANNUAL TRANSFERS, TOTAL COSTS, AND TRANSFERS AND COSTS AS PERCENT OF PAYROLL, REVENUE, AND PROFIT BY INDUSTRY, YEAR 1—Continued

Industry	Transfers (millions)	Direct costs (millions)	Costs and transfers		
			As percent of payroll	As percent of revenue	As percent of profit [a]
Public administration	10.2	10.6	0.002	0.001	([b])

Notes: Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019. Payroll, revenue, costs, and transfers all exclude the federal government.

Sources: Private sector payroll and revenue data from 2012 Economic Census. State and local payroll and revenue data from State and Local Government Finances Summary: FY2016 are used for the Public Administration industry. Profit to revenue ratios calculated from 2012 Internal Revenue Service Corporation Income Tax Returns. Inflated to 2018$ using GDP deflator.

[a] Profit data based on corporations only.

[b] Profit is not applicable for public administration.

Although labor market conditions vary by Census Region and industry, the effects from updating the standard salary level and the HCE compensation level will not unduly affect any of the regions or industries. The proportion of total costs and transfers in each region will be fairly consistent with the proportion of total workers in each region. Additionally, although the shares will be larger for some firms and smaller for others, the average estimated costs and transfers from this final rule are very small relative to current payroll or current revenue—less than a tenth of a percent of payroll and less than one-hundredth of a percent of revenue in each region and in each industry.

vii. Regulatory Alternatives

As mentioned earlier, the Department considered a range of alternatives before selecting its methods for updating the standard salary level and the HCE compensation level (*see* § VI.C). As seen in Table 25, the Department has calculated the salary levels, the number of affected workers, and the associated costs and transfers for the alternative methods that the Department considered.

TABLE 25—UPDATED STANDARD SALARY AND HCE COMPENSATION LEVELS AND ALTERNATIVES, AFFECTED EAP WORKERS, COSTS, AND TRANSFERS, YEAR 1

Alternative	Salary level [a]	Affected EAP workers (1,000s)	Year 1 effects (millions)	
			Adj. & managerial costs [b]	Transfers
Standard Salary Level (Weekly)				
Alt. #1: No change	$455	0		
Alt. #2: Maintain average minimum wage protection since 2004 [b]	502	218	27.1	29.6
Alt. #3: 2004 Method, South (excluding Washington D.C., MD & VA) or Retail [c]	673	1,043	169.4	276.7
Final rule: 2004 method [c]	684	1,156	184.1	296.1
Alt. #4: Kantor long test [d]	724	1,552	247.4	406.1
Alt. #5: 2016 method [e]	976	4,345	732.9	1,325.8
HCE Compensation Level (Annually)				
HCE alt. #1: No change	100,000	0		
Final rule: 80th percentile of full-time salaried workers	107,432	102	18.4	100.3
HCE alt. #2: 90th percentile of full-time salaried workers	145,964	246	53.3	301.7

Note: Impacts estimated using pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.

[a] Regulatory familiarization costs are excluded because they do not vary significantly based on the selected values of the salary levels.

[b] When the $455 weekly threshold was established in 2004, the federal minimum wage was $5.15, so the salary threshold equated to minimum wage and overtime pay at time-and-one-half for hours over 40 for an employee working no more than 72.2 hours. That amount fell with increases in the minimum wage and is now 55.2 hours. The weighted average across the 15 years since the overtime threshold was last changed is 59.5 hours, and a threshold that would provide 59.5 hours of $7.25 minimum wage and overtime pay would be $502.

[c] Full-time salaried workers with various industry/region exclusions (excludes workers not subject to the FLSA, not subject to the salary level test, and in some workers in agriculture or transportation). Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.

[d] 10th percentile of likely exempt workers. Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.

[e] 40th percentile earnings of nonhourly full-time workers in the South Census region, provided by BLS. The salary level reflects the first automatic update that would have taken place under the 2016 final rule.

viii. Projections

1. Methodology

The Department projected affected workers, costs, and transfers forward for ten years. This involved several steps.

First, the Department calculated workers' projected earnings in future years. The wage growth rate is calculated as the compound annual growth rate in median wages using the historical CPS MORG data for occupation-industry categories from 2007 to 2017.[223] This is the annual

[223] To increase the number of observations, three years of data were pooled for each of the endpoint years. Specifically, data from 2006, 2007, and 2008 (converted to 2007 dollars) were used to calculate the 2007 median wage and data from 2016, 2017, and 2018 (converted to 2017 dollars) were used to calculate the 2017 median wage.

growth rate that when compounded (applied to the first year's wage, then to the resulting second year's wage, etc.) yields the last historical year's wage. In occupation-industry categories where the CPS MORG data had an insufficient number of observations to reliably calculate median wages, the Department used the growth rate in median wages calculated from BLS' Occupational Employment Statistics (OES).[224] Any remaining occupation-industry combinations without estimated median growth rates were assigned the median of the growth rates in median wages from the CPS MORG data for all industries and occupations. For projecting costs, we similarly projected wage rates for the human resource and managerial workers whose time is spent on these tasks.

Second, the Department compared workers' counter-factual earnings (*i.e.,* absent this final rule) to the earnings levels. If the counter-factual earnings are below the relevant level (*i.e.,* standard or HCE) then the worker is considered affected. In other words, in each year affected EAP workers were identified as those who would be exempt in Year 1 absent any change to the current regulations but have projected earnings in the future year that are less than the relevant salary level.

Third, sampling weights were adjusted to reflect employment growth. The employment growth rate is the compound annual growth rate based on the ten-year employment projection from BLS' National Employment Matrix (NEM) for 2016 to 2026 within an occupation-industry category.

Adjusted hours for workers affected in Year 1 were re-estimated in Year 2 using a long-run elasticity of labor demand of -0.4.[225] For workers newly affected in Year 2 through Year 10, employers' wage and hour adjustments are estimated in that year, as described in section VI.D.iv, except the long-run elasticity of labor demand of -0.4 is used. Employer adjustments are made in the first year the worker is affected and then applied to all future years in which the worker continues to be affected (unless the worker switches to a Type 4 worker). Workers' earnings in predicted years are earnings post employer adjustments, with overtime pay, and with ongoing wage growth based on historical growth rates (as described above).

2. Estimated Projections

The Department estimated that the final rule will affect 1.3 million EAP workers in Year 1 and 0.9 million workers in Year 10 (Table 26). The projected number of affected workers includes workers who were not EAP exempt in the base year but would have become exempt in the absence of this final rule in Years 2 through 10. For example, a worker who passes the standard duties test may earn less than $455 in Year 1 but between $455 and the new salary level in subsequent years; such a worker will be counted as an affected worker.

The Department quantified three types of direct employer costs in the ten-year projections: (1) Regulatory familiarization costs; (2) adjustment costs; and (3) managerial costs. Regulatory familiarization costs only occur in Year 1. Although start-up firms must still become familiar with the FLSA following Year 1, the difference between the time necessary for familiarization with the current part 541 regulations and the regulations as modified by the final rule is essentially zero. Therefore, projected regulatory familiarization costs for new entrants over the next nine years are zero.

Adjustment costs will occur in any year in which workers are newly affected. After Year 1, these costs will be relatively small since the majority of workers will be affected in Year 1. Management costs will recur each year for all affected EAP workers whose hours are adjusted. However, managerial costs generally decrease over time as the number of affected EAP workers decreases. The Department estimated that Year 1 managerial costs will be $134.4 million; by Year 10 these costs decline to $94.5 million.

The Department projected two types of transfers from employers to employees associated with workers affected by the regulation. Transfers due to the minimum wage provision will be $75.4 million in Year 1 and will fall to $26.1 million in Year 10 as increased earnings over time move workers' implicit rate of pay above the minimum wage.[226] Transfers due to overtime pay also decrease because wage growth raises workers' earnings above the earnings thresholds over time thus decreasing the number of affected workers. Thus, transfers due to the overtime pay provision are estimated to decrease from $321.0 million in Year 1 to $221.3 million in Year 10. Projected costs and transfers were deflated to 2019 dollars using the Congressional Budget Office's projections for the CPI–U.[227]

TABLE 26—PROJECTED COSTS AND TRANSFERS, STANDARD AND HCE SALARY LEVELS

Year (year #)	Affected EAP workers (millions)	Costs				Transfers		
		Reg. fam.	Adjustment [a]	Managerial	Total	Due to MW	Due to OT	Total
		(Millions 2019$)						
Year:								
Year 1	1.3	$340.4	$68.2	$134.4	$543.0	$75.4	$321.0	$396.4
Year 2	1.2	0.0	2.0	132.3	134.3	42.8	264.9	307.7
Year 3	1.1	0.0	1.9	126.7	128.5	37.4	266.5	303.9
Year 4	1.1	0.0	2.7	121.4	124.1	33.2	248.7	281.9
Year 5	1.1	0.0	3.1	116.8	119.9	31.2	269.0	300.1
Year 6	1.0	0.0	2.9	110.7	113.6	29.5	257.3	286.8
Year 7	1.0	0.0	3.2	103.9	107.1	29.5	236.9	266.5
Year 8	0.9	0.0	3.8	99.8	103.6	28.0	241.8	269.7
Year 9	0.9	0.0	4.1	95.3	99.4	26.4	235.0	261.4
Year 10	0.9	0.0	4.6	94.5	99.1	26.1	221.3	247.4
Annualized value:								

[224] To lessen small sample bias, this rate was only calculated using CPS MORG data when these data contained at least 30 observations in each period.

[225] This elasticity estimate is based on the Department's analysis of the following paper: Lichter, A., Peichl, A. & Siegloch, A. (2014). The Own-Wage Elasticity of Labor Demand: A Meta-Regression Analysis. IZA DP No. 7958.

[226] Increases in minimum wages were not projected. If state or federal minimum wages increase during the projected timeframe then projected minimum wage transfers may be underestimated.

[227] Congressional Budget Office. 2018. The Budget and Economic Outlook: 2018 To 2028. *See https://www.cbo.gov/publication/53651.*

TABLE 26—PROJECTED COSTS AND TRANSFERS, STANDARD AND HCE SALARY LEVELS—Continued

Year (year #)	Affected EAP workers (millions)	Costs				Transfers		
		Reg. fam.	Adjustment [a]	Managerial	Total	Due to MW	Due to OT	Total
		(Millions 2019$)						
3% real discount rate		38.7	10.5	114.8	164.0	36.9	258.1	295.0
7% real discount rate		45.3	11.7	116.3	173.3	38.1	260.6	298.8

[a] Adjustment costs occur in all years when there are newly affected workers.

Table 26 also summarizes annualized costs and transfers over the ten-year projection period, using 3 percent and 7 percent real discount rates. The Department estimated that total direct employer costs have an annualized value of $173.3 million per year over ten years when using a 7 percent real discount rate. The annualized value of total transfers was estimated to equal $298.8 million.

ix. Alternative Regulatory Baseline, Including Calculation of Cost Savings Under Executive Order 13771

Other portions of this regulatory impact analysis contain estimates of the impacts of this final rule relative to the 2004 final rule, which is the rule that the Department is currently enforcing. However, OMB Circular A–4 states that multiple regulatory baselines may be analytically relevant. In this case, a second informative baseline is the 2016 final rule, which is currently in the Code of Federal Regulations (CFR).[228] Moreover, for purposes of determining whether this rule is deregulatory under E.O. 13771, the economic impacts should be compared to what is currently published in the CFR. As such, most of this section presents an estimate of the cost savings of this final rule relative to the 2016 rule, and in addition to estimating annualized cost savings for the final rule using a 10-year time horizon, we also estimated annualized cost savings in perpetuity in accordance with E.O. 13771 accounting standards. This perpetual time horizon makes it especially important to avoid overemphasizing short-run compensation stickiness in the estimation approach; as such, the quantitative estimates will incorporate a relatively high compensation adjustment, the 80 percent derived from Barkume (2010), which assumes an initial overtime premium is paid, rather than the adjustment reflected in the estimates that are elsewhere identified as primary.[229] Later in this section, the Department presents transfer and benefits estimates from the analysis accompanying the 2016 final rule—values that are also relevant to this second regulatory baseline.

To ensure that the estimated costs of the 2016 final rule can be directly and appropriately compared with the costs estimated for this final rule, the Department started with the analytic model for this final rule and replaced this final rule's salary and compensation thresholds with the thresholds that would be required by the 2016 final rule, including that rule's provision to automatically update the salary level on a triennial basis. The Department assumed that initial regulatory familiarization costs would be identical under adoption of either this final rule or the 2016 final rule, because the same number of employers would be potentially affected in Year 1. In addition, implementation of the 2016 rule would have resulted in the first automatic update occurring in 2020, and therefore the Department used that value to represent Year 1 of the 2016 rule for 2020. Similarly, automatic updates in Years 7 and 10 from the 2016 final rule become the second and third automatic updates in the comparison. Finally, the Department projected earnings levels for year 13 of the 2016 rule to use as the final automatic update in the comparison. Therefore, the *only* differences in estimated costs presented here between the 2016 final rule and this final rule are attributable to the difference in earnings thresholds and the effects of the 2016 final rule's automatic updating mechanism.

TABLE 27—WEEKLY EARNINGS THRESHOLDS USED IN COMPARISON OF 2016 AND 2019 FINAL RULES

Year	2016 Final rule [a]		2019 Final rule	
	Standard salary threshold	HCE compensation threshold	Standard salary threshold	HCE compensation threshold
2020 [b]	$984	$2,837	$684	$2,066
2023	1,049	3,080	684	2,066
2026	1,118	3,345	684	2,066
2029	1,192	3,632	684	2,066

[a] Earnings levels in 2020, 2023, and 2026 are the projected salary levels as reported in the 2016 final rule. The 2029 levels were calculated using the same growth rate as was used in the 2016 final rule to estimate the projected levels in 2023 and 2026; the growth rate of the 40th percentile in the South from FY2005 to FY2015.

