DEPARTMENT OF LABOR

Wage and Hour Division

29 CFR Part 541

RIN 1235-AA11

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 Fair Labor Standards Act (FLSA or Act) guarantees a minimum wage for all hours worked during the workweek and overtime premium pay of not less than one and one-half times the employee's regular rate of pay for hours worked over 40 in a workweek. While these protections extend to most workers, the FLSA does provide a number of exemptions. In this Final Rule, the Department of Labor (Department) revises final regulations under the FLSA implementing the exemption from minimum wage and overtime pay for executive, administrative, professional, outside sales, and computer employees. These exemptions are frequently referred to as the "EAP" or "white collar" exemptions. To be considered exempt under part 541, employees must meet certain minimum requirements related to their primary job duties and, in most instances, must be paid on a salary basis at not less than the minimum amounts specified in the regulations.

In this Final Rule the Department updates the standard salary level and total annual compensation requirements to more effectively distinguish between overtime-eligible white collar employees and those who may be exempt, thereby making the exemption easier for

employers and employees to understand and ensuring that the FLSA's intended overtime protections are fully implemented. The Department sets the standard salary level for exempt EAP employees at the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region. The Department also permits employers to satisfy up to 10 percent of the standard salary requirement with nondiscretionary bonuses, incentive payments, and commissions, provided these forms of compensation are paid at least quarterly. The Department sets the total annual compensation requirement for an exempt Highly Compensated Employee (HCE) equal to the annualized weekly earnings of the 90th percentile of full-time salaried workers nationally. The Department also adds a provision to the regulations that automatically updates the standard salary level and HCE compensation requirements every three years by maintaining the earnings percentiles set in this Final Rule to prevent these thresholds from becoming outdated. Finally, the Department has not made any changes in this Final Rule to the duties tests for the EAP exemption.

DATES: This Final Rule is effective on December 1, 2016.

FOR FURTHER INFORMATION CONTACT: Director, Division of Regulations, Legislation and Interpretation, U.S. Department of Labor, Wage and Hour Division, Room S-3502, 200 Constitution Avenue, N.W., Washington, D.C. 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 Wage and Hour Division (WHD) district office. Locate the nearest office by calling

the 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 at http://www.dol.gov/whd/america2.htm for a nationwide listing of WHD district and area offices.

SUPPLEMENTARY INFORMATION:

Table of Contents

I. Executive Summary

The Fair Labor Standards Act (FLSA or Act) guarantees a minimum wage for all hours worked and limits to 40 hours per week the number of hours an employee can work without additional compensation. Section 13(a)(1) of the FLSA, which was included in the original Act in 1938, exempts from these minimum wage and overtime pay protections "any employee employed in a bona fide executive, administrative, or professional capacity." The exemption is premised on the belief that these kinds of workers typically earn salaries well above the minimum wage and enjoy other privileges, including above-average fringe benefits, greater job security, and better opportunities for advancement, setting them apart from workers entitled to overtime pay. The statute delegates to the Secretary of Labor the authority to define and delimit the terms of the exemption.

The Department has undertaken this rulemaking in order to revise the regulations so that they effectively distinguish between overtime-eligible white collar employees who Congress intended to be protected by the FLSA's minimum wage and overtime provisions and bona fide EAP employees whom it intended to exempt. When the definition becomes outdated, employees who Congress intended to protect receive neither the higher salaries and above-average benefits expected for EAP employees nor do they receive overtime pay, and employers do not have an efficient means of identifying workers who are, and are not, entitled to the FLSA's protections. With this Final Rule, the Department will ensure that white collar employees who should receive extra pay for overtime hours will do so and that the test for exemption remains up-to-date so future workers will not be denied the protections that Congress intended to afford them.

In 1938, the Department issued the first regulations at 29 CFR part 541 defining the scope of the section 13(a)(1) white collar exemption. Since 1940, the regulations implementing the exemption have generally required each of three tests to be met for the exemption to apply: (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"). While payment of a salary does not make an employee ineligible for overtime compensation, the Department has nonetheless long recognized the salary level test is the best single test of exempt status for white collar employees. The salary level test is an objective measure that helps distinguish white collar employees who are entitled to overtime from those who may be bona fide executive, administrative, or professional (EAP) employees. If left at the same amount over time, however, the effectiveness of the salary level test as a means of determining exempt status diminishes as the wages of employees increase and the real value of the salary threshold falls.

The Department has updated the salary level requirements seven times since 1938, most recently in 2004 when the salary level an employee must be paid to come within the standard test for EAP exemption was set at $455 per week ($23,660 per year for a full-year worker), which nearly tripled the $155 per week minimum salary level required for exemption up to that point. The Department also modified the duties tests in 2004, eliminating the "long" and "short" tests that had been part of the regulations since 1949 and replacing them with the "standard" test. The historic long test paired a lower salary requirement with a stringent duties test including a 20 percent cap on the amount of time most exempt employees could spend on nonexempt duties, while the short test paired a higher salary requirement with a less stringent duties test. In other words, prior to the 2004 Final Rule, to exempt lower-paid employees from receiving overtime the employer would have to meet more rigorous requirements; but for higher-paid employees,

the requirements to establish the applicability of the exemption were less rigorous. The standard test established by the Department in the 2004 Final Rule paired a duties test closely based on the less-stringent short duties test with a salary level derived from the lower long test salary level. This had the effect of making it easier for employers to both pay employees a lower salary and not pay them overtime for time worked beyond 40 hours. The 2004 Final Rule also created an exemption for highly compensated employees (HCE), which imposes a very minimal duties test but requires that an employee must earn at least $100,000 in total annual compensation.

On March 13, 2014, President Obama signed a Presidential Memorandum directing the Department to update the regulations defining which white collar workers are protected by the FLSA's minimum wage and overtime standards. 79 FR 18737 (Apr. 3, 2014). The memorandum instructed the Department to look for ways to modernize and simplify the regulations while ensuring that the FLSA's intended overtime protections are fully implemented. The Department published a proposal to update the part 541 regulations on July 6, 2015.

One of the Department's primary goals in this rulemaking is updating the standard salary requirement, both in light of the passage of time since 2004, and because the Department has concluded that the effect of the 2004 Final Rule's pairing of a standard duties test based on the less rigorous short duties test with the kind of low salary level previously associated with the more rigorous long duties test was to exempt from overtime many lower paid workers who performed little EAP work and whose work was otherwise indistinguishable from their overtime-eligible colleagues. This has resulted in the inappropriate classification of employees as EAP exempt—that is overtime exempt—who pass the standard duties test but would have failed the long duties test. As the Department noted in our proposal, the salary level's function in helping to differentiate overtime-eligible employees from employees who may be exempt takes on

greater importance when the duties test does not include a specific limit on the amount of nonexempt works that an exempt employee may perform.

In the Notice of Proposed Rulemaking (NPRM), the Department proposed setting the standard salary level at the 40th percentile of weekly earnings of full-time salaried workers nationally and setting the HCE total annual compensation requirement at the annualized value of the 90th percentile of weekly earnings of full-time salaried workers nationally. The Department further proposed to automatically update these levels annually to ensure that they would continue to provide an effective test for exemption. In the NPRM, the Department also asked for the public's comments on whether nondiscretionary bonuses or incentive payments should count toward some portion of the required salary level. Finally, the Department also discussed concerns with the standard duties tests and sought comments on a series of questions regarding possible changes to the tests.

After considering the comments, the Department has made several changes from the proposed rule to the Final Rule. In particular, the Department has modified the standard salary level to more fully account for the lower salaries paid in certain regions. In this Final Rule, the Department sets the standard salary level equal to the 40th percentile of earnings of full-time salaried workers in the lowest-wage Census Region (currently the South). This results in a salary level of $913 per week, or $47,476 annually for a full-year worker, based on data from the fourth quarter of 2015.[1] The Department believes that a standard salary level set at the 40th percentile of full-time salaried employees in the lowest-wage Census Region will accomplish the goal of

[1] The Bureau of Labor Statistics (BLS) estimated this value using Current Population Survey (CPS) data for earnings of full-time (defined as at least 35 hours per week) non-hourly paid employees. For the purpose of this rulemaking, the Department considers data representing compensation paid to non-hourly workers to be an appropriate proxy for compensation paid to salaried workers.

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 90th percentile of earnings of full-time salaried workers nationally ($134,004 annually based on the fourth quarter of 2015), as we proposed. This increase will bring the annual compensation requirement in line with the level established in 2004. The Department believes that this will avoid the unintended exemption of large numbers of employees in high-wage areas—such as secretaries in New York City or Los Angeles—who are clearly not performing EAP duties.

In order to prevent the salary and compensation levels from becoming outdated, the Department is including in the regulations a mechanism to automatically update the salary and compensation thresholds by maintaining the fixed percentiles of weekly earnings set in this Final Rule. In response to comments, however, the Final Rule provides for updates every three years rather than for annual updates as proposed. The first update will take effect on January 1, 2020. The Department believes that regularly updating the salary and compensation levels is the best method to ensure that these tests continue to provide an effective means of distinguishing between overtime-eligible white collar employees and those who may be bona fide EAP employees. Based on historical wage growth in the South, at the time of the first update on January 1, 2020, the standard salary level is likely to be approximately $984 per week ($51,168 annually for a full-year worker) and the HCE total annual compensation requirement is likely to be approximately $147,524.

The Department also revises the regulations to permit employers for the first time 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 a quarterly or more frequent basis. Finally, the Department has not made any changes to the duties tests in this Final Rule. The majority of the revisions occur in §§ 541.600, 541.601, 541.602 and new § 541.607; conforming changes were also made in §§ 541.100, 541.200, 541.204, 541.300, 541.400, 541.604, 541.605, and 541.709.

In FY2017,[2] the Department estimates there will be approximately 159.9 million wage and salary workers in the United States, of whom we estimate that 22.5 million will be exempt EAP workers potentially affected by this Final Rule.[3] In Year 1, FY2017, the Department estimates that 4.2 million currently exempt workers who earn at least the current weekly salary level of $455 but less than the 40th earnings percentile in the South ($913) would, without some intervening action by their employers, become entitled to minimum wage and overtime protection under the FLSA (Table ES1). Similarly, an estimated 65,000 currently exempt workers who earn at least $100,000 but less than the annualized earnings of the 90th percentile of full-time salaried workers nationally ($134,004), and who meet the HCE duties test but not the standard duties test, may also become eligible for minimum wage and overtime protection. In Year 10, with triennial automatic updating of the salary and compensation levels, the Department projects that 5.0 million workers will be affected by the change in the standard salary level test and 221,000 workers will be affected by the change in the HCE total annual compensation test.

Additionally, the Department estimates that another 5.7 million white collar workers who are currently overtime eligible because they do not satisfy the EAP duties tests and who currently

[2] Affected workers, costs, and transfers were estimated for the 2017 fiscal year ("FY2017") because this will be the first year the updated salary levels will be in effect. FY2017 spans from October 1, 2016 to September 30, 2017.

[3] White collar workers not subject to the EAP salary level test include teachers, academic administrative personnel, physicians, lawyers, judges, and outside sales workers.

earn at least $455 per week but less than $913 per week will have their overtime protection strengthened in Year 1 because their status as overtime-eligible will be clear based on the salary test alone without the need to examine their duties. Reducing the number of workers for whom employers must apply the duties test to determine exempt status simplifies the application of the exemption and is consistent with the President's directive.

The Department quantified three direct costs to employers in this Final Rule: (1) regulatory familiarization costs; (2) adjustment costs; and (3) managerial costs. Assuming a 7 percent discount rate, the Department estimates that average annualized direct employer costs will total $295.1 million per year (Table ES1). In addition to the direct costs, this Final Rule will also transfer income from employers to employees in the form of higher earnings. We estimate average annualized transfers to be $1,189.1 million. The Department also projects average annualized deadweight loss of $9.2 million, and notes that the projected deadweight loss is small in comparison to the amount of estimated costs.

The change to a standard salary level based on the lowest-wage Census Region has decreased the salary amount from the proposal, resulting in a smaller number of affected workers and lower transfers than estimated in the NPRM. Direct costs are higher than predicted in the NPRM, primarily because the Department has increased its estimate of the number of affected workers who work some overtime. Additionally, in response to comments, the Department has increased estimated regulatory familiarization and adjustment costs in the Final Rule.

Finally, the impacts of the Final Rule extend beyond those we have estimated quantitatively. The Department discusses other transfers, costs, and benefits in the relevant sections.

Table ES1: Summary of Regulatory Costs and Transfers, Standard and HCE Salary Levels (Millions 2017$)

Impact	Year 1	Future Years [a]	Average Annualized Value

		Year 2	Year 10	3% Real Rate	7% Real Rate
Affected Workers (1,000s)					
Standard	4,163	3,893	5,045	--	--
HCE	65	73	217	--	--
Total	4,228	3,965	5,261	--	--
Costs and Transfers (Millions 2017$) [b]					
Direct employer costs	$677.9	$208.0	$284.2	$288.0	$295.1
Transfers [c]	$1,285.2	$936.5	$1,607.2	$1,201.6	$1,189.1
DWL	$6.4	$8.7	$11.1	$9.3	$9.2

[a] Costs/transfers in years 3 through 9 are within the range bounded by the estimates for years 2 and 10.
[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.

II. Background

A. What the FLSA Provides

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 one and one-half times the employee's regular rate of pay for all hours worked over 40 in a workweek.[4] 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'

[4] As discussed below, the Department estimates that 132.8 million workers are subject to the FLSA and the Department's regulations. Most of these workers are covered by the Act's minimum wage and overtime pay protections.

grant of rulemaking authority, the Department in 1938 issued the first regulations at part 541 defining the scope of the section 13(a)(1) exemptions. Because Congress explicitly delegated to the Secretary of Labor the power to define and delimit the specific terms of the exemptions through notice and comment rulemaking, regulations so issued have the binding effect of law. See Batterton v. Francis, 432 U.S. 416, 425 n.9 (1977).

The Department has consistently used our rulemaking authority to define and clarify the section 13(a)(1) exemptions. Since 1940, the implementing regulations have generally required each of three tests to be met for the exemptions to apply: (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").

Employees who meet the requirements of part 541 are exempted from both the Act's minimum wage and overtime pay protections. As a result, an employer may employ such employees for any number of hours in the workweek without paying the minimum hourly wage or an overtime premium. Some state laws have stricter exemption standards than those described above. 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.

B. Legislative History

Section 13(a)(1) was included in the original Act in 1938 and was based on provisions contained in the earlier National Industrial Recovery Act of 1933 (NIRA) and state law

precedents. Specific references in the legislative history to the exemptions contained in section 13(a)(1) are scant. Although section 13(a)(1) exempts covered employees from both the FLSA's minimum wage and overtime requirements, its most significant impact is its removal of these employees from the Act's overtime protections.

The requirement that employers pay a premium rate of pay for all hours worked over 40 in a workweek is grounded in two policy objectives. The first is to spread employment (or, in other words, reduce involuntary unemployment) by incentivizing employers to hire more employees rather than requiring existing employees to work longer hours. See, e.g., Davis v. J.P. Morgan Chase, 587 F.3d 529, 535 (2d Cir. 2009). The second policy objective is to reduce overwork and its detrimental effect on the health and well-being of workers. See, e.g., Barrentine v. Arkansas-Best Freight System, Inc., 450 U.S. 728, 739 (1981).

In contrast, the exemptions contained in section 13(a)(1) were premised on the belief that the type of work exempt employees performed was difficult to standardize to any time frame and could not be easily spread to other workers after 40 hours in a week, making enforcement of the overtime provisions difficult and generally precluding the potential job expansion intended by the FLSA's time-and-a-half overtime premium. See Report of the Minimum Wage Study Commission, Volume IV, pp. 236 and 240 (June 1981).[5] Further, the exempted workers typically earned salaries well above the minimum wage and were presumed to enjoy other privileges to compensate them for their long hours of work, setting them apart from the nonexempt workers entitled to overtime pay. See id.

[5] Congress created the Minimum Wage Study Commission as part of the Fair Labor Standards Amendments of 1977. See Sec. 2(e)(1), Pub. L. 95-151, 91 Stat. 1246 (Nov. 1, 1977). This independent commission was tasked with examining many FLSA issues, including the Act's minimum wage and overtime exemptions, and issuing a report to the President and to Congress with the results of its study.

The universe of employees eligible for the section 13(a)(1) exemptions has fluctuated with amendments to the FLSA. Initially, persons employed in a "local retailing capacity" were exempt, but Congress eliminated that language from section 13(a)(1) in 1961 when the FLSA was expanded to cover retail and service enterprises. See Pub. L. 87-30, 75 Stat. 65 (May 5, 1961). Teachers and academic administrative personnel were added to the exemption when elementary and secondary schools were made subject to the FLSA in 1966. See Sec. 214, Pub. L. 89-601, 80 Stat. 830 (Sept. 23, 1966). The Education Amendments of 1972 made the Equal Pay provisions, section 6(d) of the FLSA, expressly applicable to employees who were otherwise exempt from the FLSA under section 13(a)(1). See Sec. 906(b)(1), Pub. L. 92-318, 86 Stat. 235 (June 23, 1972).

A 1990 enactment expanded the EAP exemptions to include computer systems analysts, computer programmers, software engineers, and similarly skilled professional workers, including those paid on an hourly basis if paid at least 6½ times the minimum wage. See Sec. 2, Pub. L. 101-583, 104 Stat. 2871 (Nov. 15, 1990). The compensation test for computer-related occupations was subsequently capped at $27.63 an hour (6½ times the minimum wage in effect at the time) as part of the 1996 FLSA Amendments, when Congress enacted the new section 13(a)(17) exemption for such computer employees. Section 13(a)(17) also incorporated much of the regulatory language that resulted from the 1990 enactment. See 29 U.S.C. 213(a)(17), as added by the 1996 FLSA Amendments (Sec. 2105(a), Pub. L. 104-188, 110 Stat. 1755 (Aug. 20, 1996)).

C. Regulatory History

The FLSA became law on June 25, 1938, and the Department issued the first version of the part 541 regulations, setting forth criteria for exempt status under section 13(a)(1), that October.

3 FR 2518 (Oct. 20, 1938). Following a series of public hearings, which were discussed in a report issued by WHD,[6] the Department published revised regulations in 1940, which, among other things, added the salary basis test. 5 FR 4077 (Oct. 15, 1940). Further hearings were convened in 1947, as discussed in a WHD-issued report,[7] and the Department issued revised regulations in 1949, which updated the salary levels required to meet the salary level test for the various exemptions. 14 FR 7705 (Dec. 24, 1949). An explanatory bulletin interpreting some of the terms used in the regulations was published as subpart B of part 541 in 1949. 14 FR 7730 (Dec. 28, 1949). In 1954, the Department issued revisions to the regulatory interpretations of the salary basis test. 19 FR 4405 (July 17, 1954). In 1958, based on another WHD-issued report,[8] the regulations were revised to update the required salary levels. 23 FR 8962 (Nov. 18, 1958). Additional changes, including salary level updates, were made to the regulations in 1961 (26 FR 8635, Sept. 15, 1961), 1963 (28 FR 9505, Aug. 30, 1963), 1967 (32 FR 7823, May 30, 1967), 1970 (35 FR 883, Jan. 22, 1970), 1973 (38 FR 11390, May 7, 1973), and 1975 (40 FR 7091, Feb. 19, 1975). Revisions to increase the salary levels in 1981 were stayed indefinitely by the Department. 46 FR 11972 (Feb. 12, 1981). In 1985, the Department published an Advance Notice of Proposed Rulemaking that reopened the comment period on the 1981 proposal and broadened the review to all aspects of the regulations, including whether to increase the salary levels, but this rulemaking was never finalized. 50 FR 47696 (Nov. 19, 1985).

---

[6] 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").

[7] 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").

[8] Report and Recommendations on Proposed Revision of Regulations, Part 541, Under the Fair Labor Standards Act, by Harry S. Kantor, Presiding Officer, Wage and Hour and Public Contracts Divisions, U.S. Department of Labor (Mar. 3, 1958) ("Kantor Report").

The Department revised the part 541 regulations twice in 1992. First, the Department created a limited exception from the salary basis test for public employees, permitting public employers to follow public sector pay and leave systems requiring partial-day deductions from pay for absences for personal reasons or due to illness or injury not covered by accrued paid leave, or due to budget-driven furloughs, without defeating the salary basis test required for exemption. 57 FR 37677 (Aug. 19, 1992). The Department also implemented the 1990 law requiring it to promulgate regulations permitting employees in certain computer-related occupations to qualify as exempt under section 13(a)(1) of the FLSA. 57 FR 46744 (Oct. 9, 1992); see Sec. 2, Pub. L. 101-583, 104 Stat. 2871 (Nov. 15, 1990).

On March 31, 2003, the Department published a Notice of Proposed Rulemaking proposing significant changes to the part 541 regulations. 68 FR 15560 (Mar. 31, 2003). On April 23, 2004, the Department issued a Final Rule (2004 Final Rule), which raised the salary level for the first time since 1975, and made other changes, some of which are discussed below. 69 FR 22122 (Apr. 23, 2004). Current regulations retain the three tests for exempt status that have been in effect since 1940: a salary basis test, a salary level test, and a job duties test.

D. Overview of Existing Regulatory Requirements

The regulations in part 541 contain specific criteria that define each category of exemption provided by section 13(a)(1) for bona fide executive, administrative, and professional employees (including teachers and academic administrative personnel), and outside sales employees. The regulations also define those computer employees who are exempt under section 13(a)(1) and section 13(a)(17). See §§ 541.400-.402. The employer bears the burden of establishing the applicability of any exemption from the FLSA's pay requirements. Job titles and job descriptions do not determine exempt status, nor does paying a salary rather than an hourly rate.

To qualify for the EAP exemption, employees must meet certain tests regarding their job duties and generally must be paid on a salary basis of not less than $455 per week.[9] In order for the exemption to apply, an employee's specific job duties and salary must meet all the requirements of the Department's regulations. The duties tests differ for each category of exemption.

The Department last updated the part 541 regulations in the 2004 Final Rule. Prior to 2004, employers could assert the EAP exemption for employees who satisfied either a "long" test—which paired a more restrictive duties test with a lower salary level—or a "short" test—which paired less stringent duties requirements with a higher salary level.[10] In the 2004 Final Rule the Department abandoned the concept of separate long and short tests, opting instead for one "standard" test, and set the salary level under the new standard duties test at $455 per week for executive, administrative, and professional employees.

Under the current part 541 regulations, an exempt executive employee must be compensated on a salary basis at a rate of not less than $455 per week and have a primary duty of managing the enterprise or a department or subdivision of the enterprise. See § 541.100(a)(1)-(2). An exempt executive must also customarily and regularly direct the work of at least two employees and have the authority to hire or fire, or the employee's suggestions and recommendations as to

[9] Alternatively, administrative and professional employees may be paid on a "fee basis." This occurs where an employee is paid an agreed sum for a single job regardless of the time required for its completion. See § 541.605(a). Salary level test compliance for fee basis employees is assessed by determining whether the hourly rate for work performed (i.e., the fee payment divided by the number of hours worked) would total at least $455 per week if the employee worked 40 hours. See § 541.605(b). Some employees, such as doctors and lawyers (§ 541.600(e)), teachers (§§ 541.303(d); 541.600(e)), and outside sales employees (§ 541.500(c)), are not subject to a salary or fee basis test. Some, such as academic administrative personnel, are subject to a special, contingent salary level. See § 541.600(c). There is also a separate salary level in effect for workers in American Samoa (§ 541.600(a)), and a special salary test for motion picture industry employees (§ 541.709).

[10] From 1949 until 2004 the regulations contained both long and short tests for exemption.

the hiring, firing, or other change of status of employees must be given particular weight. See § 541.100(a)(3)-(4).

An exempt administrative employee must be compensated on a salary or fee basis at a rate of not less than $455 per week and have a primary duty of the performance of office or non-manual work directly related to the management or general business operations of the employer or the employer's customers. See § 541.200. An exempt administrative employee's primary duty must include the exercise of discretion and independent judgment with respect to matters of significance. See id.

An exempt professional employee must be compensated on a salary or fee basis at a rate of not less than $455 per week and have a primary duty of (1) work requiring knowledge of an advanced type in a field of science or learning customarily acquired by prolonged, specialized, intellectual instruction and study, or (2) work that is original and creative in a recognized field of artistic endeavor, or (3) teaching in a school system or educational institution, or (4) work as a computer systems analyst, computer programmer, software engineer, or other similarly-skilled worker in the computer field. See §§ 541.300; 541.303; 541.400. An exempt professional employee must perform work requiring the consistent exercise of discretion and judgment, or requiring invention, imagination, or talent in a recognized field of artistic endeavor. See § 541.300(a)(2). The salary requirements do not apply to certain licensed or certified doctors, lawyers, and teachers. See §§ 541.303(d); 541.304(d).

An exempt outside salesperson must be customarily and regularly engaged away from the employer's place of business and have a primary duty of making sales, or obtaining orders or contracts for services or for the use of facilities. See § 541.500. There are no salary or fee requirements for exempt outside sales employees. See id.

The 2004 Final Rule also created a test for exemption of highly compensated executive, administrative, and professional employees. Under the HCE exemption, 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 exempt duties or responsibilities of an executive, administrative, or professional employee identified in the standard tests for exemption. See § 541.601. The HCE exemption applies only to employees whose primary duty includes performing office or non-manual work; non-management production line workers and employees who perform work involving repetitive operations with their hands, physical skill, and energy are not exempt under this section no matter how highly paid. See id. Finally, in the 2004 Final Rule, the Department, mindful that nearly 30 years had elapsed between salary level increases, and in response to commenter concerns that similar lapses would occur in the future, expressed an intent to "update the salary levels on a more regular basis." 69 FR 22171.

E. Presidential Memorandum

On March 13, 2014, President Obama signed a Presidential Memorandum directing the Department to update the regulations defining which "white collar'' workers are protected by the FLSA's minimum wage and overtime standards. See 79 FR 18737 (Apr. 3, 2014). The memorandum instructed the Department to look for ways to modernize and simplify the regulations while ensuring that the FLSA's intended overtime protections are fully implemented. As the President noted at the time, the FLSA's overtime protections are a linchpin of the middle class, and the failure to keep the salary level requirement for the white collar exemption up to

date has left millions of low-paid salaried workers without this basic protection.[11] The current salary level threshold for exemption of $455 per week, or $23,660 annually, is below the 2015 poverty threshold for a family of four.[12]

Following issuance of the memorandum, the Department embarked on an extensive outreach program, meeting with over 200 organizations in Washington, D.C. and several other locations, as well as by conference call. A wide range of stakeholders attended the listening sessions: employees, employers, business associations, non-profit organizations, employee advocates, unions, state and local government representatives, tribal representatives, and small businesses. In these sessions the Department asked stakeholders to address, among other issues: (1) what is the appropriate salary level for exemption; (2) what, if any, changes should be made to the duties tests; and (3) how can the regulations be simplified.

The stakeholders shared their concerns with various aspects of the current regulations, suggestions for changes, and general concerns about the scope of the exemption. The Department greatly appreciated the wide range of views that were shared during the outreach sessions. The information shared during those sessions informed the Department's NPRM.

The Department's outreach also made clear, however, that there are some widespread misconceptions about overtime eligibility under the FLSA, some of which were echoed in the comments received on the NPRM. For example, many employers and employees mistakenly believe that payment of a salary automatically disqualifies an employee from entitlement to overtime compensation irrespective of the duties performed. Many employees are also unaware

---

[11] See http://www.whitehouse.gov/the-press-office/2014/03/13/fact-sheet-opportunity-all-rewarding-hard-work-strengthening-overtime-pr.

[12] See http://www.census.gov/hhes/www/poverty/data/threshld/index.html (the 2015 poverty threshold for a family of four with two related children). The 2015 poverty threshold for a family of four with two related people under 18 in the household is $24,036.

of the duties required to be performed in order for the exemption to apply. Additionally, many employers seem to mistakenly believe that newly overtime-eligible employees (i.e., those earning between the current and new salary levels) must be converted to hourly compensation.[13] Similarly, some employers erroneously believe that they are prohibited from paying nondiscretionary bonuses to EAP employees, given that they cannot be used to satisfy the salary requirement. Some employers also mistakenly believe that the EAP regulations limit their ability to permit white collar employees to work part-time or job share.[14]

F. The Department's Proposal

On July 6, 2015, in accordance with the Presidential Memorandum, the Department published a Notice of Proposed Rulemaking to propose revisions to the part 541 regulations. See 80 FR 38516 (July 6, 2015). The Department's proposal focused primarily on updating the salary and HCE compensation levels by proposing that the standard salary level be set at the 40th percentile of weekly earnings of full-time salaried workers, proposing to increase the HCE annual compensation requirement to the annualized value of the 90th percentile of weekly earnings of full-time salaried workers, and proposing a mechanism for automatically updating the salary and

[13] Such misconceptions are not new. In 1949 the Department noted "the failure of some employers to realize that salary is not the sole test of exemption." Weiss Report at 8 n.27. In 1940 the Department responded to the assertion that employers would convert overtime-eligible white collar employees to hourly pay instead of more secure salaries, stating: "Without underestimating the general desirability of weekly or monthly salaries which enable employees to adjust their expenditures on the basis of an assured income (so long as they remain employed), there is little advantage in salaried employment if it serves merely as a cloak for long hours of work. Further, such salaried employment may well conceal excessively low hourly rates of pay." Stein Report at 7.

[14] As the Department has previously explained, there is no special salary level for EAP employees working less than full-time. See 69 FR 22171. Employers, however, can pay white collar employees working part-time or job sharing a salary of less than the required EAP salary threshold and will not violate the Act so long as the salary equals at least the minimum wage for all hours worked and the employee does not work more than 40 hours a week. See FLSA2008-1NA (Feb. 14, 2008). See also section IV.A.iv.

compensation levels going forward to ensure that they will continue to provide a useful and effective test for exemption. While the primary regulatory changes proposed were in §§ 541.600 and 541.601, the Department proposed additional conforming changes to update references to the salary level throughout part 541 as well as to update the special salary provisions for American Samoa and the motion picture industry. In addition to these proposed changes, the Department also discussed whether to include nondiscretionary bonuses in determining whether the standard salary level is met and whether changes to the duties tests are warranted, but did not propose specific regulatory revisions on these issues.

More than 270,000 individuals and organizations timely commented on the NPRM during the sixty-day comment period that ended on September 4, 2015. The Department received comments from a broad array of constituencies, including small business owners, Fortune 500 corporations, 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, federal government agencies, state and local governments and representatives, tribal governments and representatives, professional associations, and other interested members of the public. All timely received comments may be viewed on the www.regulations.gov website, docket ID WHD-2015-0001.

Several organizations' submissions included attachments from their individual members generally using substantively identical form comments: for example, AFSCME (24,122 comments), Center for American Progress (6,697 comments from two submissions), CREDO Action (58,927 comments), Democracy for America (34,932 comments), Economic Policy Institute (72,131 comments from five submissions), Faculty Forward and SEIU (515

comments), Jobs with Justice (5,136 comments), Mom's Rising (16,114 comments from three submissions), National Partnership for Women and Families (21,192 comments from two submissions), National Restaurant Association (2,648 comments), National Women's Law Center (6,753 comments from two submissions), Partnership to Protect Workplace Opportunity (1,770 comments from five submissions), Social Security Works (15,575 comments), Society for Human Resource Management (827 comments from two submissions), and others. Other organizations attached membership signatures to their comments. These included Care2 (37,459 signatures), the International Franchise Association (17 signatures), Organizing for Action (76,625 signatures), and 15 different post-doctoral associations (560 signatures).

Many of the comments the Department received were: (1) very general statements of support or opposition; (2) personal anecdotes that did not address a specific aspect of the proposed changes; or (3) identical or nearly identical "campaign" comments sent in response to comment initiatives sponsored by various groups. A large number of commenters favored some change to the existing regulations, and commenters expressed a wide variety of views on the merits of particular aspects of the Department's proposal. Some commenters requested that the Department withdraw the proposal. Acknowledging that there are strong views on the issues presented in this rulemaking, the Department has carefully considered the timely submitted comments addressing the proposed changes.

Significant issues raised in the timely received comments are discussed below, together with the Department's response to those comments and a topical discussion of the changes that have been made in the Final Rule and its regulatory text. The Department also received a number of submissions after the close of the comment period, including some campaign comments, from a range of commenters representing both employers and employees. Late comments were not

considered in the development of this Final Rule, and are not discussed in this Final Rule. In instances where an organization submitted both timely and untimely comments, only the timely comments were considered.