[b] Standard salary threshold reflects the 2016 final rule projection for 2020. If the earnings levels were recalculated using current data (2018Q3 through 2019Q2) they would be $976 and $2,888.

However, this approach means that the estimated costs presented here for the 2016 final rule are not directly comparable to those published in the **Federal Register** (81 FR 32391). The differences between the previously

[228] 29 CFR part 541.

[229] As noted previously, even Barkume's result was estimated for a population that included hourly workers. The fixed-job model is probably more likely to hold for salaried workers than for hourly workers because salaried workers directly observe their weekly total earnings, not their implicit equivalent hourly wage; therefore, applying the partial adjustment to the fixed-job model as estimated by these studies may overestimate the transfers between employers and salaried workers and other associated impacts.

published 2016 cost estimates and those presented here are primarily due to: Earnings levels associated with 2020; an increase in the number of establishments that would incur regulatory familiarization costs to account for economic growth between 2012 (estimates for the 2016 final rule were based on 2012 SUSB data) and 2016 (estimates for this final rule are based on 2016 SUSB data); the use of more recent CPS MORG data (the 2016 final rule used pooled CPS data for 2013 through 2015 inflated to represent FY 2017); the use of the Barkume-derived 80 percent compensation adjustment estimate, rather than the estimate that averages Barkume's findings with Trejo's; an increase in the wage rates used to value staff time spent on regulatory familiarization, adjustment, and monitoring; an increase in the managerial time estimate from 5 to 10 minutes; incorporating a 17 percent overhead rate in those wage rates; and minor improvements to the model.[230]

The estimated total perpetual annualized costs of the 2016 rule are $676.9 million using a 7 percent discount rate. For purposes of this E.O. 13771 analysis, the estimated total perpetual annualized costs of this final rule are $142.0 million using a 7 percent discount rate. The Department then subtracted direct regulatory costs expected to have been incurred under the 2016 final rule from the direct costs estimated under this final rule. Direct employer costs of this final rule are estimated to be, on average, $534.8 million lower per year in perpetuity than the 2016 final rule (using a 7 percent discount rate).

The cost savings from this final rule are primarily attributable to two factors. First, a lower standard salary level will result in fewer affected workers in any given year. If fewer workers are affected, then management must consider and make earnings adjustments for fewer employees, and must monitor hours worked for fewer employees. Second, this analysis does not incorporate automatic updating whereas the 2016 final rule incorporated a triennial automatic updating mechanism. Therefore, regulatory familiarization costs are now only incurred in Year 1 and adjustment costs are primarily incurred in Year 1. Additionally, managerial costs now gradually decrease over time rather than increasing every three years.

In the 2016 final rule, the Department estimated average annualized transfers of $1,189.1 million over a ten-year period using a discount rate of 7 percent. The Department also estimated that avoided litigation costs resulting from the rule could total approximately $31.2 million per year.[231] The Department includes these values here for reference.

EPI compared the estimated number of affected workers under the 2016 final rule to the estimate in the proposed rule, and commented that the Department's estimate ''that 2.8 million fewer workers will be impacted under its proposal than under the 2016 rule . . . is a vast underestimate.'' The alleged underestimate of affected workers resulted in part from EPI comparing the estimated impacts of the 2016 final rule in 2020 (*i.e.,* Year 4 of the 2016 rule) with the 2020 impacts of this rule (*i.e.,* Year 1 of this final rule).[232] Thus, EPI used the earnings levels associated with the first automatic update (which it calculated to be $51,053 for the standard salary level) for the 2016 rule. The Department has adjusted the calculation to use the 2016 final rule's predicted salary levels for 2020 when calculating Year 1 impacts.[233]

EPI also contended that the Department underestimated the difference between the number of workers affected by the 2016 final rule and the number affected by the NPRM because the Department's analysis ''[left] out an entire group of workers who would be affected by the rule— those who will no longer get *strengthened* protections.'' The majority of the difference between EPI's estimate of the number of affected workers and the NPRM's estimate is due to EPI including workers whose overtime protections were strengthened in the estimate of affected workers. However, in both this rule and the 2016 final rule, workers with strengthened overtime protections—those who fail the standard duties test and earn at least $455 but below the new standard salary level— are included in the description of affected workers but not in the official calculation of affected workers. This is because workers with strengthened protections are not directly impacted by changes in the regulations; they only directly benefit from the rulemaking if they are currently misclassified as exempt. Even so, the Department notes that this final rule will strengthen overtime protections for 4.1 million workers who currently fail the standard duties test and now will also earn below the standard salary level.

VII. Final Regulatory Flexibility Analysis (FRFA)

The Regulatory Flexibility Act of 1980 (RFA) as amended by the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA), hereafter jointly referred to as the RFA, requires that an agency prepare an initial regulatory flexibility analysis (IRFA) when proposing, and a final regulatory flexibility analysis (FRFA) when issuing, regulations that will have a significant economic impact on a substantial number of small entities. The agency is also required to respond to public comment on the NPRM.[234] The Chief Counsel for Advocacy of the Small Business Administration submitted public comments on the NPRM which are addressed below.

A. Objectives of, and Need for, the Final Rule

The FLSA requires covered employers to: (1) Pay employees who are covered and not exempt from the Act's requirements not less than the Federal minimum wage for all hours worked and overtime premium pay at a rate of not less than one and one-half times the employee's regular rate of pay for all hours worked over 40 in a workweek, and (2) make, keep, and preserve records of the persons employed by the employer and of the wages, hours, and other conditions and practices of employment.

The FLSA provides a number of exemptions from the Act's minimum wage and overtime pay provisions, including one for bona fide executive, administrative, and professional (EAP) employees. The exemption applies to employees employed in a bona fide executive, administrative, or professional capacity and for outside sales employees, as those terms are ''defined and delimited'' by the Department. 29 U.S.C. 213(a)(1). The Department's regulations implementing these ''white collar'' exemptions are codified at 29 CFR part 541.

For an employer to exclude an employee from minimum wage and overtime protection pursuant to the EAP exemption, the employee generally must

[230] As previously discussed, one such improvement is the Department's application of conditional probabilities to estimate the number of HCE workers. *See supra* note 160.

[231] In this final rule, the Department has revised (from the 2016 rule) how it calculates avoided litigation costs so the number referenced here for the 2016 final rule is not directly comparable to the calculation of reduced litigation costs for this final rule.

[232] *See https://www.epi.org/files/pdf/165984.pdf,* at 7.

[233] The Department also notes there are a variety of reasons for the discrepancy between the Department's and EPI's calculations, including use of different data and methodological differences.

[234] *See* 5 U.S.C. 604.

meet three criteria: (1) The employee must be paid a predetermined and fixed salary that is not subject to reduction because of variations in the quality or quantity of work performed (the ''salary basis test''); (2) the amount of salary paid must meet a minimum specified amount (the ''salary level test''); and (3) the employee's job duties must primarily involve executive, administrative, or professional duties as defined by the regulations (the ''duties test''). The salary level requirement was created to identify the dividing line distinguishing workers who may be performing exempt duties from the nonexempt workers whom Congress intended to be protected by the FLSA's minimum wage and overtime provisions.

The Department has periodically updated the regulations governing these tests since the FLSA's enactment in 1938. The Department is currently enforcing the 2004 final rule, which, among other revisions, created the standard duties test and paired it with a salary level test of $455 per week. The 2004 final rule also created a new ''highly compensated'' test for exemption. Under this test, employees who are paid total annual compensation of at least $100,000 (which must include at least $455 per week paid on a salary or fee basis) are exempt from the FLSA's overtime requirements if they customarily and regularly perform at least one of the duties or responsibilities of an exempt EAP employee identified in the standard tests for exemption.[235]

The Department's primary objective in this rulemaking is to ensure that the revised salary levels will continue to provide a useful and effective test for exemption. The premise behind the standard salary level is to be an appropriate dividing line between employees who are nonexempt and employees who may be performing exempt duties. The threshold essentially screens out obviously nonexempt employees whom Congress intended to be protected by the FLSA's minimum wage and overtime provisions. If left unchanged, the effectiveness of the salary level test as a means to help determine exempt status diminishes as nonexempt employee wages increase over time.

Employees who meet the requirements of part 541 are excluded from the Act's minimum wage and overtime pay protections. As a result, employees may work any number of hours in the workweek and not be subject to the FLSA's overtime pay requirements. Some state laws have stricter exemption standards than those described above. The FLSA does not preempt any such stricter state standards. If a state law establishes a higher standard than the provisions of the FLSA, the higher standard applies as a matter of state law in that specific state.[236]

To restore the function of the standard salary level and the HCE total compensation requirements as appropriate bright-line tests between overtime-protected employees and those who may be bona fide EAP employees, the Department is increasing the minimum salary level necessary for exemption from the FLSA's minimum wage and overtime requirements as an EAP employee from $455 to $684 a week for the standard salary test, and from $100,000 to $107,432 per year for the HCE test.

B. The Agency's Response to Public Comments

Small business commenters expressed concerns with the Department's estimates of the proposed rule's costs and other impacts. These concerns are acknowledged and addressed in sections VI.d.iii and VI.d.iv, which we incorporate herein.

C. Comment by the Chief Counsel for Advocacy of the Small Business Administration

SBA's Office of Advocacy (SBA Advocacy) generally supported the Department's proposal. SBA Advocacy's comment was based largely on feedback received from small businesses, many of whom told SBA Advocacy that the higher threshold in the 2016 final rule ($47,476) would have been disruptive and costly to small businesses. In its roundtables on the 2019 rulemaking, in contrast, SBA Advocacy heard that most small businesses would only have a few affected employees, and could absorb the costs from this rulemaking. SBA Advocacy listed a few recommendations for the Department to consider. Several of these recommendations (and related issues raised by other commenters) are also addressed elsewhere in this final rule.

SBA Advocacy recommended an adjustment to the calculation of the standard salary level. It indicated that some small businesses recommended that the Department ''adopt a narrower Census definition for areas with the lowest wages in the south when calculating and adjusting the new minimum salary threshold.'' SBA Advocacy, along with other commenters, specifically recommended that the Department ''focus on [a] more narrow geographic area like the East-South Central Census [Division] (which includes Alabama, Kentucky, Mississippi, and Tennessee) when adjusting the national wages; or provide more flexibility for these areas.'' The Department evaluated an alternative that eliminates higher-wage areas (District of Columbia, Maryland, and Virginia) from the data set used to determine the salary level (see Sections VI.D.vii and IV.A.v.). As previously discussed, the Department ultimately decided not to adopt this alternative, because it believes that using the entire South Census Region and the retail industry nationwide results in an appropriate nationwide salary level that is based on a low-wage region but can still serve as a meaningful dividing line in higher-wage regions. Using the entire South is also consistent with the methodology used in the 2004 final rule.

SBA Advocacy and a few other commenters also asserted that the Department underestimated small business compliance costs. SBA Advocacy stated that small businesses disagreed with the Department's estimate that, on average, establishments (including small businesses) will have a one-hour burden for rule familiarization, a 1.25-hour burden per affected worker in adjustment costs, and a 5-minute burden per worker per week for scheduling and monitoring. SBA Advocacy stated that small businesses have told them ''that it may take . . . many hours and several weeks to understand and implement this rule,'' and that ''[m]any small businesses spend a disproportionately higher amount of time and money on outside compliance staff.'' As discussed in more detail above, however, the Department believes that its estimates of time for rule familiarization and adjustment costs are appropriate, particularly given that the final rule is limited in scope and that most small businesses are already likely familiar with their responsibilities under the part 541 regulations. Additionally, these estimates represent an average of all establishments, some of which will spend little time on these activities and some of whom will spend more time than the average. However, the Department acknowledges that the prior 5 minutes per newly nonexempt overtime worker may be low and has doubled this estimate to 10 minutes.

Regarding the proposed transfer calculations, SBA Advocacy took issue with the Department's estimates that affected small business establishments would have, on average, $422 to $3,187

[235] § 541.601.

[236] *See* 29 U.S.C. 218(a).

in additional payroll costs in the first year (based on the proposed rule). Rather, SBA Advocacy stated that ''[s]mall businesses have told Advocacy that their payroll costs will be in the thousands of dollars.'' This comment, however, does not explain what methodological approach the Department should use to estimate transfers, or how much, if at all, the Department's approach underestimated such transfers. Therefore, the Department concludes that this comment does not provide a sufficient basis for changing its transfer calculation methodology.

D. Description of the Number of Small Entities to Which the Final Rule Will Apply

i. Definition of Small Entity

The RFA defines a ''small entity'' as a (1) small not-for-profit organization, (2) small governmental jurisdiction, or (3) small business. The Department used the entity size standards defined by SBA, in effect as of October 1, 2017, to classify entities as small.[237] SBA establishes separate standards for individual 6-digit NAICS industry codes, and standard cutoffs are typically based on either the average number of employees, or the average annual receipts. For example, small businesses are generally defined as having fewer than 500, 1,000, or 1,250 employees in manufacturing industries and less than $7.5 million in average annual receipts for nonmanufacturing industries. However, some exceptions do exist, the most notable being that depository institutions (including credit unions, commercial banks, and non-commercial banks) are classified by total assets (small defined as less than $550 million in assets). Small governmental jurisdictions are another noteworthy exception. They are defined as the governments of cities, counties, towns, townships, villages, school districts, or special districts with populations of less than 50,000 people.[238]

Parameters that are used in the small business cost analysis are provided in Table 28.

TABLE 28—OVERVIEW OF PARAMETERS USED FOR COSTS TO SMALL BUSINESSES

Small business costs	Cost
Direct and Payroll Costs	
Average total cost per affected entity [a]	$3,656.
Range of total costs per affected entity [a]	$1,678–$31,118.
Average percent of revenue per affected entity [a]	0.15%.
Average percent of payroll per affected entity [a]	0.81%.
Average percent of small business profit	0.05%.
Direct Costs	
Regulatory familiarization:	
Time (first year)	1 hour per establishment.
Hourly wage	$43.38.
Adjustment:	
Time (first year affected)	75 minutes per newly affected worker.
Hourly wage	$43.38.
Managerial:	
Time (weekly)	10 minutes per affected worker.
Hourly wage	$50.92.
Payroll Increases	
Average payroll increase per affected entity [a]	$2,393.
Range of payroll increases per affected entity [a]	$0–$26,943.

[a] Using the methodology where all employees at an affected small firm are affected. This assumption generates upper-end estimates. Lower-end cost estimates are significantly smaller.

ii. Data Sources and Methods

The Department obtained data from several sources to determine the number of small entities and employment in these entities for each industry. However, the Statistics of U.S. Businesses (SUSB) was used for most industries. Industries for which the Department used alternative sources include credit unions,[239] commercial banks and savings institutions,[240] agriculture,[241] and public administration.[242] Unless otherwise noted, the Department used the latest available data in each case, so data years differ between sources.

For each industry, the SUSB 2012 data tabulates total employment, establishment, and firm counts by both enterprise employment size (*e.g.,* 0–4 employees, 5–9 employees) and receipt size (*e.g.,* less than $100,000, $100,000–$499,999).[243] The Department combined these categories with the SBA size standards to estimate the proportion of establishments and employees in each industry that are considered small or employed by a small entity, respectively. The general

[237] *See https://www.sba.gov/sites/default/files/files/Size_Standards_Table_2017.pdf.*

[238] *See http://www.sba.gov/advocacy/regulatory-flexibility-act* for details.

[239] National Credit Union Association. (2012). 2012 Year End Statistics for Federally Insured Credit Unions. Available at: *https://www.cuna.org/uploadedFiles/Global/About_Credit_Unions/NationalProfile-M18-Bank.pdf.*

[240] Federal Depository Insurance Corporation. (2018). Statistics on Depository Institutions—Compare Banks. Available at: *https://www5.fdic.gov/SDI/index.asp.* Data are from 3/31/18 for employment and from 6/30/2017 for share of firms and establishments that are ''small.''

[241] United States Department of Agriculture. (2019). 2017 Census of Agriculture: United States Summary and State Data: Volume 1, Geographic Area Series, Part 51. Available at: *https://www.nass.usda.gov/Publications/AgCensus/2017/Full_Report/Volume_1,_Chapter_1_US/usv1.pdf.*

[242] Census of Governments. 2017. Available at: *https://www.census.gov/data/tables/2017/econ/gus/2017-governments.html.*

[243] The SUSB defines employment as of March 12th.

methodological approach was to classify all establishments or employees in categories below the SBA cutoff as in ''small entity'' employment.[244] If a cutoff fell in the middle of a defined category, a uniform distribution of employees across that bracket was assumed to determine what proportion should be classified as small. The Department assumed that the small entity share of credit card issuing and other depository credit intermediation institutions (which were not separately represented in FDIC asset data), is similar to that of commercial banking and savings institutions. The estimated share of employment in small entities was applied to the CPS data to estimate the number of affected workers in small entities. Similarly, the estimated share of establishments that are small was applied to the most recent SUSB data available (2016) to determine the number of small entities.

The Department also estimated the number of small establishments by employer type (nonprofit, for-profit, government). The calculation of the number of establishments by employer type is similar to the calculation of the number of establishments by industry. However, instead of using SUSB data by industry, the Department used SUSB data by Legal Form of Organization for nonprofit and for-profit establishments, and data from the 2012 Census of Governments for small governments. The 2012 Census of Governments report includes a breakdown of state and local governments by the population of their underlying jurisdiction, allowing us to estimate the number of governments that are small. The estimated share of establishments that are small was applied to the 2016 SUSB data available and the estimated share of governments that are small was applied to the 2017 Census of Governments.

iii. Number of Small Entities and Employees

Table 29 presents the estimated number of establishments and small establishments in the U.S. (hereafter, the terms ''establishment'' and ''entity'' are used interchangeably and are considered equivalent for the purposes of this FRFA).[245] Based on the methodology described above, the Department found that of the 7.8 million establishments relevant to this analysis, 81 percent (6.3 million) are small by SBA standards. These small establishments employ about 53.1 million workers, about 37 percent of workers employed by all establishments (excluding self-employed, unpaid workers, and members of the armed forces), and account for roughly 36 percent of total payroll ($2.9 trillion of $8.0 trillion).[246]

TABLE 29—NUMBER OF ESTABLISHMENTS AND EMPLOYEES BY SBA SIZE STANDARDS, BY INDUSTRY AND EMPLOYER TYPE

Industry/employer type	Establishments (1,000s)		Workers (1,000s) [a]		Annual payroll (billions)	
	Total	Small	Total	Small business employed	Total	Small
Total	7,847.9	6,345.4	143,184.6	53,058.6	$7,976.2	$2,868.0
Industry [b]						
Agriculture	9.3	8.6	(c)	(c)	(c)	(c)
Forest., log., fish., hunt., and trap	13.3	12.9	(c)	(c)	(c)	(c)
Mining	27.2	22.0	(c)	(c)	(c)	(c)
Construction	696.7	676.9	8,525.6	5,482.7	478.8	309.5
Nonmetallic mineral prod. manuf	15.0	11.5	(c)	(c)	(c)	(c)
Prim. metals and fab. metal prod	59.4	55.8	1,652.6	1,004.7	91.6	54.7
Machinery manufacturing	23.5	21.5	1,240.7	673.2	79.9	44.0
Computer and elect. prod. manuf	12.4	11.0	1,173.5	552.2	109.9	53.5
Electrical equip., appliance manuf	5.7	4.9	(c)	(c)	(c)	(c)
Transportation equip. manuf	11.7	10.1	2,616.6	728.6	183.3	47.0
Wood products	14.3	13.1	(c)	(c)	(c)	(c)
Furniture and fixtures manuf	15.0	14.6	(c)	(c)	(c)	(c)
Misc. and not spec. manuf	26.0	25.1	1,512.1	888.6	92.9	53.8
Food manufacturing	27.1	23.9	1,809.0	829.3	81.2	35.9
Beverage and tobacco products	8.5	7.6	(c)	(c)	(c)	(c)
Textile, app., and leather manuf	15.6	15.2	575.8	390.3	26.0	17.5
Paper and printing	29.6	27.6	871.7	464.6	49.5	25.3
Petroleum and coal prod. manuf	2.2	1.2	(c)	(c)	(c)	(c)
Chemical manufacturing	13.5	10.7	1,423.2	553.8	121.0	45.4
Plastics and rubber products	12.1	10.1	(c)	(c)	(c)	(c)
Wholesale trade	412.5	328.3	3,440.5	1,583.3	216.4	98.3
Retail trade	1,069.1	688.8	15,694.5	5,398.1	617.8	234.8
Transport. and warehousing	231.0	183.8	6,355.2	1,740.6	329.9	84.4
Utilities	18.2	7.8	1,391.6	264.2	110.6	20.3
Publishing ind. (ex. internet)	27.5	21.2	(c)	(c)	(c)	(c)
Motion picture and sound recording	25.5	22.3	(c)	(c)	(c)	(c)
Broadcasting (except internet)	8.3	4.6	554.0	129.4	39.2	8.6
Internet publishing and broadcasting	8.1	6.8	(c)	(c)	(c)	(c)
Telecommunications	59.2	13.3	(c)	(c)	(c)	(c)

[244] The Department's estimates of the numbers of affected small entities and affected workers who are employees of small entities are likely overestimates as the Department had no credible way to estimate which enterprises with annual revenues below $500,000 also did not engage in interstate commerce.

[245] SUSB reports data by ''enterprise'' size designations (a business organization consisting of one or more domestic establishments that were specified under common ownership or control). However, the number of enterprises is not reported for the size designations. Instead, SUSB reports the number of ''establishments'' (individual plants, regardless of ownership) and ''firms'' (a collection of establishments with a single owner within a given state and industry) associated with enterprises size categories. Therefore, numbers in this analysis are for the number of establishments associated with small enterprises, which may exceed the number of small enterprises. We based the analysis on the number of establishments rather than firms for a more conservative estimate (potential overestimate) of the number of small businesses.

[246] Since information is not available on employer size in the CPS MORG, respondents were randomly assigned as working in a small business based on the SUSB probability of employment in a small business by detailed Census industry. Annual payroll was estimated based on the CPS weekly earnings of workers by industry size.

TABLE 29—NUMBER OF ESTABLISHMENTS AND EMPLOYEES BY SBA SIZE STANDARDS, BY INDUSTRY AND EMPLOYER TYPE—Continued

Industry/employer type	Establishments (1,000s)		Workers (1,000s) [a]		Annual payroll (billions)	
	Total	Small	Total	Small business employed	Total	Small
Internet serv. providers and data	13.6	9.0	([c])	([c])	([c])	([c])
Other information services	4.2	3.6	([c])	([c])	([c])	([c])
Finance	295.5	129.8	4,506.3	847.0	374.8	70.7
Insurance	181.5	141.7	2,746.7	722.0	197.0	51.8
Real estate	336.8	286.4	2,091.1	1,274.7	126.5	77.5
Rental and leasing services	53.7	26.7	([c])	([c])	([c])	([c])
Professional and technical services	903.5	819.1	10,196.2	4,770.7	897.3	414.2
Management of companies and enterprises	55.4	34.1	([c])	([c])	([c])	([c])
Admin. and support services	384.9	328.8	5,080.7	2,309.8	210.7	87.7
Waste manag. and remed. Services	24.6	18.4	([c])	([c])	([c])	([c])
Educational services	103.4	90.6	14,196.6	3,089.0	793.8	162.1
Hospitals	7.1	1.7	([c])	([c])	([c])	([c])
Health care services, except hospitals	700.5	575.8	10,074.6	4,787.1	496.9	236.3
Social assistance	182.9	149.0	3,040.0	1,703.7	113.2	60.5
Arts, entertainment, and recreation	137.2	126.3	2,760.6	1,394.5	108.9	54.4
Accommodation	66.8	55.8	1,475.8	566.4	55.6	21.1
Food services and drinking places	636.7	500.7	8,946.1	2,422.7	240.4	65.4
Repair and maintenance	214.8	199.8	1,614.1	1,214.7	72.9	53.9
Personal and laundry services	230.3	201.6	1,763.1	1,300.1	57.1	41.6
Membership associations & organizations	309.2	298.3	2,104.1	1,545.8	112.2	80.9
Private households	([d])	([d])	([c])	([c])	([c])	([c])
Public administration [e]	90.1	72.8	7,527.9	685.8	499.4	40.1
Employer Type						
Nonprofit, private	584.0	504.6	10,190.1	4,170.3	586.5	216.4
For profit, private	7,173.8	5,753.9	111,050.8	46,579.0	6,080.5	2,525.3
Government (state and local)	90.1	72.9	18,078.8	2,309.4	1,020.2	126.3

Note: Establishment data are from the Survey of U.S. Businesses 2016; worker and payroll data from pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.

[a] Excludes the self-employed and unpaid workers.

[b] Summation across industries may not add to the totals reported due to suppressed values and some establishments not reporting an industry.

[c] Data not displayed because sample size of affected workers in small establishments is less than 10 due to reliability concerns.

[d] SUSB does not provide information on private households.

[e] Establishment number represents the total number of governments, including state and local. Data from Census of Governments, 2017.

As discussed in section VI.B.iii, estimates of workers subject to the FLSA do not exclude workers employed by enterprises that do not meet the enterprise coverage requirements because there is no data set that would adequately inform an estimate of the size of this worker population. Although not excluding such workers only affects a small percentage of workers generally, it may have a larger effect (and result in a larger overestimate) for non-profits, because revenue from charitable activities is not included when determining enterprise coverage.

iv. Number of Affected Small Entities and Employees

To estimate the probability that an exempt EAP worker in the CPS data is employed by a small establishment, the Department assumed this probability is equal to the proportion of all workers employed by small establishments in the corresponding industry. That is, if 50 percent of workers in an industry are employed in small entities, then on average small entities are expected to employ 1 out of every 2 exempt EAP workers in this industry.[247] The Department applied these probabilities to the population of exempt EAP workers to find the number of workers (total exempt EAP workers and total affected by the rule) that small entities employ. No data are available to determine whether small businesses (or small businesses in specific industries) are more or less likely than non-small businesses to employ exempt EAP workers or affected EAP workers. Therefore, the best assumption available is to assign the same rates to all small and non-small businesses.[248] [249]

[247] The Department used CPS microdata to estimate the number of affected workers. This was done individually for each observation in the relevant sample by randomly assigning them a small business status based on the best available estimate of the probability of a worker to be employed in a small business in their respective industry (3-digit Census codes). While aggregation to the 262 3-digit Census codes is certainly possible, many of these industry codes contain too few observations to be reliable.

[248] There is a strand of literature that indicates that small establishments tend to pay lower wages than larger establishments. This may imply that workers in small businesses are more likely to be affected than workers in large businesses; however, the literature does not make clear what the appropriate alternative rate for small businesses should be.

[249] Workers are designated as employed in a small business based on their industry of employment. The share of workers considered small in nonprofit, for profit, and government entities is therefore the weighted average of the shares for the industries that compose these categories.

The Department estimated that small entities employ 480,900 of the 1.3 million affected workers (38.2 percent) (Table 30). This composes 0.9 percent of the 53.1 million workers that small entities employ. The sectors with the highest total number of affected workers employed by small establishments are: Professional and technical services (79,700); retail trade (47,500); and health care services, except hospitals (43,500). The sectors with the largest percent of small business workers who are affected include: broadcasting (except internet) (2.0 percent); arts, entertainment, and recreation (1.9 percent); and insurance (1.9 percent).