The Department received a number of comments that are beyond the scope of this rulemaking. These include, for example, comments asking the Department to issue a rule requiring employers to provide employees with "clear pay stubs," and requesting that the Department clarify the definition of "establishment" under the exemption for seasonal amusement or recreational establishments. The Department does not address such issues 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., Alliance for Strong Families and Communities (describing "a tremendous amount of confusion in the non-profit sector concerning who is currently covered by FLSA"); Independent Sector (stating that this rulemaking process has "highlighted a lack of clarity regarding when and how the Fair Labor Standards Act applies to the nonprofit sector workforce"); Alliance of Arizona Nonprofits. Some commenters, such as CASA, asserted that most charitable organizations are not covered enterprises under the FLSA and, as a result, this rulemaking "will not reach a very sizable number of employees of not-for-profit organizations." Other commenters stated that non-profit employees may be individually covered because they engage in interstate commerce. A comment submitted on behalf of 57 professors specializing in employment and labor law, however, asserted that the "overwhelming majority of the millions of employees excluded from FLSA coverage because their not-for-profit employers are not subject to enterprise coverage also are not subject to individual FLSA coverage," and Economic Policy Institute (EPI) asserted that non-profit employers can limit the number of employees covered on an individual basis by managing interstate commerce activity.

The Department notes that the FLSA does not provide special rules for non-profit organizations or their employees, nor does this Final Rule. Nevertheless, we agree that it is important for such organizations to understand their obligations under the Act. As a general matter, non-profit charitable organizations are not covered enterprises under the FLSA unless they engage in ordinary commercial activities (for example, operating a gift shop). See 29 U.S.C. 203(r)-(s), 206(a), 207(a). For a non-profit organization, enterprise coverage applies only to the activities performed for a business purpose; it does not extend to the organization's charitable activities. An organization that performs only charitable services, such as providing free food to the hungry, is not a covered enterprise; however, an employee of such a non-profit employer may nevertheless be covered on an individual basis. See 29 U.S.C. 206(a), 207(a). The FLSA covers an employee on an individual basis—that is, an individual is protected by the FLSA regardless of whether the individual works for a covered enterprise—if he or she engages in interstate commerce through activities such as making out-of-state phone calls, sending mail, or handling credit card transactions. This individual coverage applies even if the employee is not engaging in such activities for a business purpose. For example, if an employee regularly calls an out-of-state store and uses a credit card to purchase food for a non-profit that provides free meals for the homeless, that employee is protected by the FLSA on an individual basis, even though the non-profit may not be covered as an enterprise. WHD, however, will not assert that an employee who on isolated occasions spends an insubstantial amount of time performing such work is individually covered by the FLSA.

The Department also refers interested stakeholders to guidance on the application of the FLSA to non-profit organizations available in WHD Fact Sheet #14A: Non-Profit Organizations and

the Fair Labor Standards Act;[15] see also Fact Sheet #14: Coverage Under the Fair Labor Standards Act (FLSA).[16] Additional information regarding the applicability of the FLSA to non-profits can be found in the WHD Administrator's blog post.[17] Moreover, a number of WHD Opinion Letters address the applicability of the FLSA to non-profits. See, e.g., FLSA2009-20 (Jan. 16, 2009); FLSA2008-8 (Sept. 29, 2008); FLSA2005-52 (Nov. 14, 2005); FLSA2005-8NA (Sept. 2, 2005); FLSA2005-12NA (Sept. 23, 2005); FLSA2004-29NA (Nov. 30, 2004).[18] Finally, the Department is issuing additional guidance for the non-profit sector in connection with the publication of this Final Rule.

Commenters also asked for guidance on the application of the EAP exemption to educational institutions. See, e.g., College and Universities Human Resources Executives; Michigan Head Start; Savannah-Chatham County Public School System. Preschools, elementary and secondary schools, and institutions of higher education are covered by the FLSA, and nothing in this Final Rule changes that coverage. 29 U.S.C. 203(r)(2)(A). Employees of such institutions therefore are generally protected by the FLSA's minimum wage and overtime provisions; however, special provisions apply to many personnel at these institutions that make them overtime exempt.

Although the EAP exemption expressly applies to an "employee employed in the capacity of academic administrative personnel or teacher" 29 U.S.C. 213(a)(1); see §§ 541.204, .303, the salary level and salary basis requirements do not apply to bona fide teachers. § 541.303(d), .600(e). Accordingly, the increase in the standard salary level in this Final Rule will not affect the overtime eligibility of bona fide teachers.

---

[15] Available at: http://www.dol.gov/whd/regs/compliance/whdfs14a.pdf.
[16] Available at: http://www.dol.gov/whd/regs/compliance/whdfs14.pdf.
[17] Available at: http://blog.dol.gov/2015/08/26/non-profits-and-the-proposed-overtime-rule/.
[18] Available at: http://www.dol.gov/whd/opinion/flsa.htm; http://www.dol.gov/whd/opinion/flsana.htm .

Commenters such as the NEA asked the Department to clarify which workers qualify as bona fide teachers. Teachers are exempt if their primary duty is teaching, tutoring, instructing or lecturing in the activity of imparting knowledge, and if they are employed and engaged in this activity as a teacher in an educational establishment. § 541.303(a). An educational establishment is "an elementary or secondary school system, an institution of higher education or other educational institution."[19] § 541.204(b). Teachers may include professors, adjunct instructors, primary and secondary school teachers, and teachers of skilled and semi-skilled trades and occupations. Preschool and kindergarten teachers may also qualify for exemption under the same conditions as teachers in elementary and secondary schools. See Fact Sheet #46: Daycare Centers and Preschools Under the Fair Labor Standards Act. In addition, coaches may qualify for the exemption if their primary duty is teaching as opposed to recruiting students to play sports or performing manual labor. Some commenters addressed other non-teaching staff. For example, CUPA-HR commented about workers including academic affairs counselors and advisors, textbook managers, and managers in food service, security, and building and grounds, among other employees working at colleges and universities. Academic administrative personnel subject to the exemption include: superintendents; principals and vice-principals; department heads in institutions of higher education; academic counselors and advisors; and other employees with similar responsibilities. Academic administrative employees are subject to the salary basis requirement, but the Department notes that a special provision allows this requirement to be met if such employees are paid "on a salary basis which is at least equal to the entrance salary for teachers in the educational establishment by which [they are] employed." § 541.204(a)(1). To the extent that this entrance salary is below the salary level established in this

[19] For purposes of the exemption, no distinction is drawn between public and private schools, or between those operated for profit and those that are not for profit. § 541.204(b).

rule, academic administrative personnel will be exempt if their salary equals or exceeds the entrance salary. Employees whose work relates to general business operations, building management and maintenance, or the health of students and staff (such as lunch room managers), do not perform academic administrative functions. § 541.204(c).

The Department also received several comments about postdoctoral scholars. See, e.g., Association of American Medical Colleges; National Postdoctoral Association; UAW Local 5810. Postdoctoral scholars who do not have a primary duty of teaching are not considered bona fide teachers; these employees would generally meet the duties test for the learned professional exemption and would be subject to the salary basis and salary level tests.

Finally, the Council on Government Relations commented that "it is our understanding that the Wage and Hour Division does not assert an employee-employer relationship for graduate students who are simultaneously performing research under faculty supervision." The Department views graduate students in a graduate school engaged in research under the supervision of a member of the faculty and in the course of obtaining advanced degrees as being in an educational relationship and not in an employment relationship with either the school or of any grantor funding the research, even though the student may receive a stipend for performing the research. 1994 WL 1004845 (June 28, 1994). In an effort to assist the educational sector with the issues addressed above, the Department is issuing additional guidance for this sector in connection with the publication of this Final Rule.

Lastly, in an attempt to address concerns that the terms exempt and nonexempt were not sufficiently descriptive or intuitive, in the NPRM the Department used the terms "overtime-protected" and "overtime-eligible" as synonyms for nonexempt, and "not overtime-protected"

and "overtime-ineligible" as synonyms for exempt.[20] The Department received very few comments on this new terminology. The Department believes that these new terms are less confusing to the public and continues to use them in this Final Rule.

G. Effective Date

The Department received a number of comments concerning the effective date of the Final Rule. Citing the need to reduce the burden of implementation, many commenters representing employers requested a delayed effective date following publication of the Final Rule. Commenters including the Fisher & Phillips law firm, the National Association of Independent Schools and the National Association of Business Officers, requested an effective date at least 120 days after publication as was done in the Department's 2004 rulemaking.

Other commenters requested a longer period. The American Car Rental Association (ACRA), Dollar Tree, and the Retail Industry Leaders Association (RILA) each requested a delayed effective date of at least six months following publication of the Final Rule. The United States Chamber of Commerce (Chamber), the Food Marketing Institute (FMI), H-E-B, Island Hospitality Management, the National Association of Landscape Professionals (NALP), the National Council of Chain Restaurants (NCCR), the National Retail Federation (NRF), and the Securities Industry and Financial Markets Association (SIFMA) each requested a one-year delayed effective date. Finally, Laff and Associates, the National Association for Home Care and Hospice, and American Network of Community Options and Resources (ANCOR), which coordinated with more than three dozen home health care organizations, submitted comments requesting an effective date at least two years following publication of the Final Rule, to afford states sufficient time to allocate and appropriate funding.

[20] The Department is using the more precise term "overtime exempt" rather than "overtime-ineligible" in this Final Rule.

More than 55,000 individuals submitted comments coordinated by the Center for American Progress, EPI, and MomsRising, requesting that the salary level be raised without delay. Many labor organizations and social justice and women's advocacy organizations, including the Center for Law and Social Policy, the Center for Popular Democracy, the First Shift Justice Project, the Institute for Women's Policy Research (IWPR), the Leadership Conference on Civil and Human Rights, the National Education Association (NEA), the National Coalition of Classified Education Support Employees Union, the National Urban League, the Public Justice Center, the United Automobile, Aerospace and Agricultural Implement Workers of America (UAW), Women Employed, and others, similarly urged the Department to implement the Final Rule as soon as possible.

The Department has set an effective date of December 1, 2016 for the Final Rule. As several commenters noted, the Department's 2004 Final Rule set an effective date 120 days following publication of the final rule. See 79 FR 22126 (April 23, 2004). Explaining that a 120-day 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), we concluded at that time that "a period of 120 days after the date of publication will provide employers ample time to ensure compliance with the final regulations." Id. The changes provided in the 2004 Final Rule were more extensive and more complicated for employers to implement—the 2004 Final Rule included several significant changes: (1) a significant percentage increase in the salary threshold; (2) a significant 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 light of the Department's

decision not to make changes to the standard duties test at this time, the primary change in this Final Rule is the revision to the salary level test and, therefore, this rule will be much less complicated for employers to implement. Accordingly, the Department believes that the December 1, 2016 effective date for this Final Rule (more than 180 days after publication) will provide ample time for employers to ensure compliance.

Multiple commenters also requested a delayed enforcement period or some form of safe harbor following the effective date of the Final Rule ranging from six months to two years. See, e.g., ACRA; American Insurance Association and the Property Casualty Insurers Association of America (AIA-PCI); AT&T; Chamber; Dollar Tree; International Franchise Association (IFA); the Littler Mendelson law firm; RILA; the Wessels Sherman law firm; World Travel. Several commenters also asked the Department to provide compliance assistance, whether related specifically to the changes implemented by the Final Rule or more broadly to the FLSA's white collar regulations in general. See, e.g., Chamber; Dollar Tree; IFA; Littler Mendelson; RILA.

The Department appreciates employer concerns regarding compliance and enforcement in light of this rulemaking. As explained above, the Department believes that the December 1, 2016 effective date will provide employers ample time to make any changes that are necessary to comply with the final regulations. 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

One of the Department's primary goals in this rulemaking is updating the section 13(a)(1) exemption's standard salary level requirement. A salary level test has been part of the regulations since 1938 and has been long recognized as "the best single test" of exempt status.

Stein Report at 19, 42; see Weiss Report at 8-9; Kantor Report at 2-3. The salary an employer pays an employee provides "a valuable and easily applied index to the 'bona fide' character of the employment for which exemption is claimed" and ensures that section 13(a)(1) of the FLSA "will not invite evasion of section 6 [minimum wage] and section 7 [overtime] for large numbers of workers to whom the wage-and-hour provisions should apply." Stein Report at 19.

The salary level's function in differentiating exempt from overtime-eligible employees takes on greater importance when there is only one duties test that has no limitation on the amount of nonexempt work that an exempt employee may perform, as has been the case since 2004. Historically, the Department set two different salary tests that were paired with different duties tests. The long test salary level set at the low end of salaries paid to exempt employees imposed a cap on the amount of nonexempt work that an exempt employee could perform. This aspect of the long duties test made it effective in distinguishing lower-paid exempt EAP employees from overtime-eligible employees. In effect, the long duties test ensured that employers could not avoid paying overtime by assigning lower-paid employees a minimal amount of exempt work. The short test salary level, which was historically set at a level between 130 and 180 percent of the long test salary level, did not impose any specific limit on the amount of nonexempt work since that distinction was not considered necessary to aid in classifying higher-paid exempt EAP employees. In eliminating the two salary tests in 2004, the Department instead set the single standard salary level equivalent to the historic levels of the former long test salary, but paired it with a standard duties test based on the short duties test, which did not include a limit on nonexempt work. The effect of this mismatch was to exempt from overtime many lower-wage workers who performed little EAP work and whose work was otherwise indistinguishable from their overtime-eligible colleagues.

The Department has now concluded that the standard salary level we set in 2004 did not account for the absence of the more rigorous long duties test and thus has been less effective in distinguishing between EAP employees who are exempt from overtime and overtime-eligible employees. Additionally, the salary level required for exemption under section 13(a)(1) is currently $455 a week and has not been updated in more than 10 years. The annual value of the salary level ($23,660) is now lower than the poverty threshold for a family of four. As the relationship between the current standard salary level and the poverty threshold shows, the effectiveness of the salary level test as a means of helping determine exempt status diminishes as the wages of employees entitled to overtime pay increase and the real value of the salary threshold falls.

By way of this rulemaking, the Department seeks to update the standard salary level to ensure that it works effectively with the standard duties test to distinguish exempt EAP employees from overtime-protected white collar workers. This will make the exemptions easier for employers and workers to understand and ensure that the FLSA's intended overtime protections are fully implemented. The Department also proposed to update the total annual compensation required for the HCE exemption, because it too has been unchanged since 2004 and must be updated to avoid the unintended exemption of employees in high-wage areas who are clearly not performing EAP duties.

In a further effort to respond to changing conditions in the workplace, the Department's proposal also requested comment on whether to allow nondiscretionary bonuses and incentive payments to satisfy some portion of the standard test salary requirement. Currently, such bonuses are only included in calculating total annual compensation under the HCE test, but some

stakeholders have urged broader inclusion, pointing out that in some industries significant portions of salaried EAP employees' earnings may be in the form of such bonuses.

The Department also proposed automatically updating the salary and compensation levels to prevent the levels from becoming outdated. The Department proposed to automatically update the standard salary test, the total annual compensation requirement for highly compensated employees, and the special salary levels for American Samoa and for motion picture industry employees, in order to ensure the continued utility of these tests over time. As the Department explained in 1949, the salary test is only a strong measure of exempt status if it is up to date, and a weakness of the salary test is that increases in wage rates and salary levels over time gradually diminish its effectiveness. See Weiss Report at 8. A rule providing for automatic updates to the salary level using a consistent methodology that has been subject to notice and comment rulemaking will maintain the utility of the dividing line set by the salary level without the need for frequent rulemaking. This modernization of the regulations will provide predictability for employers and employees by replacing infrequent, and thus more drastic, salary level increases with gradual changes occurring at set intervals.

Finally, the Department has always recognized that the salary level test works in tandem with the duties tests to identify bona fide EAP employees. The Department discussed concerns with the duties test for executive employees in the NPRM. The proposal also included questions about the duties tests including requiring exempt employees to spend a specified amount of time performing their primary duty (e.g., a 50 percent primary duty requirement as required under California state law) or otherwise limiting the amount of nonexempt work an exempt employee may perform, and adding to the regulations additional examples illustrating how the exemption may apply to particular occupations. The Department's proposal sought feedback on whether

such revisions to the duties tests are needed to ensure that these tests fully reflect the purpose of the exemption.