TABLE 30—NUMBER OF AFFECTED WORKERS EMPLOYED BY SMALL ESTABLISHMENTS, BY INDUSTRY AND EMPLOYER TYPE

Industry	Workers (1,000s)		Affected workers (1,000s) [a]	
	Total	Small business employed	Total	Small business employed
Total	143,184.6	53,058.6	1,257.3	480.9
Industry				
Agriculture	([c])	([c])	([c])	([c])
Forest., log., fish., hunt., and trap	([c])	([c])	([c])	([c])
Mining	([c])	([c])	([c])	([c])
Construction	8,525.6	5,482.7	51.6	34.7
Nonmetallic mineral prod. manuf	([c])	([c])	([c])	([c])
Prim. metals and fab. metal prod	1,652.6	1,004.7	7.8	3.9
Machinery manufacturing	1,240.7	673.2	7.1	4.1
Computer and elect. prod. manuf	1,173.5	552.2	8.4	3.9
Electrical equip., appliance manuf	([c])	([c])	([c])	([c])
Transportation equip. manuf	2,616.6	728.6	15.0	4.1
Wood products	([c])	([c])	([c])	([c])
Furniture and fixtures manuf	([c])	([c])	([c])	([c])
Misc. and not spec. manuf	1,512.1	888.6	7.9	4.4
Food manufacturing	1,809.0	829.3	5.5	3.1
Beverage and tobacco products	([c])	([c])	([c])	([c])
Textile, app., and leather manuf	575.8	390.3	4.6	2.6
Paper and printing	871.7	464.6	7.2	4.5
Petroleum and coal prod. manuf	([c])	([c])	([c])	([c])
Chemical manufacturing	1,423.2	553.8	10.6	3.7
Plastics and rubber products	([c])	([c])	([c])	([c])
Wholesale trade	3,440.5	1,583.3	35.8	17.7
Retail trade	15,694.5	5,398.1	129.9	47.5
Transport. and warehousing	6,355.2	1,740.6	25.7	5.5
Utilities	1,391.6	264.2	12.4	3.8
Publishing ind. (ex. internet)	([c])	([c])	([c])	([c])
Motion picture and sound recording	([c])	([c])	([c])	([c])
Broadcasting (except internet)	554.0	129.4	8.2	2.5
Internet publishing and broadcasting	([c])	([c])	([c])	([c])
Telecommunications	([c])	([c])	([c])	([c])
Internet serv. providers and data	([c])	([c])	([c])	([c])
Other information services	([c])	([c])	([c])	([c])
Finance	4,506.3	847.0	76.8	15.2
Insurance	2,746.7	722.0	60.2	13.7
Real estate	2,091.1	1,274.7	25.4	17.3
Rental and leasing services	([c])	([c])	([c])	([c])
Professional and technical services	10,196.2	4,770.7	173.1	79.7
Management of companies & enterprises	([c])	([c])	([c])	([c])
Admin. and support services	5,080.7	2,309.8	33.5	13.5
Waste manag. and remed. services	([c])	([c])	([c])	([c])
Educational services	14,196.6	3,089.0	74.5	12.3
Hospitals	([c])	([c])	([c])	([c])
Health care services, except hospitals	10,074.6	4,787.1	91.0	43.5
Social assistance	3,040.0	1,703.7	52.8	28.3
Arts, entertainment, and recreation	2,760.6	1,394.5	53.0	26.7
Accommodation	1,475.8	566.4	9.8	4.0
Food services and drinking places	8,946.1	2,422.7	27.1	8.1
Repair and maintenance	1,614.1	1,214.7	11.4	8.2
Personal and laundry services	1,763.1	1,300.1	6.8	5.8
Membership associations & organizations	2,104.1	1,545.8	35.3	25.3
Private households	([c])	([c])	([c])	([c])
Public administration [b]	7,527.9	685.8	50.9	5.2
Employer Type				
Nonprofit, private	10,190.1	4,170.3	125.0	58.4

TABLE 30—NUMBER OF AFFECTED WORKERS EMPLOYED BY SMALL ESTABLISHMENTS, BY INDUSTRY AND EMPLOYER TYPE—Continued

Industry	Workers (1,000s)		Affected workers (1,000s) [a]	
	Total	Small business employed	Total	Small business employed
For profit, private	111,050.8	46,579.0	1,000.5	410.5
Government (state and local)	18,078.8	2,309.4	131.9	11.9

Note: Worker data are from pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.
[a] Estimation of affected workers employed by small establishments was done at the Census 4-digit occupational code and industry level. Therefore, at the more aggregated 51 industry level shown in this table, the ratio of small business employed to total employed does not equal the ratio of affected small business employed to total affected for each industry, nor does it equal the ratio for the national total because relative industry size, employment, and small business employment differs from industry to industry.
[b] Establishment number represents the total number of state and local governments. Data from Census of Governments, 2017.
[c] Data not displayed due to reliability concerns; sample size of affected workers in small establishments is less than 10.

Because no information is available on how affected workers are distributed among small establishments that employ affected workers, the Department estimated a range for effects. At one end of this range, the Department assumed that each small establishment employs no more than one affected worker, meaning that at most 480,900 of the 6.3 million small establishments will employ an affected worker. Thus, these assumptions provide an upper bound estimate of the number of affected small establishments (although it provides a lower bound estimate of the effect per small establishment because costs are spread over a larger number of establishments). The impacts experienced by an establishment would increase as the share of its workers that are affected increases. Establishments that employ only affected workers are most likely to experience the most severe effects. Therefore, to estimate a lower-end estimate for the number of affected establishments (which generates an upper-end estimate for impacts per establishment) the Department assumed that all workers employed by an affected establishment are affected.

For the purposes of estimating this lower-range number of affected small establishments, the Department used the average size of a small establishment as the typical size of an affected small establishment.[250] The average number of employees in a small establishment is the number of workers that small establishments employ divided by the total number of small establishments in that industry (SUSB 2012). Thus, the number of affected small establishments in an industry, if all employees of an affected establishment are affected, equals the number of affected small establishment employees divided by the average number of employees per small establishment.

Table 31 summarizes the estimated number of affected workers that small establishments employ and the expected range for the number of affected small establishments by industry. The Department estimated that the rule will affect 480,900 workers who are employed by somewhere between 63,400 and 480,900 small establishments; this composes from 1.0 percent to 7.6 percent of all small establishments. It also means that from 5.9 million to 6.3 million small establishments incur no more than minimal regulatory familiarization costs (*i.e.,* 6.3 million minus 480,900 equals 5.9 million; 6.3 million minus 63,400 equals 6.3 million, using rounded values). The table also presents the average number of affected employees per establishment using the method in which all employees at the establishment are affected. For the other method, by definition, there is always one affected employee per establishment. Also displayed is the average payroll per small establishment by industry (based on both affected and non-affected small establishments), calculated by dividing total payroll of small businesses by the number of small businesses (Table 29) (applicable to both methods).

TABLE 31—NUMBER OF SMALL AFFECTED ESTABLISHMENTS AND EMPLOYEES BY INDUSTRY AND EMPLOYER TYPE

Industry	Affected workers in small entities (1,000s)	Number of small affected establishments (1,000s) [a]		Per establishment	
		One affected employee per estab. [b]	All employees at estab. affected [c]	Affected employees [a]	Average annual payroll ($1,000s)
Total	480.9	480.9	63.4	7.6	$452.0
Industry					
Agriculture	([d])	([d])	([d])	([d])	([d])

[250] This is not the true lower bound estimate of the number of affected establishments. Strictly speaking, a true lower bound estimate of the number of affected small establishments would be calculated by assuming all employees in the largest small establishments are affected. For example, if the SBA standard is that establishments with 500 employees are ''small,'' and 1,350 affected workers are employed by small establishments in that industry, then the smallest number of establishments that could be affected in that industry (the true lower bound) would be three. However, because such an outcome appears implausible, the Department determined a more reasonable lower estimate would be based on average establishment size.

TABLE 31—NUMBER OF SMALL AFFECTED ESTABLISHMENTS AND EMPLOYEES BY INDUSTRY AND EMPLOYER TYPE—Continued

Industry	Affected workers in small entities (1,000s)	Number of small affected establishments (1,000s) [a]		Per establishment	
		One affected employee per estab. [b]	All employees at estab. affected [c]	Affected employees [a]	Average annual payroll ($1,000s)
Forest., log., fish., hunt., and trap	([d])	([d])	([d])	([d])	([d])
Mining	([d])	([d])	([d])	([d])	([d])
Construction	34.7	34.7	4.3	8.1	457.2
Nonmetallic mineral prod. manuf	([d])	([d])	([d])	([d])	([d])
Prim. metals and fab. metal prod	3.9	3.9	0.2	18.0	980.4
Machinery manufacturing	4.1	4.1	0.1	31.4	2,048.1
Computer and elect. prod. manuf	3.9	3.9	0.1	50.1	4,856.7
Electrical equip., appliance manuf	([d])	([d])	([d])	([d])	([d])
Transportation equip. manuf	4.1	4.1	0.1	72.5	4,677.3
Wood products	([d])	([d])	([d])	([d])	([d])
Furniture and fixtures manuf	([d])	([d])	([d])	([d])	([d])
Misc. and not spec. manuf	4.4	4.4	0.1	35.5	2,146.1
Food manufacturing	3.1	3.1	0.1	34.7	1,504.7
Beverage and tobacco products	([d])	([d])	([d])	([d])	([d])
Textile, app., and leather manuf.	2.6	2.6	0.1	25.6	1,151.1
Paper and printing	4.5	4.5	0.3	16.9	918.3
Petroleum and coal prod. manuf.	([d])	([d])	([d])	([d])	([d])
Chemical manufacturing	3.7	3.7	0.1	51.8	4,246.9
Plastics and rubber products	([d])	([d])	([d])	([d])	([d])
Wholesale trade	17.7	17.7	3.7	4.8	299.5
Retail trade	47.5	47.5	6.1	7.8	340.9
Transport. and warehousing	5.5	5.5	0.6	9.5	459.4
Utilities	3.8	3.8	0.1	34.0	2,612.6
Publishing ind. (ex. internet)	([d])	([d])	([d])	([d])	([d])
Motion picture and sound recording	([d])	([d])	([d])	([d])	([d])
Broadcasting (except internet)	2.5	2.5	0.1	28.0	1,851.5
Internet publishing and broadcasting	([d])	([d])	([d])	([d])	([d])
Telecommunications	([d])	([d])	([d])	([d])	([d])
Internet serv. providers and data	([d])	([d])	([d])	([d])	([d])
Other information services	([d])	([d])	([d])	([d])	([d])
Finance	15.2	15.2	2.3	6.5	545.0
Insurance	13.7	13.7	2.7	5.1	365.7
Real estate	17.3	17.3	3.9	4.5	270.4
Rental and leasing services	([d])	([d])	([d])	([d])	([d])
Professional and technical services	79.7	79.7	13.7	5.8	505.6
Management of companies and enterprises	([d])	([d])	([d])	([d])	([d])
Admin. and support services	13.5	13.5	1.9	7.0	266.8
Waste manag. and remed. services	([d])	([d])	([d])	([d])	([d])
Educational services	12.3	12.3	0.4	34.1	1,790.4
Hospitals	([d])	([d])	([d])	([d])	([d])
Health care services, except hospitals	43.5	43.5	5.2	8.3	410.4
Social assistance	28.3	28.3	2.5	11.4	405.9
Arts, entertainment, and recreation	26.7	26.7	2.4	11.0	430.7
Accommodation	4.0	4.0	0.4	10.1	378.3
Food services and drinking places	8.1	8.1	1.7	4.8	130.7
Repair and maintenance	8.2	8.2	1.4	6.1	269.9
Personal and laundry services	5.8	5.8	0.9	6.4	206.4
Membership associations & organizations	25.3	25.3	4.9	5.2	271.4
Private households	([d])	([d])	([d])	([d])	([d])
Public administration [f]	5.2	5.2	0.6	9.4	550.3
Employer Type					
Nonprofit, private	58.4	58.4	7.1	8.3	428.8
For profit, private	410.5	410.5	50.7	8.1	438.9
Government (state and local)	11.9	11.9	0.4	31.7	1,734.0

Note: Establishment data are from the Survey of U.S. Businesses 2016; worker and payroll data from pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.

[a] Estimation of both affected small establishment employees and affected small establishments was done at the most detailed industry level available. Therefore, the ratio of affected small establishment employees to total small establishment employees for each industry may not match the ratio of small affected establishments to total small establishments at the more aggregated industry level presented in the table, nor will it equal the ratio at the national level because relative industry size, employment, and small business employment differs from industry to industry.

[b] This method may overestimate the number of affected establishments and therefore the ratio of affected workers to affected establishments may be greater than 1-to-1. However, we addressed this issue by also calculating effects based on the assumption that 100 percent of workers at an establishment are affected.

[c] For example, on average, a small establishment in the construction industry employs 8.1 workers (5.5 million employees divided by 676,900 small establishments). This method assumes if an establishment is affected then all 8.1 workers are affected. Therefore, in the construction industry this method estimates there are 4,300 small affected establishments (34,700 affected small workers divided by 8.1).

[d] Data not displayed due to reliability concerns; sample size of affected workers in small establishments is less than 10.

[e] Number of establishments is smaller than number of affected employees; thus, total number of establishments reported.

[f] Establishment number represents the total number of state and local governments.

v. Projected Impacts to Affected Small Entities

For small entities, the Department projected various types of effects, including regulatory familiarization costs, adjustment costs, managerial costs, and payroll increases to employees. The Department estimated a range for the number of small affected establishments and the impacts they incur. However, few establishments are likely to incur the effects at the upper end of this range because it seems unlikely that the final rule would affect all employees at a small firm. While the upper and lower bounds are likely over- and under-estimates, respectively, of effects per small establishment, the Department believes that this range of costs and payroll increases provides the most accurate characterization of the effects of the rule on small employers.[251] Furthermore, the smaller estimate of the number of affected establishments (*i.e.,* where all employees are assumed to be affected) will result in the largest costs and payroll increases per entity as a percent of establishment payroll and revenue, and the Department expects that many, if not most, entities will incur smaller costs, payroll increases, and effects relative to establishment size.