IV. Final Regulatory Revisions

A. Standard Salary Level

i. History of the Standard Salary Level

The FLSA became law on June 25, 1938, and the first version of part 541, issued later that year, set a minimum salary level of $30 per week for exempt executive and administrative employees. See 3 FR 2518. Since 1938, the Department has increased the salary levels seven times: in 1940, 1949, 1958, 1963, 1970, 1975, and 2004. See Table A. While the Department has refined the method for calculating the salary level to fulfill its mandate, the purpose of the salary level requirement has remained consistent—to define and delimit the scope of the executive, administrative, and professional exemptions. See 29 U.S.C. 213(a)(1). The Department has long recognized that the salary paid to an employee is the "best single test" of exempt status, Stein Report at 19, and that the salary level test furnishes a "completely objective and precise measure which is not subject to differences of opinion or variations in judgment." Weiss Report at 8-9. The Department reaffirmed this position in the 2004 Final Rule, explaining that the "salary level test is intended to help distinguish bona fide executive, administrative, and professional employees from those who were not intended by Congress to come within these exempt categories," and reiterating that any increase in the salary level must "have as its primary objective the drawing of a line separating exempt from nonexempt employees." 69 FR 22165.

Table A: Weekly Salary Levels for Exemption

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			

In 1940, the Department maintained the $30 per week salary level set in 1938 for executive employees, increased the salary level for administrative employees, and established a salary level for professional employees. The Department used salary surveys from federal and state government agencies, experience gained under the National Industrial Recovery Act, and federal government salaries to determine the salary level that was the "dividing line" between employees performing exempt and nonexempt work. See Stein Report at 9, 20-21, 31-32. The Department recognized that the salary level falls within a continuum of salaries that overlaps the outer boundaries of exempt and nonexempt employees. Specifically, the Department stated:

> To make enforcement possible and to provide for equity in competition, a rate should be selected in each of the three definitions which will be reasonable in the light of average conditions for industry as a whole. In some instances the rate selected will inevitably deny exemption to a few employees who might not unreasonably be exempted, but, conversely, in other instances it will undoubtedly permit the exemption of some persons who should properly be entitled to the benefits of the act.

Id. at 6. Taking into account the average salary levels for employees in numerous industries, and the percentage of employees earning below these amounts, the Department set the salary level for each exemption slightly below the "dividing line" suggested by these averages.

In 1949, the Department again looked at salary data from state and federal agencies, including the Bureau of Labor Statistics (BLS). The data reviewed included wages in small towns and low-wage industries, earnings 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. See Weiss Report at 10, 14-17, 19-20. The Department noted that the "salary level adopted must exclude the great bulk of nonexempt persons if it is to be effective." Id. at 18. 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 calculated the percentage increase in weekly earnings from 1940 to 1949, and then adopted new salary levels "at a figure slightly lower than might be indicated by the data" in order to protect small businesses. Id. at 8, 14. The Department also cautioned that "a dividing line cannot be drawn with great precision but can at best be only approximate." Id. at 11.

Also in 1949, the Department established a second, less-stringent duties test for each exemption, but only for those employees paid at or above a higher "short test" salary level. Those paid above the higher salary level were exempt if they also met a "short" duties test, which lessened the duties requirements for exemption.[21] The original, more thorough duties test became known as the "long" test, and remained for more than 50 years the test employers were required to satisfy for those employees whose salary was insufficient to meet the higher short test salary level. Apart from the differing salary requirements, the most significant difference between the short test and the long test was the long test's limit on the amount of time an exempt employee could spend on nonexempt duties while allowing the employer to claim the exemption. A bright-line, 20 percent cap on nonexempt work was instituted as part of the long duties test in 1940 for executive and professional employees, and in 1949 for administrative employees.[22] The

[21] These higher salary levels are presented under the "Short Test" heading in Table A.
[22] 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).

short duties tests did not include a specific limit on nonexempt work.[23] The rationale for the less rigorous short duties test was that employees who met the higher salary level were more likely to meet "all the requirements for exemption . . . including the requirement with respect to nonexempt work." Id. at 22-23. Thus, a "short-cut test for exemption . . . would facilitate the administration of the regulations without defeating the purposes of section 13(a)(1)." Id.

In contrast to the Department's extensive discussion of the methodology for setting the long test salary level, the Department's rulemakings have included comparatively little discussion of the methodology for setting the short test levels. While the Department set the long test salary level based on an analysis of the defined sample, we set the short test salary level in relation to the long test salary, and the initial short test salary set in 1949 was 133 percent of the highest long test salary (administrative and professional). In 1958, the Department rejected the suggestion that the short test salary level should be increased by the same dollar amount that the highest long test salary levels were increased and instead increased the short test salary to maintain the "percentage differential in relation to the highest [long test] salary requirement." See Kantor Report at 10. In 1970, the Department adopted a "slightly higher percentage

[23] For example, the long duties test in effect from 1949 to 2004 for administrative employees required that an exempt employee: (1) have a primary duty consisting of the performance of office or non-manual work directly related to management policies or general business operations of the employer or the employer's customers; (2) customarily and regularly exercise discretion and independent judgment; (3) regularly and directly assist a proprietor or a bona fide executive or administrative employee, or perform under only general supervision work along specialized or technical lines requiring special training, experience, or knowledge, or execute under only general supervision special assignments and tasks; and (4) not devote more than 20 percent (or 40 percent in a retail or service establishment) of hours worked in the workweek to activities that are not directly and closely related to the performance of the work described above. See § 541.2 (2003). By contrast, the short duties test in effect during the 1949 to 2004 period provided that an administrative employee paid at or above the short test salary level qualified for exemption if the employee's primary duty consisted of the performance of office or non-manual work directly related to management policies or general business operations of the employer or the employer's customers which includes work requiring the exercise of discretion and independent judgment. See id.

differential" between the "basic and [short test] salary figures," than previously existed, resulting in an approximately 143 percent ratio between the highest long test salary level (professional) and the short test. 35 FR 885. From 1949 to 1975 the Department set a single short test salary level that applied to all categories of EAP employees while maintaining multiple long test salary levels that applied to the different categories. The ratio of the short test salary level to the long test salary levels ranged from approximately 130 percent to 180 percent over this period.[24] The existence of separate short and long tests remained part of the Department's regulations until 2004. See Table A.

In setting the long test salary level in 1958, the Department considered data collected during 1955 WHD investigations on the "actual salaries paid" to employees who "qualified for exemption" (i.e., 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 of white collar and manufacturing employees during the period not covered by the Department's investigations. Kantor Report at 6. 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." Id. at 6-7. In other words, the Department set the long test salary level so that only a limited number of workers performing EAP duties (about 10 percent) in the lowest-wage regions and industries would fail to meet the salary level test and therefore be overtime protected. In laying out this methodology, the Department

[24] The smallest ratio occurred in 1963 and was between the long test salary requirement for professionals ($115) and the short test salary level ($150). The largest ratio occurred in 1949 and was between the long test salary requirement for executives ($55) and the short test salary level ($100).

echoed comments from the Weiss Report that the salary tests "simplify enforcement by providing a ready method of screening out the obviously nonexempt employees," and that "[e]mployees that do not meet the salary test are generally also found not to meet the other requirements of the regulations." Id. at 2-3. The Department also noted that in our experience misclassification of overtime-protected employees occurs more frequently when the salary levels have "become outdated by a marked upward movement of wages and salaries." Id. at 5.

The Department followed a similar methodology when determining the appropriate long test salary level increase in 1963, using data regarding salaries paid to exempt workers collected in a 1961 WHD survey. See 28 FR 7002. 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 a week. See 28 FR 7004. The professional exemption 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. See id. The Department noted that these salary levels approximated the same percentages used in 1958:

> Salary tests set at this level would bear approximately the same relationship to the minimum salaries reflected in the 1961 survey data as the tests adopted in 1958, on the occasion of the last previous adjustment, bore to the minimum salaries reflected in a comparable survey, adjusted by trend data to early 1958. At that time, 10 percent of the establishments employing executive employees paid one or more executive employees less than the minimum salary adopted for executive employees and 15 percent of the establishments employing administrative or professional employees paid one or more employees employed in such capacities less than the minimum salary adopted for administrative and professional employees.

Id.

The Department continued to use a similar methodology when updating the long test salary levels in 1970. After examining data from 1968 WHD investigations, 1969 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,[25] the Department increased the long test salary level for executive employees to $125 per week when the salary 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. See 35 FR 884-85. The Department also increased the long test salary levels for administrative and professional employees to $125 and $140, respectively.

In 1975, instead of following these prior approaches, the Department set the long test salary levels based on increases in the Consumer Price Index (CPI), although the Department adjusted the salary level downward "in order to eliminate any inflationary impact." 40 FR 7091. As a result of this recalibration of the 1970 levels, the long test salary level for the executive and administrative exemptions was set at $155, while the professional level was set at $170. 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," and were not meant to set a precedent for future salary level increases. Id. at 7091-92. Although the Department intended to revise the salary levels after completion of the BLS study of actual salaries paid to employees, the envisioned process was never completed, and the "interim" salary levels remained unchanged for the next 29 years.

As reflected in Table A, the short test salary level increased in tandem with the long test level throughout the various rulemakings since 1949. Because the short test was designed to capture only those white collar employees whose salary was sufficiently high to indicate a stronger

[25] Earnings Data Pertinent to a Review of the Salary Tests for Executive, Administrative and Professional Employees As Defined in Regulations Part 541, (1969), cited in 34 FR 9935.

likelihood of exempt status and thus warrant a less stringent duties requirement, the short test salary level was always set significantly higher than the long test salary levels. Thus, in 1975 while the long test salary levels ranged from $155 to $170, the short test level was $250.

The salary level test was most recently updated in 2004, when the Department abandoned the concept of separate long and short tests, opting instead for one "standard" test, and set the salary level associated with the new standard duties test at $455 for executive, administrative, and professional employees. Due to the lapse in time between the 1975 and 2004 rulemakings, the salary threshold for the long duties tests (i.e., the lower salary level) did not reflect salaries being paid in the economy and had become ineffective at distinguishing between overtime-eligible and overtime exempt white collar employees. For example, at the time of the 2004 Final Rule, the salary levels for the long duties tests were $155 for executive and administrative employees and $170 for professional employees, while a full-time employee working 40 hours per week at the federal minimum wage ($5.15 per hour) earned $206 per week. See 69 FR 22164. Even the short test salary level at $250 per week was not far above the minimum wage.

The Department in the 2004 Final Rule based the new "standard" duties tests on the short duties tests (which did not limit the amount of nonexempt work that could be performed), and tied them to a single salary test level that was updated from the long test salary (which historically had been paired with a cap on nonexempt work). See 69 FR 22164, 22168-69; see also 68 FR 15570 ("Under the proposal, the minimum salary level to qualify for exemption from the FLSA minimum wage and overtime requirements as an executive, administrative, or professional employee would be increased from $155 per week to $425 per week. This salary level would be referred to as the 'standard test,' thus eliminating the 'short test' and 'long test' terminology."). The Department concluded that it would be burdensome to require employers to

comply with a more complicated long duties test given that the passage of time had rendered the long test salary level largely obsolete. See 69 FR 22164; 68 FR 15564-65. The Department stated at the time that the new standard test salary level accounted for the elimination of the long duties test. See 69 FR 22167.

In determining the new salary level in 2004, the Department reaffirmed our oft-repeated position that the salary level is the "best single test" of exempt status. See 69 FR 22165. Consistent with prior rulemakings, the Department relied on actual earnings data. However, instead of using salary data gathered from WHD investigations, as was done under the Kantor method, the Department used Current Population Survey (CPS) data that encompassed most salaried employees. The Department also set the salary level to exclude roughly the bottom 20 percent of these salaried employees in each of the subpopulations: (1) the South and (2) the retail industry. Thus in setting the standard salary level, the Department was consistent with our previous practice of setting the long test salary level near the lower end of the current range of salaries. Although prior long test salary levels were based on salaries of approximately the lowest 10 percent of exempt salaried employees in low-wage regions and industries (the Kantor long test method), the Department stated that the change in methodology was warranted in part to account for the elimination of the short and long duties tests, and because the utilized data sample included nonexempt salaried employees, as opposed to only exempt salaried employees. However, as the Department acknowledged, the salary arrived at by this method was, in fact, equivalent to the salary derived from the Kantor long test method. See 69 FR 22168. Based on the adopted methodology, the Department ultimately set the salary level for the new standard test at $455 per week.

In summary, the regulatory history reveals a common methodology used, with some variations, to determine appropriate salary levels. In almost every case, the Department examined a broad set of data on actual wages paid to salaried employees and then set the long test salary level at an amount slightly lower than might be indicated by the data. In 1940 and 1949, the Department set the long test salary levels by looking to the average salary paid to the lowest level of exempt employees. Beginning in 1958, the Department set the long test salary levels to exclude approximately the lowest-paid 10 percent of exempt salaried employees in low-wage regions, employment size groups, city sizes, and industry sectors, and we followed a similar methodology in 1963 and 1970. The levels were based on salaries in low-wage categories in order to protect the ability of employers in those areas and industries to utilize the exemptions and in order to mitigate the impact of salaries in higher-paid regions and sectors. In 1975, the Department increased the long test salary levels based on changes in the CPI, adjusting downward to eliminate any potential inflationary impact. See 40 FR 7091 ("However, in order to eliminate any inflationary impact, the interim rates hereinafter specified are set at a level slightly below the rates based on the CPI."). In each of these rulemakings, the Department set the short test salary level in relation to, and significantly higher than, the long test salary levels (ranging from approximately 130 to 180 percent of the long test salary levels).

In 2004, the Department eliminated the short and long duties tests in favor of a standard duties test (that was similar to the prior less rigorous short test) for each exemption and a single salary level for executive, administrative, and professional employees. This most recent revision established a standard salary level of $455 per week using earnings data of full-time salaried employees (both exempt and nonexempt) in the South and in the retail sector. As in the past, the

Department used lower-salary data sets to accommodate those businesses for which salaries were generally lower due to geographic or industry-specific reasons.

ii. Standard Salary Level Proposal

To restore the effectiveness of the salary test, in the NPRM the Department proposed to set the standard salary level equal to the 40th percentile of weekly earnings of full-time salaried workers nationally. Using salary data from 2013, the proposed methodology resulted in a standard salary level of $921 per week, or $47,892 annually. The Department estimated that, by the time of publication of a Final Rule, the proposed methodology would result in a standard salary level of approximately $970 per week, or $50,440 annually.

In proposing to update the salary threshold, the Department sought to reflect increases in actual salary levels nationwide since 2004. As the Department explained in the NPRM, when left at the same amount over time, the effectiveness of the salary level test as a means of determining exempt status diminishes as the wages of employees entitled to overtime increase and the real value of the salary threshold falls. See 80 FR 38517.

The Department also sought to adjust the salary level to address our conclusion that the salary level we set in 2004 was too low given the Department's elimination of the more rigorous long duties test. As discussed above, for many decades the long duties test—which limited the amount of time an exempt employee could spend on nonexempt duties and was paired with a lower salary level—existed in tandem with a short duties test—which did not contain a specific limit on the amount of nonexempt work and was paired with a salary level that was approximately 130 to 180 percent of the long test salary level. In 2004, the Department eliminated the long and short duties tests and created the new standard duties test, based on the short duties test. The creation of a single standard test that did not limit nonexempt work caused

new uncertainty as to what salary level is sufficient to ensure that employees intended to be overtime-protected are not subject to inappropriate classification as not overtime-protected, while minimizing the number of employees disqualified from the exemption even though their primary duty is EAP exempt work. As the Department had observed in 1975, if the salary level associated with such a test is too low, employers may use it to inappropriately classify as exempt employees who would not meet the more rigorous long duties test. 40 FR 7092 ("[T]here are indications that certain employers are utilizing the high salary test to employ otherwise nonexempt employees (i.e., those who perform work in excess of the 20 percent tolerance for nonexempt work or the 40 percent tolerance allowed in the case of executive and administrative employees in retail and service establishments) for excessively long workweeks."). Rather than pair the standard duties test with a salary level based on the higher short test salary level, however, we tied the new standard duties test to a salary level based on the long duties test. This resulted in a standard salary level that, even in 2004, was too low to effectively screen out from the exemption overtime-eligible white collar employees.

The importance of ensuring that the standard duties test is not paired with too low of a salary level is illustrated by the Department's Burger King litigation in the early 1980's, when the short and long tests were still actively in use. The Department brought two actions arguing that Burger King assistant managers were entitled to overtime protection. Sec'y of Labor v. Burger King Corp., 675 F.2d 516 (2d Cir. 1982); Sec'y of Labor v. Burger King Corp., 672 F.2d 221 (1st Cir. 1982). One group of assistant managers satisfied the higher short test salary level and was therefore subject to the less rigorous short duties test; the other group was paid less and was therefore subject to the long duties test with its limit on nonexempt work. All of the assistant managers performed the same duties, which included spending significant amounts of time

performing the same routine, nonexempt work as their subordinates. Both appellate courts found that the higher paid employees were not overtime protected—even though they performed substantial amounts of nonexempt work—because they satisfied the short duties test. The lower paid employees, however, were overtime-protected by application of the more rigorous long duties test. If the long test's lower salary threshold had been paired with a duties test that did not limit nonexempt work—as the Department did in 2004—the lower paid assistant managers would have also lost overtime protection.

In this rulemaking, the Department sought to correct the mismatch between the standard salary level (based on the old long test) and the standard duties test (based on the old short test). As we noted in the NPRM, we are concerned that at the current low salary level employees in lower-level management positions who would have failed the long duties test may be inappropriately classified as ineligible for overtime. At the same time, the Department proposed a lower salary level than the average salary traditionally used for the short duties test in order to minimize the potential that bona fide EAP employees, especially in low-wage regions and industries, might become overtime-protected because they fall below the proposed salary level. As the Department explained, an up-to-date and effective salary level protects against the misclassification of overtime-eligible workers as exempt and simplifies application of the exemption for employers and employees alike.

Consistent with prior rulemakings, the Department reached the proposed salary level after considering available data on actual salary levels currently being paid in the economy. Specifically, as we did in 2004, the Department used CPS data comprising full-time nonhourly employees to determine the proposed salary level. Unlike in the 2004 rulemaking, however, the Department did not further restrict the data by filtering out various employees based on statutory

and regulatory exclusions from FLSA coverage or the salary requirement (such as federal employees, doctors, lawyers, and teachers).

The Department proposed to set the salary level as a percentile rooted in the distribution of earnings rather than a specific dollar amount. Because earnings are linked to the type of work salaried workers perform, a percentile serves as an appropriate proxy for distinguishing between overtime-eligible and overtime exempt white collar workers. Based on the historical relationship of the short test salary level to the long test salary level, the Department determined that a salary between approximately the 35th and 55th percentiles of weekly earnings of full-time salaried workers nationwide would work appropriately with the standard duties test. The Department proposed to set the salary level at the low end of this range—the 40th percentile of weekly earnings of full-time salaried workers nationally—to account for low-wage regions and industries and for the fact that employers no longer have a long duties test to fall back on for purposes of exempting lower-salaried workers performing bona fide EAP duties. The Department explained, however, that a standard salary threshold significantly below the 40th percentile would require a more rigorous duties test than the current standard duties test in order to effectively distinguish between white collar employees who are overtime protected and those who may be bona fide EAP employees. See 80 FR 38519, 38532, 38543.

iii. Final Revisions to the Standard Salary Level

The Final Rule adopts the proposed methodology for setting the standard salary level as a percentile of actual salaries currently being paid to full-time nonhourly employees, as reported by BLS based on data obtained from the CPS. However, we have adjusted the data set used in response to a substantial number of comments asserting that the salary level proposed would render overtime-eligible too many bona fide EAP employees in low-wage areas. Rather than set

the salary level at the 40th percentile of weekly earnings of full-time salaried workers nationally, this Final Rule sets the salary level at the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region. Census Regions are groupings of states and the District of Columbia that subdivide the United States for the presentation of data by the United States Census Bureau. The current Census Regions are: the Northeast, the Midwest, the South, and the West.[26] The Department determined the "lowest-wage Census Region" by examining the 40th percentile of weekly earnings of full-time salaried workers based on CPS data in each region. For the purposes of this rulemaking, we define the "lowest-wage Census Region" as the Census Region having the lowest 40th percentile of weekly earnings of full-time salaried workers, which currently is the South.[27]

In keeping with our practice, the Department relies on the most up-to-date data available to derive the final salary level from this methodology. See 69 FR 22168. In the NPRM, the Department utilized 2013 salary data for estimating the salary level resulting from the proposed methodology, which was current at the time the Department developed the proposal. In this Final Rule, we rely on salary data from the fourth quarter of 2015, as published by BLS, to set the salary level.[28] Using this data, the Department has determined that the required standard salary level will be $913 per week, or $47,476 annually, based on the 40th percentile of weekly earnings of full-time salaried workers in the South. The $913 salary level that results from the methodology is at the low end of the historical range of short test salary levels, based on the

[26] See https://www.census.gov/geo/reference/gtc/gtc_census_divreg.html.
[27] For simplicity, in this rulemaking we refer to the lowest-wage Census Region and the South interchangeably.
[28] BLS currently publishes this data at: http://www.bls.gov/cps/research_series_earnings_nonhourly_workers.htm.

historical ratios between the short and long test salary levels ($889 - $1231). See section VI.C.iii.

White collar employees subject to the salary level test earning less than $913 per week will not qualify for the EAP exemption, and therefore will be eligible for overtime, irrespective of their job duties and responsibilities. Employees earning this amount or more on a salary or fee basis will qualify for exemption only if they meet the standard duties test, which is unchanged by this Final Rule. As a result of this increase, 4.2 million employees who meet the standard duties test will no longer fall within the EAP exemption and therefore will be overtime-protected. Additionally, 8.9 million employees paid between $455 and $913 per week who do not meet the standard duties test —5.7 million salaried white collar employees and 3.2 million salaried blue collar employees—will now face a lower risk of misclassification.

iv. Discussion of Comments

1. Proposed Increase in the Standard Salary Level

The overwhelming majority of commenters agreed that the standard salary level needs to be increased, including many commenters writing on behalf of employers, such as the Business Roundtable, Catholic Charities USA, College and University Professional Association for Human Resources (CUPA-HR), CVS Health, the National Restaurant Association (NRA), and the Northeastern Retail Lumber Association. Multiple commenters echoed the Department's observation in the NPRM that the current standard salary level of $455 per week, or $23,660 annually, is below the 2014 poverty threshold for a family of four.[29] The American Federation of Labor and Congress of Industrial Organizations (AFL-CIO) pointed out that the current salary

[29] The 2015 poverty threshold for a family of four with two related people under 18 in the household is $24,036. Available at: http://www.census.gov/hhes/www/poverty/data/threshld/index.html.

level is only slightly higher than the state minimum wage for forty hours of work in several states, and noted that it has long been widely recognized that workers whose pay is "close to the minimum wage" are "not the kind of employees Congress intended to deny overtime protection" (citing Stein Report at 5). Some salaried employees currently classified as exempt managers commented that they earn less per hour than the employees they supervise.

The Department also received multiple comments, including comments from the American Sustainable Business Council and the Heartland Alliance for Human Needs and Human Rights, expressing concern that the current salary level facilitates the misclassification of overtime-eligible employees as overtime exempt. The RAND Corporation submitted a study estimating that 11.5 percent of salaried workers are misclassified as exempt—and therefore do not receive overtime compensation—even though their primary duty is not exempt work or they earn less than the current salary level, while a human resource professional from Florida "estimate[d] that 40 percent of those employees my clients class[ify] as . . . exempt are really non-exempt."

A few commenters, however, such as the National Grocers Association (NGA), urged the Department to maintain the current salary level of $455 per week. For example, the National Lumber and Building Material Dealers Association stated that the current salary level is appropriate for managers in many sectors and regions. Mutual of Omaha requested that the Department create a "grandfathered exemption," by applying the current salary level to currently exempt employees.

The Department received a significant number of comments in response to our proposal to set the standard salary level equal to the 40th percentile of weekly earnings of full-time salaried employees nationally (estimated to be $970 per week, or $50,440 per year, in 2016). Many commenters endorsed the proposed salary level as an appropriate dividing line between

employees performing exempt and overtime-protected work, but others objected that it was either too low or too high. The majority of employees and commenters representing employees believed the proposed salary level amount was appropriate or should be increased, while the majority of employers and commenters representing them believed the salary level amount should be lower than the threshold the Department proposed.

A large number of commenters supported the proposed salary level either by explicitly endorsing the proposed increase or supporting the Department's proposed rule generally. Commenters who supported the salary level included thousands of individual employees, writing independently or as part of comment campaigns, and organizations representing employees (such as the American Association of Retired Persons (AARP), the Coalition of Labor Union Women, National Council of La Raza, the National Domestic Workers Alliance (NDWA), the National Partnership for Women & Families (Partnership), Service Employees International Union (SEIU), the United Steel, Paper and Forestry, Rubber, Manufacturing, Energy, Allied Industrial and Service Workers International Union (USW), and many others). Some employers and human resource professionals also supported the proposed increase. For example, the owner of a hardware store in Minneapolis explained that he had observed "large businesses abuse their employees for many years by misclassifying them as exempt from overtime," and stated that the Department's proposal would "help bring things back in line." H-E-B stated that it pays "competitive wages," and is "supportive of doubling the minimum salary threshold to the proposed amount of $50,400," although it urged the Department to consider making regional adjustments because other retailers pay lower wages based on geographic differences. Some Members of Congress expressed support for the Department's proposal, although other Members of Congress opposed it.

The Department received many comments from those who endorsed the proposal (as well as those seeking a higher salary level) asserting that a significant increase to the current salary level is necessary to effectuate Congress' intent to extend the FLSA's wage and hour protections broadly to most workers in the United States. See, e.g., Comment from 57 labor law professors; AFL-CIO; Equal Justice Center; National Employment Lawyers Association (NELA); Nichols Kaster law firm; SEIU. AFL-CIO stated that Congress intended the EAP exemptions to apply only to employees who have sufficient bargaining power such that they do not need the Act's protections against overwork and who perform work that cannot be easily spread to other workers. AFL-CIO and the EPI further stated that Congress knew from experience with Depression-era worker protection legislation that employers sometimes misclassified ordinary workers as managers to evade paying overtime premiums, and as a result, exempted only "bona fide" executive, administrative, and professional employees. The National Employment Law Project (NELP) commented that the Department set the salary level too low in 2004, especially when paired with a more lenient duties test than the prior long duties test. A comment submitted on behalf of 57 labor law professors noted that, even if the Department had paired the $455 per week standard salary level set in 2004 with a more rigorous duties test, it was still lower than necessary to achieve a threshold equivalent to the inflation-adjusted amount of the 1975 long test salary level.

The Department agrees with commenters that a significant increase in the salary threshold is required to ensure the FLSA's overtime protections are fully implemented. The salary level test should provide an "index to the 'bona fide' character of the employment for which exemption is claimed" and ensure that the EAP exemption "will not invite evasion" of the FLSA's minimum wage and overtime requirements "for large numbers of workers to whom the wage-and-hour

provisions should apply." Stein Report at 19. The current salary level, however, is less than the 10th percentile of weekly earnings of full-time salaried workers both nationally and in the South. The salary threshold's function in differentiating exempt from nonexempt employees takes on greater importance, moreover, when there is only one standard duties test that has no limitation on the amount of nonexempt work that an exempt employee may perform, as has been the case since 2004. As the Department has long recognized, if too low a salary level accompanies a duties test that does not limit nonexempt work, employers may utilize the salary test to employ "otherwise nonexempt employees," who perform large amounts of nonexempt work, "for excessively long workweeks." 40 FR 7092. The Department believes that the effect of the 2004 Final Rule's pairing of a standard duties test based on the short duties test (for higher paid employees) with a salary test based on the long test (for lower paid employees) was to exempt from overtime many lower paid workers who performed little EAP work and whose work was otherwise indistinguishable from their overtime-eligible colleagues.[30] This has resulted in the inappropriate classification of employees as EAP exempt who pass the standard duties test but would have failed the long duties test. A significant increase from the 2004 threshold is therefore necessary, not only to account for the declining real value of the salary threshold, but

[30] Jobs With Justice illustrated this phenomenon in its comment by recounting the experience of a store manager who was classified as exempt even though she made only $34,700 per year and regularly worked 70 hours per week, spending her time performing routine tasks such as "unloading merchandise from trucks, stocking shelves and ringing up purchases." See also In re Family Dollar FLSA Litigation, 637 F.3d 508, 511, 516-18 (4th Cir. 2011) (holding that a retail manager paid $655 per week plus bonus was an exempt executive even though she "devoted most of her time to doing . . . mundane physical activities" such as unloading freight, stocking shelves, working the cash register, or sweeping the floors); Soehnle v. Hess Corp., 399 Fed. App'x 749, 750 (3d Cir. 2010) (holding that a gas station manager who was paid an annual salary of $34,000, worked approximately 70 hours per week, and spent 85 percent of time operating a cash register was an exempt executive).

also to correct for the fact that the Department set the standard salary level in 2004 without adjusting for the elimination of the more rigorous long duties test.

Many commenters (including some that believe that the proposed salary level is reasonable) urged the Department to choose a method that results in a higher salary level. The vast majority of these commenters, including NELA, Nichols Kaster, the Rudy, Exelrod, Zieff & Lowe law firm, the Texas Employment Lawyers Association, and the United Food and Commercial Workers International Union (UFCW), asserted that the Department should set the standard salary level equal to the 50th percentile of earnings of full-time salaried workers nationally. The Center for Effective Government stated that the Department should set the standard salary level equal to the 60th percentile of earnings of full-time salaried workers nationally. NELP recommended that the Department adjust for inflation the short test salary level adopted by the Department in 1975, or in the alternative, adopt a threshold of $1,122 per week.

Commenters, such as the UFCW, pointed out that the Department's proposed salary is lower than the average historical salary ratio associated with the short duties test, which is the basis for the standard duties test. Multiple commenters noted that the proposed salary level covers a smaller share of all salaried workers (40 percent) than the 1975 short test salary level, which covered 62 percent of full-time salaried employees. See, e.g., AFL-CIO; NELA; Rudy, Exelrod, Zieff & Lowe. NELA stated that the 1975 short test salary level was 1.57 times the median wage of all full-time wage and salary workers, a ratio which they asserted would result in a current salary threshold of over $65,000 per year based on first quarter 2015 data. EPI commented that the proposed salary level is lower than the short test salary levels adopted by the Department in the 1960s and 1970s, when adjusted for inflation to 2013 dollars. EPI also asserted that the salary threshold should be higher than the inflation-adjusted amounts of short test salary levels

from the past in part to account for the fact that management and professional salaries grew faster than the rate of inflation after 1970, noting that CEO pay among the top 350 U.S. corporations was almost 11 times higher in 2014 than it was in 1978, after adjusting for inflation. Other commenters, including USW, similarly cited the large growth in high-level executive pay in recent decades in support of the Department's proposal.

Commenters urging a higher salary level also asserted that the Department's proposed salary level excludes from overtime protection too large a percentage of employees in traditionally nonexempt occupations and is too low to adequately minimize the risk of inappropriately classifying overtime-eligible workers as overtime exempt. AFL-CIO stated that the Department has previously set the long test salary level at an amount about 25 percent higher than the average starting salary for newly hired college graduates, and they asserted that this would yield a standard salary level of $52,000 per year. AFL-CIO contended that the salary test must be set at a "high enough level that large numbers of eligible workers are not stranded above the threshold." NELA likewise urged the Department to "aim for a threshold where the number of non-exempt employees earning salaries above the threshold equals the number of otherwise exempt employees earning less than the threshold"—an amount we estimated in the NPRM would be roughly equal to the 50th percentile of weekly earnings of full-time salaried workers nationally. See 80 FR 38560.

The Department understands commenters' concerns that the proposed standard salary level was lower than the 50th percentile of full-time salaried workers ($1,065 based on 2013 data) and updating the 1975 short test salary ($1,083 based on 2013 data). As the Department stated in the NPRM, however, we are concerned that a standard salary threshold at that level, in the absence

of a lower salary long test to fall back on, would deny employers the ability to use the exemption for too many employees in low-wage areas and industries who perform EAP duties.

In contrast to commenters representing employees, a great number of commenters representing employers and many individual employers objected that the Department's proposed salary level was too high. While commenters supporting the proposed threshold or advocating for a higher threshold asserted that the proposal is lower than indicated by historical short test levels, commenters advocating for a lower threshold asserted that the proposed threshold is out of step with historical long test levels. For example, the Jackson Lewis law firm asserted that the proposed threshold is higher than any past long test salary level for the executive exemption, when adjusted for inflation to 2015 dollars. The Chamber stated that the ratio of the proposed salary level to the minimum wage is too high, based on an analysis they performed that weighted the historic long test salary levels three times more heavily than historic short test salary levels.