The Department expects total direct employer costs will range from $80.1 million to $97.1 million for affected small establishments (Table 32) in the first year. Small establishments that do not employ affected workers will incur an additional $254.4 million to $272.5 million in regulatory familiarization costs. The three industries with the highest costs (professional and technical services; retail trade; and health care services, except hospitals) account for about 36 percent of the costs. The transportation equipment manufacturing industry is expected to incur the largest cost per establishment ($11,700 using the method where all employees are affected), although the costs are not expected to exceed 0.25 percent of payroll. The food services and drinking places industry is expected to experience the largest effect as a share of payroll (estimated direct costs compose 0.63 percent of average entity payroll).

TABLE 32—YEAR 1 SMALL ESTABLISHMENT DIRECT COSTS, TOTAL AND PER ESTABLISHMENT, BY INDUSTRY AND EMPLOYER TYPE

Industry	Cost to small entities in year 1 [a]					
	One affected employee			All employees affected		
	Total (millions) [b]	Cost per affected entity	Percent of annual payroll	Total (millions) [b]	Cost per affected entity	Percent of annual payroll
Total	$97.1	$202	0.04%	$80.1	$1,263	0.28
Industry						
Agriculture	([c])	([c])	([c])	([c])	([c])	([c])
Forest., log., fish., hunt., and trap	([c])	([c])	([c])	([c])	([c])	([c])
Mining	([c])	([c])	([c])	([c])	([c])	([c])
Construction	7.1	204	0.04	5.8	1,348	0.29
Nonmetallic mineral prod. manuf	([c])	([c])	([c])	([c])	([c])	([c])
Prim. metals and fab. metal prod	0.8	204	0.02	0.6	2,943	0.30
Machinery manufacturing	0.8	204	0.01	0.7	5,094	0.249
Computer and elect. prod. manuf	0.8	204	0.00	0.6	8,116	0.17
Electrical equip., appliance manuf	([c])	([c])	([c])	([c])	([c])	([c])
Transportation equip. manuf	0.8	204	0.00	0.7	11,720	0.25
Wood products	([c])	([c])	([c])	([c])	([c])	([c])
Furniture and fixtures manuf	([c])	([c])	([c])	([c])	([c])	([c])
Misc. and not spec. manuf	0.9	204	0.01	0.7	5,758	0.27
Food manufacturing	0.6	204	0.01	0.5	5,639	0.37
Beverage and tobacco products	([c])	([c])	([c])	([c])	([c])	([c])
Textile, app., and leather manuf	0.5	204	0.02	0.4	4,175	0.36
Paper and printing	0.9	204	0.02	0.7	2,759	0.30
Petroleum and coal prod. manuf	([c])	([c])	([c])	([c])	([c])	([c])
Chemical manufacturing	0.8	204	0.00	0.6	8,382	0.20
Plastics and rubber products	([c])	([c])	([c])	([c])	([c])	([c])
Wholesale trade	3.6	204	0.07	3.0	820	0.27
Retail trade	9.7	204	0.06	7.9	1,306	0.38
Transport. and warehousing	1.1	204	0.04	0.9	1,569	0.34
Utilities	0.8	204	0.01	0.6	5,527	0.21
Publishing ind. (ex. internet)	([c])	([c])	([c])	([c])	([c])	([c])
Motion picture and sound recording	([c])	([c])	([c])	([c])	([c])	([c])
Broadcasting (except internet)	0.5	204	0.01	0.4	4,556	0.25
Internet publishing and broadcasting	([c])	([c])	([c])	([c])	([c])	([c])
Telecommunications	([c])	([c])	([c])	([c])	([c])	([c])
Internet serv. providers and data	([c])	([c])	([c])	([c])	([c])	([c])
Other information services	([c])	([c])	([c])	([c])	([c])	([c])
Finance	3.1	204	0.04	2.5	1,095	0.20
Insurance	2.8	204	0.06	2.3	864	0.24
Real estate	3.5	204	0.08	3.0	760	0.28

[251] As noted previously, these are not the true lower and upper bounds. The values presented are the highest and lowest estimates the Department believes are plausible.

TABLE 32—YEAR 1 SMALL ESTABLISHMENT DIRECT COSTS, TOTAL AND PER ESTABLISHMENT, BY INDUSTRY AND EMPLOYER TYPE—Continued

Industry	Cost to small entities in year 1 [a]					
	One affected employee			All employees affected		
	Total (millions) [b]	Cost per affected entity	Percent of annual payroll	Total (millions) [b]	Cost per affected entity	Percent of annual payroll
Rental and leasing services	([c])	([c])	([c])	([c])	([c])	([c])
Professional and technical services	16.3	204	0.04	13.4	982	0.19
Management of companies and enterprises	([c])	([c])	([c])	([c])	([c])	([c])
Admin. and support services	2.8	204	0.08	2.3	1,175	0.44
Waste manag. and remed. services	([c])	([c])	([c])	([c])	([c])	([c])
Educational services	2.5	204	0.01	2.0	5,539	0.31
Hospitals	([c])	([c])	([c])	([c])	([c])	([c])
Health care services, except hospitals	8.9	204	0.05	7.2	1,383	0.34
Social assistance	5.8	204	0.05	4.7	1,885	0.46
Arts, entertainment, and recreation	5.4	204	0.05	4.4	1,822	0.42
Accommodation	0.8	204	0.05	0.7	1,678	0.44
Food services and drinking places	1.7	204	0.16	1.4	823	0.63
Repair and maintenance	1.7	204	0.08	1.4	1,023	0.38
Personal and laundry services	1.2	204	0.10	1.0	1,082	0.52
Membership associations & organizations	5.2	204	0.08	4.3	878	0.32
Private households	([c])	([c])	([c])	([c])	([c])	([c])
Public administration	1.1	204	0.04	0.9	1,561	0.28
Employer Type						
Nonprofit, private	11.6	199	0.05	9.4	1,330	0.31
For profit, private	86.6	211	0.05	71.0	1,400	0.32
Government (state and local)	2.4	201	0.01	1.9	5,055	0.29

Note: Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.
[a] Direct costs include regulatory familiarization, adjustment, and managerial costs.
[b] The range of costs per establishment depends on the number of affected establishments. The minimum assumes that each affected establishment has one affected worker (therefore, the number of affected establishments is equal to the number of affected workers). The maximum assumes the share of workers in small entities who are affected is also the share of small entity establishments that are affected.
[c] Data not displayed due to reliability concerns; sample size of affected workers in small establishments is less than 10.

It is possible that the costs of the final rule may be disproportionately large for small entities, especially because small entities often have limited or no human resources personnel on staff. However, the Department expects that small entities will rely upon compliance assistance materials provided by the Department or industry associations to become familiar with the final rule. Additionally, the Department notes that the final rule is quite limited in scope as it primarily makes changes to the salary component of the part 541 regulations. Finally, the Department believes that most entities have at least some nonexempt employees and, therefore, already have policies and systems in place for monitoring and recording their hours. The Department believes that applying those same policies and systems to the workers whose exemption status changes will not be an unreasonable burden on small businesses. Average weekly earnings for affected EAP workers in small establishments are expected to increase by about $6.07 per week per affected worker, using the incomplete fixed-job model [252] described in section VI.D.iv.3.[253] This will lead to $151.8 million in additional annual wage payments to employees in small entities (less than 0.6 percent of aggregate affected establishment payroll; Table 33). The largest payroll increases per establishment are expected in the sectors of textile, apparel, and leather manufacturing (up to $27,000 per entity); transportation equipment manufacturing (up to $14,600 per entity); and food manufacturing (up to $14,500 per entity). However, average payroll increases per establishment exceed 2 percent of average annual payroll in only two sectors: Food services and drinking places (3.0 percent) and textile, apparel, and leather manufacturing (2.3 percent).

[252] As explained in section VI.D.iv.3, the incomplete fixed-job model reflects the Department's determination that an appropriate estimate of the impact on the implicit hourly rate of pay for regular overtime workers should be determined using the average of Barkume's and Trejo's two estimates of the incomplete fixed-job model adjustments: A wage change that is 40 percent of the adjustment toward the amount predicted by the fixed-job model, assuming an initial zero overtime pay premium, and a wage change that is 80 percent of the adjustment assuming an initial 28 percent overtime pay premium.

[253] This is an average increase for all affected workers (both EAP and HCE), and reconciles to the weighted average of individual salary changes discussed in the Transfers section.

TABLE 33—YEAR 1 SMALL ESTABLISHMENT PAYROLL INCREASES, TOTAL AND PER ESTABLISHMENT, BY INDUSTRY AND EMPLOYER TYPE

Industry	Increased payroll for small entities in year 1 [a]				
	Total (millions)	One affected employee		All employees affected	
		Per estab.	Percent of annual payroll	Per estab.	Percent of annual payroll
Total	$151.8	$316	0.07	$2,393	0.53
Industry					
Agriculture	([b])	([b])	([b])	([b])	([b])
Forest., log., fish., hunt., and trap.	([b])	([b])	([b])	([b])	([b])
Mining	([b])	([b])	([b])	([b])	([b])
Construction	9.2	265	0.06	2,147	0.47
Nonmetallic mineral prod. manuf.	([b])	([b])	([b])	([b])	([b])
Prim. metals and fab. metal prod.	1.0	257	0.03	4,622	0.47
Machinery manufacturing	1.7	405	0.02	12,710	0.62
Computer and elect. prod. manuf.	0.3	80	0.00	4,004	0.08
Electrical equip., appliance manuf.	([b])	([b])	([b])	([b])	([b])
Transportation equip. manuf.	0.8	200	0.00	14,528	0.31
Wood products	([b])	([b])	([b])	([b])	([b])
Furniture and fixtures manuf.	([b])	([b])	([b])	([b])	([b])
Misc. and not spec. manuf.	1.7	389	0.02	13,794	0.64
Food manufacturing	1.3	417	0.03	14,476	0.96
Beverage and tobacco products	([b])	([b])	([b])	([b])	([b])
Textile, app., and leather manuf.	2.7	1,051	0.09	26,943	2.34
Paper and printing	1.1	233	0.03	3,931	0.43
Petroleum and coal prod. manuf.	([b])	([b])	([b])	([b])	([b])
Chemical manufacturing	0.9	236	0.01	12,236	0.29
Plastics and rubber products	([b])	([b])	([b])	([b])	([b])
Wholesale trade	4.7	263	0.09	1,270	0.42
Retail trade	17.1	360	0.11	2,818	0.83
Transport. and warehousing	1.8	321	0.07	3,039	0.66
Utilities		0		0	
Publishing ind. (ex. internet)	([b])	([b])	([b])	([b])	([b])
Motion picture and sound recording	([b])	([b])	([b])	([b])	([b])
Broadcasting (except internet)	1.1	451	0.02	12,620	0.68
Internet publishing and broadcasting	([b])	([b])	([b])	([b])	([b])
Telecommunications	([b])	([b])	([b])	([b])	([b])
Internet serv. providers and data	([b])	([b])	([b])	([b])	([b])
Other information services	([b])	([b])	([b])	([b])	([b])
Finance	3.6	239	0.04	1,557	0.29
Insurance	2.3	169	0.05	862	0.24
Real estate	8.5	489	0.18	2,175	0.80
Rental and leasing services	([b])	([b])	([b])	([b])	([b])
Professional and technical services	32.2	404	0.08	2,351	0.47
Management of companies and enterprises	([b])	([b])	([b])	([b])	([b])
Admin. and support services	3.6	265	0.10	1,859	0.70
Waste manag. and remed. services	([b])	([b])	([b])	([b])	([b])
Educational services	4.6	373	0.02	12,716	0.71
Hospitals	([b])	([b])	([b])	([b])	([b])
Health care services, except hospitals	5.8	134	0.03	1,114	0.27
Social assistance	4.2	148	0.04	1,690	0.42
Arts, entertainment, and recreation	15.1	567	0.13	6,260	1.45
Accommodation		0		0	
Food services and drinking places	6.6	818	0.63	3,960	3.03
Repair and maintenance	3.8	466	0.17	2,832	1.05
Personal and laundry services	0.6	110	0.05	709	0.34
Membership associations & organizations	4.1	160	0.06	831	0.31
Private households	([b])	([b])	([b])	([b])	([b])
Public administration	0.9	165	0.03	1,553	0.28
Employer Type					
Nonprofit, private	26.2	448	0.10	3,702	0.86
For profit, private	124.4	303	0.07	2,452	0.56
Government (state and local)	1.3	108	0.01	3,422	0.20

Note: Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.

[a] Aggregate change in total annual payroll experienced by small entities under the updated salary levels after labor market adjustments. This amount represents the total amount of (wage) transfers from employers to employees.

[b] Data not displayed due to reliability concerns; sample size of affected workers in small establishments is less than 10.

Table 34 presents estimated first year direct costs and payroll increases combined per establishment and the costs and payroll increases as a percent of average establishment payroll. The Department presents only the results for the upper bound scenario where all workers employed by the establishment are affected. Combined costs and payroll increases per establishment range from $1,700 in the accommodations industry to $31,100 in textile, apparel, and leather manufacturing. Combined costs and payroll increases compose more than 2 percent of average annual establishment payroll in two sectors: Food services and drinking places (3.7 percent) and textile, apparel, and leather manufacturing (2.7 percent). In all other sectors, they range from 0.2 percent to 1.9 percent of payroll.

However, comparing costs and payroll increases to payrolls overstates the effects on establishments because payroll represents only a fraction of the financial resources available to an establishment. The Department approximated revenue per small affected establishment by calculating the ratio of small business revenues to payroll by industry from the 2012 SUSB data then multiplying that ratio by average small entity payroll.[254] Using this approximation of annual revenues as a benchmark, only one sector has costs and payroll increases amounting to more than one percent of revenues, food services and drinking places (1.1 percent).