Some commenters requesting a lower salary threshold, such as the American Association of Orthopaedic Executives, Associated Builders and Contractors (ABC), and the Montana Conservation Corps, urged the Department to instead adjust the 2004 salary level for inflation. Many others stated that the Department should set the salary level at the 20th percentile of earnings of full-time salaried employees in the South and in the retail industry, as we did in 2004. See, e.g., American Hotel and Lodging Association (AH&LA); Dollar Tree; NRF. The NRA stated that it could support Alternative 3 in the NPRM, a salary level derived from the Kantor long test method taking the 10th percentile of earnings of likely exempt employees in low-wage regions, employment size groups, city sizes, and industries. Fisher & Phillips urged the Department to set the salary level at the 20th percentile of earnings of exempt employee salaries "in the lowest geographical and industry sectors." Some commenters suggested a lower

percentile of full-time salaried workers nationwide than the Department proposed. For example, the Chamber, which preferred that the Department use a different data source set to set the salary level, stated in the alternative that a salary level at up to the 30th percentile of earnings of full-time salaried workers nationally would "better reflect the actual dividing line between exempt and non-exempt employees." In addition, several commenters focused on the salary level amount rather than, or in addition to, the methodology used to derive the level. For example, a non-profit organization providing senior care recommended a salary level of up to $40,000; FMI stated that most of its grocer members would not see a significant disruption at a salary level of up to $38,376; and the BOK Financial Corporation advocated for a $30,000 salary level. Finally, some commenters, such as the Partnership to Protect Workplace Opportunity (PPWO) and IFA, asserted that the Department's proposed salary level should be lower, but declined to propose a specific number or method. Most of these suggestions do not represent a meaningful departure from the methodology the Department has historically used to set the lower long test salary level, and the Department does not believe that these suggested salary levels are sufficient to account fully for the elimination of the long duties test, as explained below.

The Department received many comments stating that by using a nationwide data set, the proposal fails to adequately account for salary disparities among regions and areas, industries, and firms of different sizes. Some commenters, including the Assisted Living Federation of America and the American Seniors Housing Association (ALFA), Jackson Lewis, and PPWO, asserted that adopting the proposal would effectively eliminate the exemption for certain industries or in certain parts of the country and, as a result, would exceed the Department's statutory authority.

Multiple commenters asserted that the proposed salary level is too high for low-wage regions. See, e.g., Chamber; FMI; International Association of Amusement Parks and Attractions; King's Daughters' School; NRF; PPWO; Society for Human Resource Management (SHRM); and many individual commenters. Several commenters cited to an analysis conducted by Oxford Economics finding that in eight southern states—Arkansas, Florida, Louisiana, Mississippi, North Carolina, Oklahoma, Tennessee, and West Virginia—more than 50 percent of nonhourly workers earn less than $970 per week, the amount the Department predicted the proposed salary level would be in 2016. PPWO cited to a study showing that 100 percent of first-line supervisors of food preparation and serving workers in Mississippi—an occupational category for which the Department predicted 10 to 50 percent of workers would likely pass the duties test when we quantified the impact of our proposal[31]—would fall below the proposed salary level. The National Association of Home Builders (NAHB) analyzed state-level data and found that 50 percent or more of first line construction supervisors in Arkansas, Mississippi, New Mexico, and Tennessee would be affected by the Department's proposal. The National Network to End Domestic Violence commented that for one of its member organizations in a rural state, nine out of eleven staff members earn less than the proposed salary level, and a lender with locations across Alabama, Louisiana, Mississippi, and Tennessee stated that 81 percent (62 out of 74) of its branch managers earn less than $51,000 per year in base salary. Some commenters, for example, the HR Policy Association and National Association of Manufacturers (NAM), expressed concern that employees performing the same duties will be exempt in one location but overtime protected in another.

[31] See Table A2—Probability Codes by Occupation, 80 FR 38594; see also 80 FR 38553-54.

In addition to these comments, multiple commenters noted that salaries may vary widely within a state or region, especially between rural or smaller communities and urban areas. Several commenters, including Columbia County, Pennsylvania, Community Transportation Association of the Northwest, Elk Valley Rancheria Indian Tribe, Jackson Lewis, the Jamestown S'Klallam Tribe, the National Board for Certified Counselors, the National Newspaper Association, NRF, and the Northern Michigan Chamber Alliance, commented that the proposed salary level is too high for rural areas and small communities. HR Policy Association stated that 14 percent of chief executives and 32 percent of general and operations managers in small cities and rural areas earn less than the salary level calculated using the proposed methodology and 2014 data. Commenters also compared earnings and the cost of living in lower-wage communities to very high wage urban areas and asserted that the Department's proposal fails to fully analyze and take into account these differences. See, e.g., America Outdoors (comparing rural areas to Washington, D.C., New York City, and San Francisco); Ashley Manor LLC; National Pest Management Association.

Several commenters also asserted that the proposed salary level ($50,440 based on projections for 2016) would have a disproportionate impact on employers in low-wage industries, such as the retail and restaurant industries. HR Policy Association stated that in the retail, accommodation, and food services and drinking places industries, over one-third of general and operations managers would fall below the proposed salary level in 2014 dollars. FMI stated that "millions of employees in retail who clearly meet the duties requirements for retail earn below $50,000." NRA cited a 2014 survey finding that the median base salary paid to restaurant managers is $47,000 and to crew and shift supervisors is $38,000, and multiple chain restaurant businesses submitted comments stating that if the Department increased the salary level to our

proposed threshold and updated it annually, "there might be no exempt employees in many of our restaurants."

The Department also heard from multiple commenters, such as IFA, the National Federation of Independent Businesses (NFIB), NGA, the National Independent Automobile Dealers Association, the National Newspaper Association, Senator David Vitter, and Representative James Inhofe, that our proposal would have a disproportionate impact on small businesses. The Office of Advocacy of the United States Small Business Administration (Advocacy) stated that the proposed salary threshold would "add significant compliance costs . . . on small entities, particularly to businesses in low-wage regions and in industries that operate with low profit margins."

Several commenters, including the Chamber, Littler Mendelson, Fisher & Phillips, and the Seyfarth Shaw law firm, noted that the Department has historically adjusted the salary level to account for low-wage regions and industries and small establishments, and asserted that the Department failed to do so in this rulemaking. These and other commenters urged the Department to account for such variations by setting the salary level at a point near the lower range of salaries in the lowest-wage regions or industries. For example, among other alternatives, the Chamber asked the Department to consider setting the salary level at the 40th percentile of earnings of full-time salaried employees in Louisiana, Mississippi, and Oklahoma ($784 per week or $40,786 annually), which it described as the three states with the lowest salaries. Many other commenters, including the International Bancshares Corporation, the National Association of Federal Credit Unions, the National Council of Young Men's Christian Associations of the United States of America (YMCA), and many individual commenters, urged

the Department to adopt different salary levels for different regions of the country or for different industries or sizes of businesses.

Commenters representing employee interests, however, disagreed that the Department should make further adjustment for low-wage regions and industries. EPI commented that because the Department's proposed standard salary level falls within historic short test levels, the Department's earlier adjustments to account for regional wage disparities are "baked in." See also AFL-CIO. This is because the Department historically set the short test level as a function of a long test level, which had been adjusted to reflect low-wage regions and industries. UFCW similarly asserted that the Department should not have proposed a salary threshold lower than the average short test salary level to account for low-wage regions and industries, because the data from which the Department drew the percentile includes the earnings of employees in low-wage industries and regions. In addition, AFL-CIO and EPI stated that the Department should be less concerned about the impact of regional wage variation than in prior rulemakings. According to an analysis conducted by EPI, over the past four decades, wages in lower-wage states have "moved much closer to national norms."

The Department has considered these comments and appreciates the strong views in this area. While our proposal did account for lower salaries in some regions and industries by setting the salary level lower than both the average historical salary ratio associated with the short duties test ($1,019 per week according to the data set used in the Final Rule) and the median of full-time salaried workers ($1,146 according to the data set used in the Final Rule), we have determined that further adjustment to account for regional variation is warranted. The proposed salary level ($972 based on the fourth quarter 2015 data) is in the lowest quarter of the historical range of the short test salary, but it is not at the bottom of the range, and based on the comments,

we are concerned that this salary would not sufficiently account for regional variation in wages. Accordingly, we have adjusted the data set used to set the salary level to further reflect salary disparities in low-wage areas. Under this Final Rule, the Department will set the standard salary level equal to the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region. Based on fourth quarter 2015 data, the lowest-wage Census Region is the South, and the 40th percentile of weekly earnings of full-time salaried workers in the South is $913.[32] See Table B. By comparison, the 40th percentile nationally is $972, and the 40th percentile in the highest-wage Census Region (the West) is $1,050.

Table B: 40th Percentile of Earnings for Full-Time Salaried Workers by Census Region

Census Region	40th Percentile of Earnings of Full-Time Salaried Workers (in 4th Quarter 2015)
South	$913
Midwest	$994
Northeast	$1,036
West	$1,050
All Census Regions	$972

This adjustment will ensure that the salary level "is practicable over the broadest possible range of industries, business sizes and geographic regions." 69 FR 22171 (citing Kantor Report at 5). Setting the salary level equal to the weekly earnings of the 40th percentile of full-time salaried workers in the lowest-wage Census Region represents the 22nd percentile of likely exempt employees in the South, the 19th percentile of likely exempt employees in the Midwest, and the 16th percentile of likely exempt employees in both the West and the Northeast.[33] The

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

[33] The population for determining employees who are likely exempt under the standard duties test is limited to potentially affected EAP workers (i.e., white collar, salaried, not eligible for

40th percentile of full-time salaried workers in the South also represents the 20th percentile of likely exempt employees working in small establishments and the 28th percentile of likely exempt employees who do not live in metropolitan areas.[34] This increase from the traditional 10 percent of exempt employees excluded by the Kantor long test method reflects the shift to a salary level appropriate to the standard duties test. Because the long duties test included a limit on the amount of nonexempt work that could be performed, it could be paired with a low salary that excluded few employees performing EAP duties. In the absence of such a limitation in the duties test, it is necessary to set the salary level higher (resulting in the exclusion of more employees performing EAP duties) because the salary level must perform more of the screening function previously performed by the long duties test. Accordingly the salary level set in this Final Rule corrects for the mismatch in the 2004 Final Rule between a low salary threshold and a less rigorous duties test.

The decrease in the salary level due to the change to the lowest-wage region data set addresses commenters' concerns that the salary test would eliminate the exemption for certain industries or certain parts of the country. For example, while PPWO asserted that the proposed salary level would have excluded from the exemption all first line supervisors of food preparation and service workers in Mississippi, the revised salary level adopted in this Final Rule excludes only 78 percent of these workers. This leaves 22 percent of such workers covered by the exemption in Mississippi—appropriately within the 10 to 50 percent of employees in this occupation nationwide predicted to pass the standard duties test under the Department's probability codes.

---

another non-EAP overtime exemption, and not in a named occupation) earning at least $455 but less than $913.

[34] The Department does not know which employees work for small businesses and therefore randomly assigns workers to small businesses. The number of likely exempt employees who do not live in metropolitan areas is based on employees who do not live in a Metropolitan Statistical Area.

See section VI Appendix A. Likewise, 55 percent of first line supervisors of construction trades and extraction workers in the South earn above the Final Rule's salary threshold, even though only 0 to 10 percent of such workers nationwide are likely to pass the standard duties test. Id. The revised salary is approximately equivalent to the 2014 median base salary paid to restaurant managers cited by NRA.

Setting the salary level equal to the 40th percentile of earnings of full-time salaried workers in the lowest-wage Census Region is consistent with the Department's historical practice of examining a broad set of data on actual wages paid to salaried employees and then setting the salary level at an amount slightly lower than might be indicated by the data. In addition, this method is consistent with our previous practice of examining data broken out by geographic area in setting the salary level. The Final Rule methodology also benefits from continuity with our 2004 methodology, in which we set the salary level equal to a percentile of the earnings of full-time salaried workers in the South. Finally, the approach adopted in this Final Rule fulfills the Department's goals of making the salary methodology simpler and more transparent. See 80 FR 38527.

The Department believes that the standard salary level set in this Final Rule will appropriately distinguish between those who likely are bona fide EAP employees and those who likely are not, when paired with the current duties test and will not require a return to a limit on the performance of nonexempt work. The Final Rule salary level, like the Department's proposed salary threshold, exceeds the inflation-adjusted 2004 salary level and the levels suggested by the Kantor long test and 2004 methods (all of which were based on the lower long test salary), but is at the low end of the historical range of short test salary levels, based on the historical ratios between the short and long test salary levels. A substantially higher standard salary threshold,

such as the levels advocated by some commenters representing employees, would fail to account for the absence of a long test, which historically allowed employers to claim the exemption at a lower salary level for employees who satisfy a more restrictive duties test. This is particularly true given that the salary threshold will apply nationwide, including in low-wage regions and low-wage industries. In the NPRM, the Department considered setting the standard salary equal to the 50th percentile of earnings of full-time salaried workers nationwide ($1,146 per week or $59,592 annually according to the data set used in this Final Rule); we also considered adjusting the 1975 short test salary level of $250 for inflation ($1,100 per week or $57,200 annually). We declined to adopt either alternative, however, due to our belief that the salary level generated through these methods would result in overtime eligibility for too many employees in low-wage regions and industries who are bona fide EAP employees. See 80 FR 38534. As discussed above, the Department received a great number of comments in response to the NPRM that confirm our concern about the applicability of such a salary level in low-wage regions and industries. Based on these comments and for the reasons discussed above, the Department has decided to use a regional data set that results in a lower standard salary level than the national data set we proposed in the NPRM.

The Department is mindful that any salary level must adequately demarcate bona fide EAP employees in higher-wage, as well as lower-wage areas. As we have previously explained when discussing the salary level to be paired with the more rigorous long duties test, the threshold "can be of little help in identifying" bona fide EAP employees when "large numbers" of traditionally nonexempt workers in large cities earn more than this amount. Weiss Report at 10. By setting the salary equal to the 40th percentile of salaries in the lowest-wage Census Region, a higher percentile than we chose in 2004, the Department's methodology is sufficiently protective of

employees in higher-wage regions and accounts for the fact that the standard salary level will be paired with a less rigorous standard duties test that does not specifically limit the amount of nonexempt work that can be performed. The $913 salary level is within the historical range of short test salary levels, based on the ratios between the short and long test salary levels, albeit at the low end of that range. To the extent that salaries in lower-wage regions have converged with salaries elsewhere in the country, as some commenters suggested, tying the salary level to salaries in the lowest-wage Census Region is even less likely to result in a threshold that is inappropriate for other areas.

The Department believes the Final Rule methodology strikes an appropriate balance between minimizing the risk of employers misclassifying overtime-eligible workers as exempt, while reducing the undue exclusions from exemption of bona fide EAP employees. As the Department explained in the NPRM, we have long recognized that there will always be white collar overtime-eligible employees who are paid above the salary threshold, as well as employees performing EAP duties who are paid below the salary threshold. Under the Final Rule, 5.7 million white collar employees who fail the standard duties test will now also fail the salary level test eliminating their risk of misclassification as exempt. The Department estimates that 732,000 of these white collar salaried workers are overtime-eligible but their employers do not recognize them as such. See section VI.C.ii. An additional 4.2 million employees who meet the standard duties test (but may not have met the long duties test prior to 2004) will no longer qualify for the EAP exemption—and therefore will become overtime eligible—because they are paid less than the new salary level. See section VI.C.ii. Although the Department recognizes that an estimated 6.5 million white collar employees who fail the standard duties test will still earn at least the new

salary level, these overtime-eligible employees will be protected by the application of the duties test.

Other measures confirm the appropriateness of the new standard salary level. The Department has traditionally considered newly hired college graduates to be overtime eligible and the Final Rule salary level is slightly higher than the average salary for college graduates under 25 years old.[35] See Weiss Report at 19. Setting the salary level at the 40th percentile of weekly earnings of full-time salaried workers in the South also places it far enough above the minimum wage to provide an effective means of screening out workers who should be overtime protected. Following each update from 1949 to 1975, the ratio of the short test salary level to the earnings of a full-time, nonexempt, minimum wage worker equaled between approximately 3.0 and 6.25.[36] The proposed salary level is 3.15 times full-time minimum wage earnings ($913 / ($7.25 x 40)), which is within the historical range.

To the extent that some commenters advocated an even further downward adjustment to the salary level to account for low-wage regions and industries, the Department believes that such an adjustment would not be appropriate given that the Department has decided not to introduce a specific limitation on the performance of nonexempt work into the standard duties test. Moreover, we note that the standard salary level must be practicable in high-wage areas as well

[35] Several commenters asserting that the Department's proposed salary level is too high, including the American Council of Engineering Companies and the American Institute of Certified Public Accountants, suggested that increasing the salary level could lead employers to classify recent college graduates or junior employees as nonexempt. The Department has long recognized that "college graduates just starting on their working careers . . . normally have not achieved bona fide administrative or professional status, nor are their salaries commensurate with those of fully trained and experienced professional or administrative employees." Weiss Report at 19.

[36] The 6.25 ratio is an outlier that was set in December 1949 (when the short test was created) and the minimum wage increased from $.40 to $.75 per hour one month later (which reduced the ratio to 3.33). To return to the 6.25 ratio, the weekly salary level would have to be set at $1,812.50, which is around the 80th percentile of full-time salaried employees nationally.

as in low-wage ones. As we have previously stated, the salary threshold "can be of little help in identifying" bona fide EAP employees when "large numbers" of traditionally nonexempt workers in high wage areas earn in excess of the salary level. Weiss Report at 10. In California and New York, for example, 69 percent of first-line supervisors in construction, 51 percent of paralegals and legal assistants, and 31 percent of secretaries and administrative assistants earn $913 or more per week, despite the fact that the probability of these workers passing the standard duties test is between 0 to 10 percent. With respect to commenters who expressed concern that employees performing the same duties will be exempt in one location and overtime protected in another, the Department notes that this has always been the case and may occur at any salary level. Lowering the salary threshold below the amount set in this Final Rule would result in a salary level that is inappropriate for traditionally nonexempt workers in high wage areas, especially when paired with the less rigorous standard duties test.

The $913 salary level adopted in this Final Rule corresponds to the low end of the historical range of salaries for the short duties test on which the current standard duties test is based ($889 to $1,231). The Department considered the possibility of adopting a salary level equal to the 35th percentile of weekly earnings of full-time salaried employees in the South, which would yield a salary level of $842 per week based on fourth quarter 2015 data. However, given that this would result in a salary level lower than the bottom of the historical range of short test salary levels, based on the historical ratios between the short and long test salary levels, the Department determined that setting the salary level at the 35th percentile of the lowest-wage Census Region would not work effectively with the standard duties test. The Department also considered adopting a higher salary level within the historical range of short test salaries as advocated by many employee representatives, but we remain concerned about the adverse effect such a

threshold might have on low-wage regions. Accordingly, the Department has concluded that the 40th percentile of weekly earnings of full-time salaried workers in the South represents the best dividing line between employees who are overtime eligible and those who may not be overtime eligible, when paired with the standard duties test.

Historically the Department has looked to low-wage industries as well as low-wage regions in setting the long test salary and, in 2004, we looked specifically to the retail industry in setting the standard salary level.[37] In developing this Final Rule, the Department examined weekly earnings of full-time salaried employees in the retail and restaurant industries to determine if adjustment based on these industries was appropriate. In the retail industry, the 40th percentile of full-time salaried employees nationally is $848 per week, a salary below the low end of the historical range of the short test salary ($889) and therefore one that would not work effectively with the standard duties test. In the restaurant industry (food services and drinking places), the 40th percentile of full-time salaried employees nationally is $724 per week. This salary is not only below the low end of the historical short test range, but also only slightly above the historical average of the long test salary level ($719).[38, 39] The Department therefore concluded that setting the salary level based on wages in these industries would require significant changes to the standard duties test, which commenters representing employers overwhelmingly opposed, see,

[37] In the past, salaries in low-wage areas and low-wage industries have been closely aligned, and in 2004 salaries in the South and in the retail industry were similar. See 69 FR 22168 ("[T]he lowest 20 percent of full-time salaried employees in the South region earn approximately $450 per week. The lowest 20 percent of full-time salaried employees in the retail industry earn approximately $455 per week."). This historical parity does not exist at the 40th percentile of workers in the restaurant and retail industries, and adjusting the salary level further to account for wages in these industries would require changes to the standard duties test.

[38] The Department calculated the historic average of the long test salary level by averaging the 20 values set for the long test (executive, administrative, and professional) from 1938 to 1975 in 2015 dollars. The historical average salary level for the long test is $719.

[39] The Department notes there are also significant levels of misclassification of overtime-eligible white collar workers as exempt in these industries. See section VI.C.ii.

e.g., NRF, NRA, FMI, and which would be inconsistent with the Department's goal of simplifying the exemption. The Department believes, moreover, that the lower salary level yielded by using the lowest-wage Census Region is appropriate over the range of industries, including low-wage industries, because it captures differences across regional labor markets without attempting to adjust to specific industry conditions.

With respect to the Chamber's suggestion that the Department limit the data set to the three lowest-wage states in the South (for which the 40th percentile of weekly earnings is $784), this methodology yields a salary level significantly below the historical range of short test salary levels and for all the reasons discussed above would therefore fail to work appropriately with the standard duties test. If the Department had instead looked to Census divisions, the West South Central division,[40] which includes Louisiana and Oklahoma has a 40th percentile of weekly earnings of full-time salaried workers of $878, and the East South Central division,[41] which includes Mississippi, has a 40th percentile of weekly earnings of full-time salaried workers of $849. Both of these would also result in a salary level that is lower than the bottom of the historical short test salary range and would thus necessitate changes to the duties test. Moreover, the Department believes that the best practice is to set the salary level based on an entire region, as we did in 2004, rather than based on a select and very small subset of states or on a Census division.[42] The three Census divisions that make up the South Census Region have lower wages

[40] The West South Central division comprises Arkansas, Louisiana, Oklahoma, and Texas.
[41] The East South Central division comprises Alabama, Kentucky, Mississippi, and Tennessee.
[42] A number of commenters noted that the Department's proposal is higher than the minimum salary level necessary for an EAP employee to be exempt from state overtime laws in two high-wage states, California ($41,600 in 2016) and New York ($35,100 in 2016). See, e.g., Corpus Christi Chamber of Commerce; FMI; IFA; Littler Mendelson. The salary thresholds for the white collar exemption in California and New York are based on multipliers of the full-time equivalents of those states' minimum wages; the salary level in California is 2 times the state minimum wage, and the salary level in New York is typically 1.875 times the state minimum

at the 40th percentile of weekly earnings of full-time salaried workers than any other Census divisions. By focusing on the lowest-wage Census Region—made up of the three lowest-wage Census divisions—we have removed the effect of the three higher earnings Census Regions on the salary level, ensuring the salary level is not driven by earnings in high- or even middle-wage regions of the country. Moreover, establishing the salary level based on a Census Region provides a sufficient data set to capture differences across regional labor markets and produces a salary level that is appropriate on a national basis.

The Department also declines to adopt different salary levels for different regions of the country or for different industries or sizes of businesses. The Department has always maintained a salary level applicable to all areas and industries. As the Department explained when we rejected regional salary thresholds in the 2004 Final Rule, adopting multiple different salary levels is not administratively feasible "because of the large number of different salary levels this would require." 69 FR 22171. Furthermore, as discussed earlier, the Department believes the methodology adopted in this Final Rule will adequately account for commenters' concerns about geographic and other disparities by setting the salary level based on salaries in the lowest-wage Census Region.

---

wage. See Cal. Lab. Code Sec. 515(a); N.Y. Comp. Codes R. & Regs, 12 §§ 142-2.1, 2.14. These multipliers are lower than the historical ratio of the Department's short test salary level and the federal minimum wage (which has never been lower than 2.98, see 80 FR 38533), and they approximate the historical ratio between the Department's long test salary level and the federal minimum wage (which, between 1958 and 1975, ranged from 1.85 to 2.38). The Department believes that the salary level yielded by our methodology, which is 3.15 times the current federal minimum wage, better corresponds to the standard duties test, which—like the old short duties test—does not include a quantitative limit on nonexempt work. The Department also notes that California requires exempt EAP employees to spend at least 50 percent of their time performing their primary duty, not counting time during which nonexempt work is performed concurrently. See Cal. Lab. Code Sec. 515(a), (e); see Heyen v. Safeway Inc., 157 Cal. Rptr. 3d 280, 302 (Cal. Ct. App. 2013).

In addition to asserting that the proposed salary level is inappropriate for low-wage regions and industries, commenters requesting a lower salary level also criticized the methodology the Department used in our proposal, took issue with the justifications underpinning the proposal, and predicted that the proposed salary level would negatively impact employers and employees. Some commenters criticized the Department for using a different percentile to set the salary threshold than it has in the past. See, e.g., FMI; National Roofing Contractors Association (asserting that the "threshold would extend to the 40th percentile of wage earners, up sharply from methodologies used when previously determining the threshold that used the 10th and 20th percentile").

Several commenters also disagreed with the Department's explanation that it was necessary to set a percentile that would not only reflect increases in nationwide salary levels since 2004, but also correct for the fact that the salary level set in 2004 was too low—when paired with a duties test based on the historical short duties test—to effectively screen out overtime-protected white collar employees from the exemption. Many of these commenters asserted that the Department did account for the elimination of the long duties test, by increasing "the percentile used from 10th to 20th." Littler Mendelson; see also AH&LA; NRF. The Chamber commented that the Department did not need to adjust for the elimination of the long duties test in 2004 because the long test salary level was so in need of updating that the long duties test had been effectively inoperative for many years. Finally, some commenters asserted that the Department improperly equates the standard duties test with the less rigorous short duties test. See, e.g., World Floor Covering Association ("DOL did not eliminate the long duty test and keep the short duty test in 2004. Rather, it combined the short and long duties tests by relaxing the strict standards under the long duty test and increasing duties under the short duty test.") The Chamber and the Iowa

Association of Business and Industry pointed out that in 2004 the Department added to the standard executive duties test an additional requirement (that the employee be one who has "the authority to hire or fire other employees or whose suggestions and recommendations" as to these matters "are given particular weight"), and the Iowa Association of Business and Industry also noted that the Department added a "matters of significance" qualification to the administrative standard duties test.

The Department disagrees with these comments, and we continue to believe that the salary level set in 2004 was too low to effectively screen out from the exemption overtime-protected white collar employees when paired with the standard duties test. As an initial matter, we disagree with commenters' suggestion that the standard duties test does not closely approximate the historic short duties test because of minor differences between the two tests. In 2004, the Department described these differences as merely "de minimis," and explained that the new standard duties test is "substantially similar" to the old short duties test. 69 FR 22192-93; 69 FR 22214. The key difference between the old short test and the old long test was that the long test imposed a bright-line 20 percent cap on the amount of time an exempt employee could spend on nonexempt duties (40 percent for employees in the retail or service industries). The short duties test, in contrast, did not impose a specific limitation on nonexempt work because the short test was intended to apply only to workers who earned salaries high enough that such a limitation was unnecessary. The standard duties test developed in 2004 takes the short test approach and does not specifically limit nonexempt work.

When moving to a standard duties test based on the short duties test in 2004, the Department relied on the methodology we had historically used to set the long test salary threshold, with two changes. First, the Department set the salary level based on the earnings of exempt <u>and</u>

nonexempt full-time salaried employees. In previous rulemakings, the Department had looked only at salary data on employees who met the EAP exemption, who earn higher salaries on average than nonexempt salaried employees. See 69 FR 22166-67. Second, recognizing that "employees earning a lower salary are more likely non-exempt," the Department offset the first change by making an additional adjustment. Id. The 2004 Final Rule set the salary level to exclude from exemption "approximately the lowest 20 percent of all salaried employees," whereas previously the Department set the salary level to exclude "approximately the lowest-paid 10 percent of exempt salaried employees." 69 FR 22168 (emphases added and in original); 69 FR 22166 (emphases added). By setting the salary threshold at a higher percentile of a data set that included employees likely to earn lower salaries, the Department explained that we reached a final salary level that was "very consistent with past approaches" to setting the long test salary threshold. 69 FR 22167.

Although the Department also recognized the need to make an additional adjustment to the long test salary level methodology because of the move to the standard duties test, see 69 FR 22167, the salary level included in the 2004 Final Rule ultimately did not do so. The Department indicated that the change in percentile could account for both the fact that the data now "included nonexempt salaried employees" and "the proposed change from the 'short' and 'long' test structure." Id.; see 68 FR 15571. At the same time, however, the Department acknowledged that the change to the 20th percentile of exempt and nonexempt salaried employees produced a salary that was in fact roughly equivalent to the salary derived through the methodology previously used to set the long test salary levels. See 69 FR 22168. As the data tables in the 2004 Final Rule show, the $455 salary level excluded only 8.2 percent of likely exempt employees in the South and 10.2 percent of likely exempt employees in retail. See 69 FR 22169,

Table 4; see also 69 FR 22168 ("The lowest 10 percent of likely exempt salaried employees in the South earn just over $475 per week.").[43] Accordingly, the Department set the standard salary level using a methodology that yielded a result consistent with the methodology we had historically used to set the salary level paired with the long duties test, even though the new standard duties test was based on the short duties test. This was a methodological error, even if employers at the time were primarily using the less rigorous short duties test. The fact that the long duties test was unused because the Department had neglected to update the salary associated with it for 29 years does not mean that we did not need to account for the removal of the long test when the standard test was established. The Department is now correcting this error by setting the salary level equivalent to the 40th, rather than the 20th, percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (the South). This percentile results in a salary level that is at the low end of the historical range of short test salary levels, based on the historical ratios between the short and long test salary levels, but is appropriately higher than the historical long test salary levels. By making this change to our 2004 methodology, the Department better accounts for the fact that the standard duties test is significantly less rigorous than the long duties test and, therefore, the salary threshold must play a greater role in protecting overtime-eligible employees.

2. Purpose of the Salary Level Test

[43] While the 2004 method and the Kantor long test method produced similar salaries in 2004, the salary levels yielded by these methods now diverge significantly. Today, the 2004 method would produce a salary level of $596 per week, while using the Kantor long test method would result in a salary level of $684 per week. See section VI.C.iii. Thus, not only would using the 2004 methodology today fail to account for elimination of the long duties test, it would result in a noticeably lower salary level than the average long test salary level between 1940 and 2004 in 2015 dollars.

Several commenters that stated that the Department's proposed threshold is too high asserted that the proposal alters the purpose of the salary test and inappropriately minimizes the role of the duties test by excluding from the exemption too many employees who satisfy the standard duties test. In support of this point, SHRM noted the Department's estimate that 25 percent of white collar workers subject to the salary level test who currently meet the duties test would be overtime-protected under the Department's proposed salary level. HR Policy Association stated that, if the salary level was set according to the Department's proposed methodology, 25 percent of accountants and auditors, 24 percent of business and financial operation managers, and 11 percent of "chief executives" would not qualify for the EAP exemption in 2014.

Several commenters representing employers stated that the salary level has historically been set at a level such that "employees below it would clearly not meet any duties test," or would be very unlikely to satisfy the duties requirements. NRA; see also HR Policy Association; Jackson Lewis; SHRM. SHRM and others asserted that the proposal would for the first time set the salary level such that a large number of employees who satisfy the duties test would be excluded from the exemption, which would therefore make them overtime eligible. These commenters pointed to the Department's statement, when setting the long test salary thresholds in 1949 and 1958, that the thresholds should not defeat the exemption for "any substantial number of individuals who could reasonably be classified for purposes of the Act as bona fide executive, administrative, or professional employees," and should provide a "ready method of screening out the obviously exempt employees." Weiss Report at 8-9; Kantor Report at 2-3. Commenters asserted that because only those who are "very likely to satisfy" the duties tests earn salaries above the Department's proposed threshold, see Jackson Lewis (emphasis in comment), the Department has turned the historical purpose of the salary level "on its head." See PPWO.

PPWO, SHRM, and others further commented that the Department's proposal improperly renders the duties test superfluous and makes the salary level test the "sole" determinant of exempt status.

The Chamber, FMI, and SHRM also stated that the Department lacks the authority to set wages for, or establish a salary level with the goal of, improving the conditions of executive, administrative, and professional employees. IFA asserted that because the Department's proposal makes nonexempt what IFA characterized as a significant number of employees who would clearly meet the duties test, the proposal "expands the number of employees eligible for overtime beyond what Congress envisioned."