TABLE 34—YEAR 1 SMALL ESTABLISHMENT DIRECT COSTS AND PAYROLL INCREASES, TOTAL AND PER ESTABLISHMENT, BY INDUSTRY AND EMPLOYER TYPE, USING ALL EMPLOYEES IN ESTABLISHMENT AFFECTED METHOD

Industry	Costs and payroll increases for small affected establishments, all employees affected			
	Total (millions)	Per estab. [a]	Percent of annual payroll	Percent of estimated revenues [b]
Total	$231.9	$3,656	0.81	0.15
Industry				
Agriculture	([c])	([c])	([c])	([c])
Forest., log., fish., hunt., and trap	([c])	([c])	([c])	([c])
Mining	([c])	([c])	([c])	([c])
Construction	15.0	3,495	0.76	0.17
Nonmetallic mineral prod. manuf	([c])	([c])	([c])	([c])
Prim. metals and fab. metal prod	1.6	7,565	0.77	0.15
Machinery manufacturing	2.3	17,804	0.87	0.18
Computer and elect. prod. manuf	0.9	12,119	0.25	0.05
Electrical equip., appliance manuf	([c])	([c])	([c])	([c])
Transportation equip. manuf	1.5	26,248	0.56	0.08
Wood products	([c])	([c])	([c])	([c])
Furniture and fixtures manuf	([c])	([c])	([c])	([c])
Misc. and not spec. manuf	2.4	19,552	0.91	0.21
Food manufacturing	1.8	20,115	1.34	0.12
Beverage and tobacco products	([c])	([c])	([c])	([c])
Textile, app., and leather manuf	3.2	31,118	2.70	0.50
Paper and printing	1.8	6,690	0.73	0.15
Petroleum and coal prod. manuf	([c])	([c])	([c])	([c])
Chemical manufacturing	1.5	20,618	0.49	0.04
Plastics and rubber products	([c])	([c])	([c])	([c])
Wholesale trade	7.7	2,090	0.70	0.04
Retail trade	25.0	4,123	1.21	0.12
Transport. and warehousing	2.7	4,608	1.00	0.23
Utilities	0.6	5,527	0.21	0.02
Publishing ind. (ex. internet)	([c])	([c])	([c])	([c])
Motion picture and sound recording	([c])	([c])	([c])	([c])
Broadcasting (except internet)	1.6	17,176	0.93	0.33
Internet publishing and broadcasting	([c])	([c])	([c])	([c])
Telecommunications	([c])	([c])	([c])	([c])
Internet serv. providers and data	([c])	([c])	([c])	([c])
Other information services	([c])	([c])	([c])	([c])
Finance	6.2	2,652	0.49	0.17
Insurance	4.6	1,727	0.47	0.11
Real estate	11.4	2,936	1.09	0.24
Rental and leasing services	([c])	([c])	([c])	([c])
Professional and technical services	45.6	3,333	0.66	0.26
Management of companies and enterprises	([c])	([c])	([c])	([c])
Admin. and support services	5.8	3,034	1.14	0.51
Waste manag. and remed. services	([c])	([c])	([c])	([c])
Educational services	6.6	18,255	1.02	0.39
Hospitals	([c])	([c])	([c])	([c])
Health care services, except hospitals	13.1	2,497	0.61	0.26
Social assistance	8.8	3,575	0.88	0.41

[254] The ratio of revenues to payroll for small businesses ranged from 2.15 (social assistance) to 43.40 (petroleum and coal products manufacturing), with an average over all sectors of 5.35. The Department used this estimate of revenue, instead of small business revenue reported directly from the 2012 SUSB so revenue aligned with payrolls in 2018.

TABLE 34—YEAR 1 SMALL ESTABLISHMENT DIRECT COSTS AND PAYROLL INCREASES, TOTAL AND PER ESTABLISHMENT, BY INDUSTRY AND EMPLOYER TYPE, USING ALL EMPLOYEES IN ESTABLISHMENT AFFECTED METHOD—Continued

Industry	Costs and payroll increases for small affected establishments, all employees affected			
	Total (millions)	Per estab. [a]	Percent of annual payroll	Percent of estimated revenues [b]
Arts, entertainment, and recreation	19.5	8,082	1.88	0.62
Accommodation	0.7	1,678	0.44	0.11
Food services and drinking places	8.0	4,783	3.66	1.09
Repair and maintenance	5.2	3,855	1.43	0.40
Personal and laundry services	1.6	1,791	0.87	0.30
Membership associations & organizations	8.4	1,710	0.63	0.16
Private households	([c])	([c])	([c])	([c])
Public administration	1.7	3,114	0.57	0.15
Employer Type				
Nonprofit, private	94.40	3,570	1.00	0.30
For profit, private	585.30	3,532	1.00	0.20
Government (state and local)	12.20	9,264	0.60	0.20

Note: Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.
[a] Total direct costs and transfers for small establishments in which all employees are affected. Impacts to small establishments in which one employee is affected will be a fraction of the impacts presented in this table.
[b] Revenues estimated by calculating the ratio of estimated small business revenues to payroll from the 2012 SUSB, and multiplying by payroll per small entity. For the public administration sector, the ratio was calculated using revenues and payroll from the 2017 Census of Governments.
[c] Data not displayed due to reliability concerns; sample size of affected workers in small establishments is less than 10.

vi. Projected Effects to Affected Small Entities in Year 2 Through Year 10

To determine how small businesses will be affected in future years, the Department projected costs to small businesses for nine years after Year 1 of the rule. Projected employment and earnings were calculated using the same methodology described in section VI.B.iii. Affected employees in small firms follow a similar pattern to affected workers in all establishments: the number decreases gradually in projected years. There are 480,900 affected workers in small establishments in Year 1 and 337,700 in Year 10. Table 35 reports affected workers in selected years only.

TABLE 35—PROJECTED NUMBER OF AFFECTED WORKERS IN SMALL ESTABLISHMENTS, BY INDUSTRY

Industry	Affected workers in small establishments (1,000s)	
	Year 1	Year 10
Total	480.9	337.7
Agriculture	([a])	([a])
Forest., log., fish., hunt., and trap	([a])	([a])
Mining	([a])	([a])
Construction	34.7	20.7
Nonmetallic mineral prod. manuf	([a])	([a])
Prim. metals and fab. metal prod	3.9	([a])
Machinery manufacturing	4.1	4.4
Computer and elect. prod. manuf	3.9	([a])
Electrical equip., appliance manuf	([a])	([a])
Transportation equip. manuf	4.1	([a])
Wood products	([a])	([a])
Furniture and fixtures manuf	([a])	([a])
Misc. and not spec. manuf	4.4	3.8
Food manufacturing	3.1	([a])
Beverage and tobacco products	([a])	([a])
Textile, app., and leather manuf	2.6	([a])
Paper and printing	4.5	([a])
Petroleum and coal prod. manuf	([a])	([a])
Chemical manufacturing	3.7	([a])
Plastics and rubber products	([a])	([a])
Wholesale trade	17.7	12.7
Retail trade	47.5	26.9
Transport. and warehousing	5.5	3.8
Utilities	3.8	([a])
Publishing ind. (ex. internet)	([a])	([a])
Motion picture and sound recording	([a])	([a])
Broadcasting (except internet)	2.5	([a])

TABLE 35—PROJECTED NUMBER OF AFFECTED WORKERS IN SMALL ESTABLISHMENTS, BY INDUSTRY—Continued

Industry	Affected workers in small establishments (1,000s)	
	Year 1	Year 10
Internet publishing and broadcasting	([a])	([a])
Telecommunications	([a])	([a])
Internet serv. providers and data	([a])	([a])
Other information services	([a])	([a])
Finance	15.2	12.1
Insurance	13.7	13.0
Real estate	17.3	12.1
Rental and leasing services	([a])	([a])
Professional and technical services	79.7	55.7
Management of companies and enterprises	([a])	([a])
Admin. and support services	13.5	9.3
Waste manag. and remed. services	([a])	([a])
Educational services	12.3	11.1
Hospitals	([a])	([a])
Health care services, except hospitals	43.5	35.3
Social assistance	28.3	25.7
Arts, entertainment, and recreation	26.7	17.6
Accommodation	4.0	([a])
Food services and drinking places	8.1	6.2
Repair and maintenance	8.2	7.6
Personal and laundry services	5.8	3.9
Membership associations & organizations	25.3	18.2
Private households	([a])	([a])
Public administration	5.2	2.7

Note: Worker data are from pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.
[a] Data not displayed because sample size of affected workers in small establishments is less than 10.

Costs to small establishments vary by year but generally decrease from Year 1 mostly because regulatory familiarization costs are zero in all projected years, and adjustment costs are relatively small. By Year 10, additional costs and payroll for small businesses have decreased from $231.9 million in Year 1 to $118.5 million (Table 36). The Department notes that, due to relatively small sample sizes, the estimates by detailed industry are not precise. This can cause some numbers in the data to vary across years by a greater amount than they will in the future.

TABLE 36—PROJECTED DIRECT COSTS AND PAYROLL INCREASES FOR AFFECTED SMALL ESTABLISHMENTS, BY INDUSTRY, USING ALL EMPLOYEES IN ESTABLISHMENT AFFECTED METHOD

Industry	Costs and payroll increases for small affected establishments, all employees affected (millions 2019)	
	Year 1	Year 10
Total	$231.9	$118.5
Agriculture	([a])	([a])
Forest., log., fish., hunt., and trap	([a])	([a])
Mining	([a])	([a])
Construction	15.0	6.1
Nonmetallic mineral prod. manuf	([a])	([a])
Prim. metals and fab. metal prod	1.6	([a])
Machinery manufacturing	2.3	2.6
Computer and elect. prod. manuf	0.9	([a])
Electrical equip., appliance manuf	([a])	([a])
Transportation equip. manuf	1.5	([a])
Wood products	([a])	([a])
Furniture and fixtures manuf	([a])	([a])
Misc. and not spec. manuf	2.4	1.1
Food manufacturing	1.8	([a])
Beverage and tobacco products	([a])	([a])
Textile, app., and leather manuf	3.2	([a])
Paper and printing	1.8	([a])
Petroleum and coal prod. manuf	([a])	([a])
Chemical manufacturing	1.5	([a])
Plastics and rubber products	([a])	([a])
Wholesale trade	7.7	7.0

TABLE 36—PROJECTED DIRECT COSTS AND PAYROLL INCREASES FOR AFFECTED SMALL ESTABLISHMENTS, BY INDUSTRY, USING ALL EMPLOYEES IN ESTABLISHMENT AFFECTED METHOD—Continued

Industry	Costs and payroll increases for small affected establishments, all employees affected (millions 2019)	
	Year 1	Year 10
Retail trade	25.0	14.7
Transport. and warehousing	2.7	0.5
Utilities	0.6	([a])
Publishing ind. (ex. internet)	([a])	([a])
Motion picture and sound recording	([a])	([a])
Broadcasting (except internet)	1.6	([a])
Internet publishing and broadcasting	([a])	([a])
Telecommunications	([a])	([a])
Internet serv. providers and data	([a])	([a])
Other information services	([a])	([a])
Finance	6.2	2.1
Insurance	4.6	2.6
Real estate	11.4	4.7
Rental and leasing services	([a])	([a])
Professional and technical services	45.6	21.8
Management of companies and enterprises	([a])	([a])
Admin. and support services	5.8	2.3
Waste manag. and remed. services	([a])	([a])
Educational services	6.6	3.9
Hospitals	([a])	([a])
Health care services, except hospitals	13.1	6.4
Social assistance	8.8	4.9
Arts, entertainment, and recreation	19.5	6.0
Accommodation	0.7	([a])
Food services and drinking places	8.0	3.7
Repair and maintenance	5.2	3.2
Personal and laundry services	1.6	0.8
Membership associations & organizations	8.4	5.9
Private households	([a])	([a])
Public administration	1.7	0.3

Note: Pooled CPS data for 7/2016–6/2019 adjusted to reflect 2018/2019.
[a] Data not displayed because sample size of affected workers in small establishments is less than 10.

E. Projected Reporting, Recordkeeping, and Other Compliance Requirements of the Final Rule

The FLSA sets minimum wage, overtime pay, and recordkeeping requirements for employment subject to its provisions. Unless exempt, covered employees must be paid at least the minimum wage and not less than one and one-half times their regular rates of pay for overtime hours worked.

Every covered employer must keep certain records for each nonexempt worker. The regulations at part 516 require employers to maintain records for employees subject to the minimum wage and overtime pay provisions of the FLSA. The recordkeeping requirements are not new requirements; however, employers will need to keep some additional records for affected employees who become nonexempt. As indicated in this analysis, this final rule expands minimum wage and overtime pay coverage to 1.2 million affected EAP workers. This will result in an increase in employer burden and was estimated in the PRA portion (section V) of this final rule. Note that the burdens reported for the PRA section of this rule include the entire information collection and not merely the additional burden estimated as a result of this final rule.

F. Steps the Agency Has Taken To Minimize the Significant Economic Impact on Small Entities

This section discusses the description of the steps the agency has taken to minimize the economic impact on small entities, consistent with the stated objectives of the FLSA. It includes a statement of the factual, policy, and legal reasons for the selected standard and HCE levels adopted in the final rule and why alternatives were rejected.

In this final rule, the Department sets the standard salary level equal to the 20th percentile of earnings of full-time salaried workers in the lowest-wage Census Region (currently the South) and/or the retail industry. Based on 2018/19 data, this results in a salary level of 684 per week, or 35,568 annually for a full-year worker. The Department believes that a standard salary level set at the 20th percentile of earnings of full-time salaried workers in the lowest-wage Census Region and/or retail industry will accomplish the goal of setting a salary threshold that adequately distinguishes between employees who may meet the duties requirements of the EAP exemption and those who likely do not, without necessitating the reintroduction of a limit on nonexempt work as existed under the long duties test. The Department sets the HCE total annual compensation level equal to the 80th percentile of earnings of full-time salaried workers nationally (107,432 annually based on 2018/19 data).[255] The Department believes that this level avoids unduly burdensome costs associated with evaluating, under the

[255] The Department estimated this value using CPS data for earnings of full-time (defined as at least 35 hours per week) nonhourly paid employees. For the purpose of this rulemaking, the Department considers data representing compensation paid to nonhourly workers to be an appropriate proxy for compensation paid to salaried workers.

standard duties test, the exemption statuses of large numbers of highly-paid white collar employees, many of whom would have remained exempt even under that test, while providing a meaningful and appropriate complement to the more lenient HCE duties test. The Department further believes that nearly all of the highly-paid white collar workers earning above this threshold ''would satisfy any duties test.'' [256]

The Department is also revising the regulations to permit employers to count nondiscretionary bonuses, incentives, and commissions toward up to 10 percent of the required salary level for the standard exemption, so long as employers pay those amounts on an annually or more frequent basis.

i. Differing Compliance and Reporting Requirements for Small Entities

This final rule provides no differing compliance requirements and reporting requirements for small entities. The Department has strived to minimize respondent recordkeeping burden by requiring no specific form or order of records under the FLSA and its corresponding regulations. Moreover, employers would normally maintain the records under usual or customary business practices.

ii. Least Burdensome Option or Explanation Required

The Department believes it has chosen the most effective option that updates and clarifies the rule and which results in the least burden. Among the options considered by the Department, the least restrictive option was taking no regulatory action. Taking no regulatory action does not address the Department's concerns discussed above under Objectives of, and Need for, the Final Rule. Pursuant to section 603(c) of the RFA, the following alternatives are to be addressed:

Differing compliance or reporting requirements that take into account the resources available to small entities. The FLSA creates a level playing field for businesses by setting a floor below which employers may not pay their employees. To establish differing compliance or reporting requirements for small businesses would undermine this important purpose of the FLSA and appears unnecessary given the small annualized cost of the rule. The Year 1 cost of the proposed rule for the average employer that qualifies as small was estimated to range from a minimum of 1,700 (accommodation industry) to a maximum of 31,100 (textile, apparel, and leather manufacturing), using the upper-bound estimates. The Department makes available a variety of resources to employers for understanding their obligations and achieving compliance. Therefore, the Department has not proposed differing compliance or reporting requirements for small businesses.

The clarification, consolidation, or simplification of compliance and reporting requirements for small entities. This final rule imposes no new reporting requirements. The Department makes available a variety of resources to employers for understanding their obligations and achieving compliance.

The use of performance rather than design standards. Under this final rule, employers may achieve compliance through a variety of means. Employers may elect to continue to claim the EAP exemption for affected employees by adjusting salary levels, hire additional workers or spread overtime hours to other employees, or compensate employees for overtime hours worked. The Department makes available a variety of resources to employers for understanding their obligations and achieving compliance.

An exemption from coverage of the rule, or any part thereof, for such small entities. Creating an exemption from coverage of this rule for businesses with as many as 500 employees, those defined as small businesses under SBA's size standards, is inconsistent with the FLSA, which applies to all employers that satisfy the enterprise coverage threshold or employ individually covered employees, regardless of employer size.[257]

G. Identification, to the Extent Practicable, of all Relevant Federal Rules That May Duplicate, Overlap, or Conflict With the Final Rule

The Department is not aware of any federal rules that duplicate, overlap, or conflict with this final rule.

VIII. Unfunded Mandates Reform Act Analysis

The Unfunded Mandates Reform Act of 1995 (UMRA),[258] requires agencies to prepare a written statement for rules for which a final rulemaking was published and that include any federal mandate that may result in increased expenditures by state, local, and tribal governments, in the aggregate, or by the private sector, of $165 million ($100 million in 1995 dollars adjusted for inflation to 2018) or more in at least one year. This statement must: (1) Identify the authorizing legislation; (2) present the estimated costs and benefits of the rule and, to the extent that such estimates are feasible and relevant, its estimated effects on the national economy; (3) summarize and evaluate state, local, and tribal government input; and (4) identify reasonable alternatives and select, or explain the non-selection, of the least costly, most cost-effective, or least burdensome alternative.

A. Authorizing Legislation

This final rule is issued pursuant to section 13(a)(1) of the Fair Labor Standards Act (FLSA or Act), 29 U.S.C. 213(a)(1). The section exempts from the FLSA's minimum wage and overtime pay requirements ''any employee employed in a bona fide executive, administrative, or professional capacity (including any employee employed in the capacity of academic administrative personnel or teacher in elementary or secondary schools), or in the capacity of outside salesman (as such terms are defined and delimited from time to time by regulations of the Secretary, subject to the provisions of [the Administrative Procedure Act] . . .).'' [259] The requirements of the exemption are contained in part 541 of the Department's regulations. Section 3(e) of the FLSA [260] defines ''employee'' to include most individuals employed by a state, political subdivision of a state, or interstate governmental agency. Section 3(x) of the FLSA [261] also defines public agencies to include the government of a state or political subdivision thereof, or any interstate governmental agency.

B. Assessment of Costs and Benefits

For purposes of the UMRA, this rule includes a federal mandate that is expected to result in increased expenditures by the private sector of more than $165 million in at least one year, but the rule will not result in increased expenditures by state, local and tribal governments, in the aggregate, of $165 million or more in any one year.

Costs to state and local governments: Based on the economic impact analysis of this final rule, the Department determined that the final rule will result in Year 1 costs for state and local governments totaling $52.1 million, of which $21.7 million are direct employer costs and $30.4 million are payroll increases (Table 37). In subsequent years, the Department estimated that state and local governments may experience payroll increases of as much as $49.0 million per year.

[256] 84 FR 10914 (internal citation omitted).

[257] *See* 29 U.S.C. 203(s).

[258] 2 U.S.C. 1501 *et seq.*

[259] 29 U.S.C. 213(a)(1).

[260] 29 U.S.C. 203(e).

[261] 29 U.S.C. 203(x).

Costs to the private sector: The Department determined that the final rule will result in Year 1 costs to the private sector of approximately $887.0 million, of which $521.0 million are direct employer costs and $366.0 million are payroll increases. In subsequent years, the Department estimated that the private sector may experience a payroll increase of as much as $284.2 million per year.

TABLE 37—SUMMARY OF YEAR 1 AFFECTED EAP WORKERS, REGULATORY COSTS, AND TRANSFERS BY TYPE OF EMPLOYER

	Total	Private	Government [a]
Affected EAP Workers (1,000s)			
Number	1,257	1,125	128
Direct Employer Costs (Millions)			
Regulatory familiarization	$340.4	$336.5	$3.9
Adjustment	68.2	61.0	7.0
Managerial	134.4	123.5	10.9
Total direct costs	543.0	521.0	21.7
Payroll Increases (Millions)			
From employers to workers	$396.4	$366.0	$30.4
Direct Employer Costs & Transfers (Millions)			
From employers	$939.4	$887.0	$52.1

[a] Includes only state, local, and tribal governments.

UMRA requires agencies to estimate the effect of a regulation on the national economy if, at its discretion, such estimates are reasonably feasible and the effect is relevant and material.[262] However, OMB guidance on this requirement notes that such macro-economic effects tend to be measurable in nationwide econometric models only if the economic effect of the regulation reaches 0.25 percent to 0.5 percent of GDP, or in the range of $51.2 billion to $102.5 billion (using 2018 GDP). A regulation with a smaller aggregate effect is not likely to have a measurable effect in macro-economic terms unless it is highly focused on a particular geographic region or economic sector, which is not the case with this final rule.

The Department's RIA estimates that the total first-year costs (direct employer costs and payroll increases from employers to workers) of the final rule will be approximately $887.0 million for private employers and $52.1 million for state and local governments. Given OMB's guidance, the Department has determined that a full macro-economic analysis is not likely to show any measurable effect on the economy. Therefore, these costs are compared to payroll costs and revenue to demonstrate the feasibility of adapting to these new rules.

Total first-year private sector costs compose 0.013 percent of private sector payrolls nationwide.[263] Total private sector first-year costs compose 0.002 percent of national private sector revenues (revenues in 2018 are projected to be $40.9 trillion).[264] The Department concludes that effects of this magnitude are affordable and will not result in significant disruptions to typical firms in any of the major industry categories.

Total first-year state and local government costs compose less than 0.01 percent of state and local government payrolls.[265] First-year state and local government costs compose 0.001 percent of state and local government revenues (projected 2018 revenues were estimated to be $3.7 trillion).[266] Effects of this magnitude will not result in significant disruptions to typical state and local governments. The $52.1 million in state and local government costs constitutes an average of approximately $578 for each of the approximately 90,126 state and local entities. The Department considers effects of this magnitude to be quite small both in absolute terms and in relation to payrolls and revenue.

C. Response to Comments

i. Consultation Prior to Issuance of the NPRM

On July 26, 2017, the Department published an RFI to gather information to aid in formulating a proposal to revise the part 541 regulations. Later, between September 7 and October 17, 2018, the Department held listening sessions in all five Wage and Hour regions throughout the country, and in Washington, DC, to supplement feedback received as part of the RFI. A wide variety of state and local government entities filed comments in response to the 2017 RFI and/or participated in the 2018 listening sessions, and the Department took their views into consideration in drafting the NPRM published earlier this year. Although several tribal governments submitted comments in response to the Department's 2015 NPRM, *see* 81 FR 32547–48, no tribal governments participated in response to the 2017 RFI or 2018 listening sessions.

[262] 2 U.S.C. 1532(a)(4).

[263] Private sector payroll costs nationwide are projected to be $6.8 trillion in 2018. This projection is based on private sector payroll costs in 2012, which were $5.3 trillion using the 2012 Economic Census of the United States. This was inflated to 2018 dollars using the GDP deflator.

[264] Private sector revenues in 2012 were $32.3 trillion using the 2012 Economic Census of the United States. This was inflated to 2018 dollars using the GDP deflator.

[265] State and local payrolls in 2016 were reported as $927.9 billion. This was inflated to 2018 payroll costs of $1,016.5 billion using the CPI–U. State and Local Government Finances Summary: FY2016. Available at *https://www.census.gov/govs/local/.*

[266] State and local revenues in 2016 were reported as $3.4 trillion. This was inflated to 2018 dollars using the CPI–U. State and Local Government Finances Summary: FY2016. Available at *https://www.census.gov/govs/local/.*

ii. Comments Received in Response to the NPRM

The Department received comments from a variety of commenters representing state and local governments, including from some elected officials.[267] These comments presented a range of views on the proposed rule, particularly the proposed increase to the standard salary level threshold. Some commenters, like the Public Housing Authorities Directors Association (PHADA), supported the proposed rule, agreeing that an update to the standard salary level is ''long overdue'' and finding the proposed increase preferable to the higher threshold adopted in the 2016 final rule. *See also* Joint Comment of the International Public Management Association for Human Resources (IPMA–HR), the International City/County Management Association (ICMA), and the Government Finance Officers Association (GFOA). Other commenters, like the Idaho Division of Human Resources (IDHR), the National Association of Counties (NACo), and the South Butler Community Library, expressed concern about the impact of any increase to the standard salary level, including from the proposed increase. While IDHR and NACo agreed that the proposed rule would be preferable to the 2016 final rule, each criticized the Department's preference for a uniform standard salary level that, they stated, would disproportionately impact employers operating in lower-income states and counties. Others representing certain state governments, however, opposed the proposed rule on the grounds that they would prefer a significantly higher standard salary level, such as the one adopted under the 2016 final rule. *See* House and Senate Democratic Caucuses of the Michigan Legislature; Michigan Governor Gretchen Whitmer; Pennsylvania Department of Labor & Industry; State AGs; Washington Governor Jay Inslee; Wisconsin Department of Workforce Development. These comments echoed many of the same criticisms of the proposed salary level levied by employee advocates discussed earlier in section IV.A.v, but the State AGs made an additional point (relevant for UMRA purposes) that a low federal threshold burdens state governments with expensive law enforcement responsibilities to protect workers in their states from unlawful misclassification. The State AGs asserted that state governments are reluctant to set their own higher exemption thresholds for fear of ''creating uneven standards for employment and [risking] competition with neighboring states.''

As explained earlier in section IV.A, the Department agrees with the overwhelming majority of commenters that an increase to the $455 per week standard salary level currently being enforced is both necessary and overdue. While the adoption of any nationwide earning threshold has a disproportionate impact on employers operating in lower-income regions and industries, the Department believes that adopting multiple salary levels that vary by region would introduce confusion and compliance costs for employers (or employees) operating across different jurisdictions. By contrast, the Department concludes that reapplying the 2004 final rule's methodology to set the standard salary level appropriately accommodates employers operating in low-wage regions.[268]

Some state and local government commenters opined on other aspects of the proposed rule. For example, NACo endorsed the Department's proposal to permit nondiscretionary bonuses and incentive payments (including commissions) to satisfy up to 10 percent of the standard salary level test; this proposal has been finalized as proposed. The joint comment submitted by IPMA–HR, ICMA, and the GFOA objected to the NPRM's proposed increase to the total annual compensation threshold for highly compensated employees, asserting that the proposed threshold of $147,414 per year ''would render the highly compensated employee exemption almost meaningless, especially for smaller governmental organizations in certain parts of the country.'' As explained in section IV.D, the Department has finalized a lower increase to the HCE threshold, to $107,432 per year, which addresses such concerns.

State and local government commenters disagreed over how the Department should update the earnings thresholds going forward. Some commenters urged the Department to adopt a mechanism to automatically update the standard salary level and HCE total compensation levels, which they viewed as critical for ensuring that the effectiveness of the earnings thresholds does not erode over time. *See* House and Senate Democratic Caucuses of the Michigan Legislature; Michigan Governor Gretchen Whitmer; State AGs; Washington Governor Jay Insee; Wisconsin Department of Workforce Development. By contrast, NACo, PHADA, and the joint comment submitted by IPMA–HR, ICMA, and the GFOA supported the Department's proposed commitment to update the earnings thresholds using notice-and-comment rulemaking every four years. As explained in section IV.E, in this final rule the Department reaffirms its intent to update the standard salary level and HCE total annual compensation threshold more regularly in the future using notice-and-comment rulemaking.

Finally, IDHR requested a delayed effective date of at least 18 months, asserting that ''[p]ublic entities, like the State [of Idaho], require sufficient time in the [budgeting] and legislative processes to address appropriations or to make statutory changes to existing state law affected by a federal law amendment.'' As explained in section II.E, the Department has set an effective date of January 1, 2020, for the final rule. The time between this rule's publication and effective date exceeds the 30-day minimum required under the Administrative Procedure Act (APA), 5 U.S.C. 553(d), and the 60 days mandated for a ''major rule'' under the Congressional Review Act, 5 U.S.C. 801(a)(3)(A). Given that the Department is currently enforcing the 2004 standard salary level, which an overwhelming majority of commenters agreed needs to be updated, the Department concludes that a lengthier delayed effective date would be imprudent.

D. Least Burdensome Option or Explanation Required

This final rule has described the Department's consideration of various options throughout the preamble and economic impact analysis (*see* section VI.C). The Department believes that it has chosen the least burdensome but still cost-effective methodology to update the salary level consistent with the Department's statutory obligation. Although some alternative options considered would have set the standard salary level at a rate lower than the updated salary level, that outcome would not necessarily be the most cost-effective or least-burdensome alternative for employers. A lower or outdated salary level would result in a less effective bright-line test for separating workers who may be exempt from those nonexempt workers intended to be

[267] As in response to the RFI, the Department did not receive any comments from tribal governments or affiliated stakeholders in response to the NPRM.

[268] IDHR and the joint comment submitted by IPMA–HR, ICMA, and the GFOA requested that the Department permit employers to prorate the salary level for part-time employees. As explained earlier, *see supra* n.72, the Department declines this request, emphasizing that the standard salary level is not an annual earnings threshold and that ''[e]xempt employees need not be paid for any workweek in which they perform no work.'' 29 CFR 541.602(a)(1).

within the Act's protection. A low salary level would also increase the burden on the employer to apply the duties test to more employees in determining whether an employee is exempt, which would inherently increase the likelihood of misclassification and, in turn, increase the risk that employees who should receive overtime and minimum wage protections under the FLSA are denied those protections.

Selecting a standard salary level inevitably affects both the risk and cost of misclassification of overtime-eligible employees earning above the salary level, as well as the risk and cost of providing overtime protection to employees performing bona fide EAP duties who are paid below the salary level. An unduly low level risks increasing employer liability from unintentionally misclassifying workers as exempt; but an unduly high standard salary level increases labor costs to employers precluded from claiming the exemption for employees performing bona fide EAP duties. Thus, the ultimate cost of the regulation is increased if the standard salary level is set either too low or too high. The Department determined that setting the standard salary level equivalent to the earnings of the 20th percentile of full-time salaried workers in the South and/or in the retail industry balances the risks and costs of misclassification of exempt status.

IX. Executive Order 13132, Federalism

The Department has (1) reviewed this final rule in accordance with Executive Order 13132 regarding federalism and (2) determined that it does not have federalism implications.

X. Executive Order 13175, Indian Tribal Governments

This final rule would not have substantial direct effects on one or more Indian tribes, on the relationship between the Federal Government and Indian tribes, or on the distribution of power and responsibilities between the Federal Government and Indian tribes.

List of Subjects in 29 CFR Part 541

Labor, Minimum wages, Overtime pay, Salaries, Teachers, Wages.

Signed at Washington, DC, this 16th day of September, 2019.

Cheryl M. Stanton,

Administrator, Wage and Hour Division.

For the reasons set out in the preamble, the Department of Labor amends title 29 of the Code of Federal Regulations part 541 as follows:

PART 541—DEFINING AND DELIMITING THE EXEMPTIONS FOR EXECUTIVE, ADMINISTRATIVE, PROFESSIONAL, COMPUTER AND OUTSIDE SALES EMPLOYEES

■ 1. The authority citation for part 541 continues to read as follows:

Authority: 29 U.S.C. 213; Pub. L. 101–583, 104 Stat. 2871; Reorganization Plan No. 6 of 1950 (3 CFR, 1945–53 Comp., p. 1004); Secretary's Order 01–2014 (Dec. 19, 2014), 79 FR 77527 (Dec. 24, 2014).

■ 2. In § 541.100, revise paragraph (a)(1) to read as follows:

§ 541.100 General rule for executive employees.

(a) * * *

(1) Compensated on a salary basis pursuant to § 541.600 at a rate of not less than $684 per week (or $455 per week if employed in the Commonwealth of the Northern Mariana Islands, Guam, Puerto Rico, or the U.S. Virgin Islands by employers other than the Federal government, or $380 per week if employed in American Samoa by employers other than the Federal government), exclusive of board, lodging or other facilities;

* * * * *

■ 3. In § 541.200, revise paragraph (a)(1) to read as follows:

§ 541.200 General rule for administrative employees.

(a) * * *

(1) Compensated on a salary or fee basis pursuant to § 541.600 at a rate of not less than $684 per week (or $455 per week if employed in the Commonwealth of the Northern Mariana Islands, Guam, Puerto Rico, or the U.S. Virgin Islands by employers other than the Federal government, or $380 per week if employed in American Samoa by employers other than the Federal government), exclusive of board, lodging or other facilities;

* * * * *

■ 4. In § 541.204, revise paragraph (a)(1) to read as follows:

§ 541.204 Educational establishments.

(a) * * *

(1) Compensated on a salary or fee basis at a rate of not less than $684 per week (or $455 per week if employed in the Commonwealth of the Northern Mariana Islands, Guam, Puerto Rico, or the U.S. Virgin Islands by employers other than the Federal government, or $380 per week if employed in American Samoa by employers other than the Federal government), exclusive of board, lodging, or other facilities; or on a salary basis which is at least equal to the entrance salary for teachers in the educational establishment by which employed; and

* * * * *

■ 5. In § 541.300, revise paragraph (a)(1) to read as follows:

§ 541.300 General rule for professional employees.

(a) * * *

(1) Compensated on a salary or fee basis pursuant to § 541.600 at a rate of not less than $684 per week (or $455 per week if employed in the Commonwealth of the Northern Mariana Islands, Guam, Puerto Rico, or the U.S. Virgin Islands by employers other than the Federal government, or $380 per week if employed in American Samoa by employers other than the Federal government), exclusive of board, lodging or other facilities; and

* * * * *

■ 6. Amend § 541.400 by removing the first two sentences of paragraph (b) and adding one sentence in their place to read as follows:

§ 541.400 General rule for computer employees.

* * * * *

(b) The section 13(a)(1) exemption applies to any computer employee who is compensated on a salary or fee basis at a rate of not less than $684 per week (or $455 per week if employed in the Commonwealth of the Northern Mariana Islands, Guam, Puerto Rico, or the U.S. Virgin Islands by employers other than the Federal government, or $380 per week if employed in American Samoa by employers other than the Federal government), exclusive of board, lodging, or other facilities. * * *

* * * * *

■ 7. Amend § 541.600 by:

■ a. Removing the first three sentences of paragraph (a) and adding one sentence in their place; and

■ b. Revising paragraph (b).

The revisions and additions read as follows:

§ 541.600 Amount of salary required.

(a) To qualify as an exempt executive, administrative or professional employee under section 13(a)(1) of the Act, an employee must be compensated on a salary basis at a rate of not less than $684 per week (or $455 per week if employed in the Commonwealth of the Northern Mariana Islands, Guam, Puerto Rico, or the U.S. Virgin Islands by employers other than the Federal Government, or $380 per week if employed in American Samoa by employers other than the Federal Government), exclusive of board, lodging or other facilities. * * *

(b) The required amount of compensation per week may be translated into equivalent amounts for periods longer than one week. For example, the $684-per-week requirement will be met if the employee is compensated biweekly on a salary basis of not less than $1,368, semimonthly on a salary basis of not less than $1,482, or monthly on a salary basis of not less than $2,964. However, the shortest period of payment that will meet this compensation requirement is one week.

* * * * *

■ 8. Amend § 541.601 by revising paragraphs (a) and (b) to read as follows:

§ 541.601 Highly compensated employees.

(a)(1) Beginning on January 1, 2020, an employee with total annual compensation of at least $107,432 is deemed exempt under section 13(a)(1) of the Act if the employee customarily and regularly performs any one or more of the exempt duties or responsibilities of an executive, administrative or professional employee as identified in subparts B, C or D of this part.

(2) Where the annual period covers periods both prior to and after January 1, 2020, the amount of total annual compensation due will be determined on a proportional basis.

(b)(1) ''Total annual compensation'' must include at least $684 per week paid on a salary or fee basis as set forth in §§ 541.602 and 541.605, except that § 541.602(a)(3) shall not apply to highly compensated employees. Total annual compensation may also include commissions, nondiscretionary bonuses and other nondiscretionary compensation earned during a 52-week period. Total annual compensation does not include board, lodging and other facilities as defined in § 541.606, and does not include payments for medical insurance, payments for life insurance, contributions to retirement plans and the cost of other fringe benefits.

(2) If an employee's total annual compensation does not total at least the amount specified in the applicable subsection of paragraph (a) by the last pay period of the 52-week period, the employer may, during the last pay period or within one month after the end of the 52-week period, make one final payment sufficient to achieve the required level. For example, for a 52-week period beginning January 1, 2020, an employee may earn $90,000 in base salary, and the employer may anticipate based upon past sales that the employee also will earn $17,432 in commissions. However, due to poor sales in the final quarter of the year, the employee actually only earns $12,000 in commissions. In this situation, the employer may within one month after the end of the year make a payment of at least $5,432 to the employee. Any such final payment made after the end of the 52-week period may count only toward the prior year's total annual compensation and not toward the total annual compensation in the year it was paid. If the employer fails to make such a payment, the employee does not qualify as a highly compensated employee, but may still qualify as exempt under subparts B, C, or D of this part.

* * * * *

■ 9. In § 541.602, revise paragraph (a)(3) to read as follows:

§ 541.602 Salary basis.

(a) * * *

(3) Up to ten percent of the salary amount required by § 541.600(a) may be satisfied by the payment of nondiscretionary bonuses, incentives and commissions, that are paid annually or more frequently. The employer may utilize any 52-week period as the year, such as a calendar year, a fiscal year, or an anniversary of hire year. If the employer does not identify some other year period in advance, the calendar year will apply. This provision does not apply to highly compensated employees under § 541.601.

(i) If by the last pay period of the 52-week period the sum of the employee's weekly salary plus nondiscretionary bonus, incentive, and commission payments received is less than 52 times the weekly salary amount required by § 541.600(a), the employer may make one final payment sufficient to achieve the required level no later than the next pay period after the end of the year. Any such final payment made after the end of the 52-week period may count only toward the prior year's salary amount and not toward the salary amount in the year it was paid.

(ii) An employee who does not work a full 52-week period for the employer, either because the employee is newly hired after the beginning of this period or ends the employment before the end of this period, may qualify for exemption if the employee receives a *pro rata* portion of the minimum amount established in paragraph (a)(3) of this section, based upon the number of weeks that the employee will be or has been employed. An employer may make one final payment as under paragraph (a)(3)(i) of this section within one pay period after the end of employment.

* * * * *

■ 10. Revise § 541.604 to read as follows:

§ 541.604 Minimum guarantee plus extras.

(a) An employer may provide an exempt employee with additional compensation without losing the exemption or violating the salary basis requirement, if the employment arrangement also includes a guarantee of at least the minimum weekly-required amount paid on a salary basis. Thus, for example, an exempt employee guaranteed at least $684 each week paid on a salary basis may also receive additional compensation of a one percent commission on sales. An exempt employee also may receive a percentage of the sales or profits of the employer if the employment arrangement also includes a guarantee of at least $684 each week paid on a salary basis. Similarly, the exemption is not lost if an exempt employee who is guaranteed at least $684 each week paid on a salary basis also receives additional compensation based on hours worked for work beyond the normal workweek. Such additional compensation may be paid on any basis (*e.g.,* flat sum, bonus payment, straight-time hourly amount, time and one-half or any other basis), and may include paid time off.

(b) An exempt employee's earnings may be computed on an hourly, a daily or a shift basis, without losing the exemption or violating the salary basis requirement, if the employment arrangement also includes a guarantee of at least the minimum weekly required amount paid on a salary basis regardless of the number of hours, days or shifts worked, and a reasonable relationship exists between the guaranteed amount and the amount actually earned. The reasonable relationship test will be met if the weekly guarantee is roughly equivalent to the employee's usual earnings at the assigned hourly, daily or shift rate for the employee's normal scheduled workweek. Thus, for example, an exempt employee guaranteed compensation of at least $725 for any week in which the employee performs any work, and who normally works four or five shifts each week, may be paid $210 per shift without violating the $684-per-week salary basis requirement. The reasonable relationship requirement applies only if the employee's pay is computed on an hourly, daily or shift basis. It does not apply, for example, to an exempt store manager paid a guaranteed salary per week that exceeds the current salary level who also receives a commission of one-half percent of all sales in the store or five percent of the store's profits, which in some weeks may total as much as, or even more than, the guaranteed salary.

■ 11. In § 541.605, revise paragraph (b) to read as follows:

§ 541.605 Fee basis.

* * * * *

(b) To determine whether the fee payment meets the minimum amount of salary required for exemption under these regulations, the amount paid to the employee will be tested by determining the time worked on the job and whether the fee payment is at a rate that would amount to at least the minimum salary per week, as required by §§ 541.600(a) and 541.602(a), if the employee worked 40 hours. Thus, an artist paid $350 for a picture that took 20 hours to complete meets the $684 minimum salary requirement for exemption since earnings at this rate would yield the artist $700 if 40 hours were worked.

■ 12. Amend § 541.709 by revising the first sentence to read as follows:

§ 541.709 Motion picture producing industry.

The requirement that the employee be paid ''on a salary basis'' does not apply to an employee in the motion picture producing industry who is compensated at a base rate of at least $1,043 per week (exclusive of board, lodging, or other facilities). * * *

* * * * *

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