Commenters representing employees, however, disagreed that the purpose of the salary level is to identify employees who are very likely to fail the duties tests. NELA and other commenters asserted that the primary purpose of the salary level is to prevent employers from inappropriately classifying as exempt those who are not "bona fide" executive, administrative, or professional employees. NELA noted that the proposed threshold is lower than the salaries of roughly 41 percent of salaried workers who fail the duties test, according to the NPRM, and AFL-CIO commented that under the proposal, "the percentage of overtime-eligible white collar salaried employees above" the salary level "will still be considerably higher than the percentage of employees below the threshold who meet the duties test." Commenters representing employees also disagreed that the Department's proposal would prevent employers from taking advantage of the exemption for a substantial number of bona fide executive, administrative, or professional employees. For instance, EPI noted that BLS scores occupations by skill, knowledge, and responsibility, and finds an hourly wage of about $24 (or $970 for a 40-hour workweek) is below the salary level associated with supervisory responsibilities.

As the Department explained in the NPRM, the purpose of the salary level test has always been to "distinguish bona fide executive, administrative, and professional employees from those who were not intended by Congress to come within these exempt categories." 80 FR 38524. Any increase in the salary level must therefore "have as its primary objective the drawing of a line separating exempt from nonexempt employees." Id. The salary methodology established in this Final Rule fulfills this purpose by effectively and efficiently demarcating between white collar employees who are overtime protected and those who may be bona fide EAP employees.

The Department does not believe that the methodology adopted in this Final Rule would defeat the exemption for too many employees who pass the standard duties test, or render the standard duties test superfluous. There will always be some employees performing EAP duties who are paid below the salary threshold, as well as overtime-eligible employees who are paid above the salary threshold (and thus whose status turns on the application of the duties test). See 80 FR 38527. Under the Final Rule, 6.5 million white collar workers who earn above the required salary level do not satisfy the standard duties test, representing 47 percent of the total number of white collar workers who fail the duties test. For these overtime-eligible salaried workers, the standard duties test rather than the salary test will dictate their exemption status. For example, 48 percent of secretaries and administrative assistants in banking nationwide earn at or above the $913 per week salary level adopted in this Final Rule, although at most 10 percent of such workers are likely to pass the standard duties test. Likewise, 71 percent of first-line supervisors of mechanics, installers, and repairers in the utilities industry nationwide earn at least $913 per week, even though only 10 to 50 percent of such workers are likely to pass the standard duties test.

By contrast, of salaried white collar workers who currently meet the standard duties test, 5.0 million (22.0 percent) earn less than $913 per week, and will thus be eligible for overtime under this Final Rule. Whenever the Department increases the salary level, it is inevitable that "some employees who have been classified as exempt under the present salary tests will no longer be within the exemption under any new tests adopted." Kantor Report at 5. As we have explained, such employees include "some whose status in management or the professions is questionable in view of their low salaries," and some "whose exempt status, on the basis of their duties and responsibilities, is questionable." Id. Moreover, as we have long been aware, if too low a salary level is paired with a duties test that does not specifically limit nonexempt work, employers may inappropriately classify as exempt workers who perform large amounts of nonexempt work. See 40 FR 7092. The Department believes that many of the workers who will no longer be exempt as a result of this rulemaking would have failed the long duties test and are currently inappropriately classified because of the mismatch between the current standard duties test and the standard salary level. To the extent that commenters expressed concerns that the proposal would exclude from exemption too many bona fide EAP employees in certain areas and industries, the Department has recalibrated the methodology in this Final Rule to better take into account salaries in low-wage regions and industries, as discussed earlier, while remaining cognizant of the corresponding but opposite impact on high-wage regions and industries. See section VI.C.ii.

Commenters asserting that the Department's proposal turned the purpose of the salary level test "on its head" misconstrue the relationship between the salary level test and the duties test as it has existed throughout most of the history of the part 541 regulations. The fact that an employee satisfies the duties test, especially the more lenient standard duties test, does not alone

indicate that he or she is a bona fide executive, administrative, or professional employee. The salary level test and duties test have always worked in tandem to distinguish those who Congress intended the FLSA to protect from those who are "bona fide" EAP employees. The Department has long recognized, moreover, that "salary is the best single indicator of the degree of importance involved in a particular employee's job," Weiss Report at 9, and "the best single test of the employer's good faith in characterizing the employment as of a professional nature." Stein Report at 42. Thus, the Department acknowledged shortly after we first promulgated the part 541 regulations that, in the absence of a clause "barring an employee from the exemption if he performs a substantial amount of nonexempt work," it becomes "all the more important" to set the salary level "high enough to prevent abuse." Stein Report at 26. This inverse correlation between the salary level and the duties requirements was the basis of the separate short and long tests, which co-existed until 2004.

As reflected in many comments favoring a lower salary level, the Department historically paired the long duties test—which limited that amount of nonexempt work an exempt employee could perform—with a salary level designed to minimize the number of employees satisfying that test who would be deemed overtime-eligible based on their salaries. Even then, the Department noted that the long test salary level should exclude the "great bulk" of nonexempt employees from the EAP exemption. Weiss Report at 18. When the Department enacted the short test in 1949, however, we recognized that this more permissive "short-cut test" for determining exempt status—which did not specifically limit the amount of time an exempt employee could spend on nonexempt duties—must be paired with a "considerably higher" salary level. Id. at 23. This salary level, the Department explained, "must be high enough" to qualify for the EAP exemption "only those persons about whose exemption there is normally no

question." Id. Accordingly, the Department set the short test threshold such that those who earned above this level would meet the requirements of the long duties test—including the limit on performing nonexempt work—"with only minor or insignificant exceptions." Id. In other words, the short test salary threshold was sufficiently high that an employee earning above this level was not only "very likely," but nearly certain, to satisfy the long duties test, as well as the short duties test. Between 1949 and 1975, the Department adhered to these principles by enacting short test salary levels at approximately 130 to 180 percent of the long test salary levels.

The standard duties test adopted in 2004, and unchanged by this Final Rule, is essentially the same as the old short duties test. It does not specifically limit the amount of time an exempt employee can spend performing nonexempt duties. Accordingly, the Department disagrees with commenters that suggest that the current duties test can be paired appropriately with a salary level derived from the same methodology we have historically used to set the salary level paired with the long duties test. The Department also disagrees, however, with commenters that suggest the current standard duties test could be paired with a salary level derived from the 50th percentile of full-time salaried workers or from the 1975 short test salary level without also reinstating a lower-salaried long test. The methodology adopted in this Final Rule results in a salary level that is higher than indicated by historical long test methodologies, but at the low end of the historical salary range of short test salary levels, based on the ratios between the short and long test salary levels. The Department believes that this approach strikes an appropriate balance between protecting overtime-eligible workers and reducing undue exclusions from exemption of bona fide EAP employees. It also does so without necessitating a return to the two-test structure or imposing a quantitative limit on nonexempt work—alternatives that many of these same commenters strenuously opposed. See section IV.F.

3. Data Used to Set the Standard Salary Level

Some commenters representing employers also raised concerns about the Department's use of the CPS data on full-time nonhourly employees. The Chamber and Fisher & Phillips advocated that rather than calculate the salary level using the CPS data, the Department should create our own data set of exempt salaried employees drawn from WHD investigations and field research. NAM stated that the CPS data provides an "apples-to-oranges" comparison because it reflects all nonhourly compensation, while the Department's proposal excludes certain forms of compensation (for example, some incentive pay) from counting toward the salary threshold, and other commenters made similar assertions. The Chamber, Fisher & Phillips, and the Iowa Association of Business and Industry (IABI) also disagreed with the Department's conclusion that CPS data on compensation paid to nonhourly workers is an appropriate proxy for compensation paid to salaried workers. Employees sampled might be paid on a piece-rate or commission basis, for example, and thus, the Chamber stated, the "non-hourly worker category is at best a rough and imprecise measure of workers paid on the basis required for exempt status." In addition, IABI, the International Foodservice Distributors Association, and others criticized the Department for declining to further restrict the CPS sample by filtering out various categories of employees—such as teachers, lawyers, or federal employees—based on statutory and regulatory exclusions from FLSA coverage or the salary requirement.

The Department continues to believe, as we did in 2004, that CPS data is the best available data for setting the salary threshold. The CPS is a large, statistically robust survey jointly administered by the Census Bureau and BLS, and it is widely used and cited by industry analysts. It surveys 60,000 households a month, covering a nationally representative sample of workers, industries, and geographic areas and includes a breadth of detail (e.g., occupation

classifications, salary, hours worked, and industry). As the Department explained in the NPRM, the CPS offers substantial advantage over data drawn from the pool of our own investigations, because the Department's investigations contain too few observations to yield statistically meaningful results. See 80 FR 38528.

The Department considers CPS data representing compensation paid to nonhourly workers to be an appropriate proxy for compensation paid to salaried workers, as we explained in the NPRM. See 80 FR 38517 n.1. The Department believes that most nonhourly workers are likely to be paid a salary, and although the data may include earnings of workers paid on a fee basis, the EAP exemption can apply to bona fide administrative and professional employees compensated in this manner. See § 541.605. Moreover, as explained in greater detail in section IV.C., the Department has adopted a change to the salary basis test in this Final Rule which will newly allow employers to satisfy as much as 10 percent of the standard salary level requirement through the payment of nondiscretionary bonuses and incentive pay (including commissions). The Department acknowledges that the CPS data set may include some compensation excluded from the salary test; however, we are not aware of any statistically robust source that more closely reflects salary as defined in our regulations, and the commenters did not identify any such source.

Finally, the Department disagrees that we should have excluded the salaries of employees in various job categories, such as teachers, doctors, and lawyers, because they are not subject to the part 541 salary level test. These white collar professionals are part of the universe of executive, administrative, and professional employees who Congress intended to exempt from the FLSA's minimum wage and overtime requirements. Including them in the data set achieves a sample that is more representative of EAP salary levels throughout the economy. Moving to an even

more standardized sample that does not require adjustments also serves the Department's goal of making the salary methodology as transparent, accessible, and as easily replicated as possible, and is consistent with the President's directive to simplify the part 541 regulations.

4. Comments Requesting a Phase-In of the Proposed Increase

Many employers and commenters representing them also expressed concern about the magnitude of the Department's proposed increase from the 2004 salary level. Under the proposal, the salary level would have increased from $455 a week to $972 per week based on fourth quarter 2015 data, a 113.6 percent overall increase and 9.5 percent average per year increase. Under the Final Rule, the salary level will increase to $913 per week, a 100.7 percent overall increase and 8.4 percent average per year increase. Several commenters, including the Chamber, Littler Mendelson, and NAHB, described the proposed percentage increase in the salary level as "unprecedented." Many commenters urged the Department to gradually phase-in an increase to the salary level. SHRM, for example, stated that a phased-in approach will provide some flexibility to employers, allowing them to gather information about the hours that currently nonexempt employees work and to budget for any increased wages and other costs. Independent Sector noted that an appropriate phase-in period would allow non-profit organizations to adjust to a new salary level without reducing programs and services. Some commenters advocating an incremental approach, such as PPWO and the Chamber, opposed the proposed salary level, but requested a gradual phase-in if the Department moves forward with the proposal. Others did not oppose the Department's proposed threshold, so long as the Department phases in the increase. See, e.g., National League of Cities; the Northeastern Retail Lumber Association; United Community Ministries; Walmart; Washington Metro Area Transit Authority (WMATA).

Contrary to some commenters' assertions, the magnitude of the salary increase proposed by the Department is not unprecedented. The 2004 Final Rule increased the then-current long test salary level for executive and administrative employees by 193.5 percent (from $155 to $455), and increased the then-current short test salary level by 82 percent (from $250 to $455). See 69 FR 22123 (explaining that the final rule nearly "triples" the "minimum salary required for exemption"). Further, as EPI pointed out in its comment, in the approximately 11 years between 1938 and 1949, the administrative long test salary test increased 150 percent. The Department acknowledges that this rulemaking enacts a sizeable increase to the 2004 salary level; however, such an increase is necessary in order to reflect increases in actual salary levels nationwide since 2004 and correct the 2004 Final Rule's mismatch between the standard duties test and the standard salary level based on the long duties test level. As we explained in the NPRM, this is the first time that the Department has needed to correct for an incongruity between the existing salary level and the applicable duties test. That said, under our proposal, the salary level effective in 2016 would have been $50,544; under the Final Rule, we project that the salary level will not reach $50,000 until the first update on January 1, 2020. Additionally, as explained in section II.G., this Final Rule has a delayed effective date of December 1, 2016—more than the 120-day delayed effective date following publication of the 2004 Final Rule. The Department believes that the timing of the effective date of this Final Rule will help minimize disruption as employers adjust to the new salary level.

5. Impacts of the Increased Salary Level

Commenters identified many impacts that they believed would flow from the proposed increase in the standard salary level. Commenters representing employers and employees differed dramatically on some of the predicted impacts of the rule. In addition, where

commenters representing employers and employees agreed on likely outcomes, they viewed the advantages and disadvantages of those outcomes quite differently.

Many employers and their representatives stated that employers would not be able to afford to increase the salaries of most of their currently exempt employees to the proposed level. Therefore, they stated that they were likely to reclassify many of these employees to overtime-protected status, which they asserted would disadvantage the employees in a number of ways and would not increase their total compensation. In contrast, employee advocates predicted that workers will benefit from the increased salary level; those who receive a salary increase to remain exempt will benefit directly, and those who are reclassified as overtime eligible will benefit in other ways, as detailed below.

Employers and their representatives, including AH&LA, CUPA-HR, NAM, NRF, and the National Small Business Association (NSBA), suggested that they would reclassify many employees to overtime-protected status. For example, the NGA surveyed its members, and 98 percent stated they would reclassify some currently exempt workers, and 80 percent stated that they would reclassify 50 percent or more because they cannot afford to increase their salaries. NCCR commented that one restaurant chain stated it likely would reclassify 90 percent of its managers and another company with more than 250 table service restaurants estimated that 85 percent of its managers have base salaries below the proposed threshold. CUPA-HR stated that 87 percent of those responding to its survey of higher education human resource professionals stated "they would have to reclassify <u>any</u> exempt employee currently making less than $47,500" (emphasis in comment).

Many employers and their representatives stated that they would convert newly nonexempt employees to hourly pay and pay them an hourly rate that would result in employees working the

same number of hours and earning the same amount of pay as before, even after accounting for overtime premium pay. Also, some employers indicated they might reduce their workers' hours, especially over time, in an attempt to avoid paying any overtime premium pay, so the formerly exempt workers' hours and pay ultimately could be lower. See, e.g., AH&LA; CUPA-HR; Jackson Lewis; NAM; NRF; NSBA.

Some commenters gave specific estimates of the percentage of newly nonexempt employees who would have their overtime hours limited. Associated General Contractors of America (AGC) surveyed its construction contractor members and more than 60 percent expected to institute policies and practices to ensure that newly overtime-eligible employees do not work more than 40 hours per week. ANCOR surveyed service provider organizations and more than 70 percent stated that they would prohibit or significantly restrict overtime hours. SHRM similarly commented that 70 percent of its survey respondents stated they would implement restrictive overtime policies. NRF cited an Oxford Economics report and stated that 463,000 retail workers would be reclassified to nonexempt status and those employees who work overtime would be converted to hourly pay, with their earnings remaining the same after their hourly rates of pay were adjusted, while an additional 231,500 retail employees would be reclassified to nonexempt status and have their hours and earnings reduced.[44]

Not all employers indicated such high numbers of employees would be reclassified, converted to hourly pay, or limited in hours. For example, NAM stated that 41 percent of manufacturers

[44] NRF commissioned Oxford Economics to examine the impact of the Department's rulemaking on the retail and restaurant industries and attached three documents produced by the firm to its comments on the NPRM. The first document is a report titled "Rethinking Overtime – How Increasing Overtime Will Affect the Retail and Restaurant Industries" and was published before the Department issued the NPRM. The second document is a letter dated July 17, 2015 that updates the estimates provided in the "Rethinking Overtime" paper in light of the Department's proposal. The third document is a letter dated August 18, 2015 that examines states' prevailing wage levels and the Department's automatic updating proposal.

stated they would reclassify employees and 37.2 percent stated they would then reduce employees' hours. NAHB stated that 33 percent of survey respondents indicated they would need to make some change regarding construction supervisors, and 56 percent of that subgroup indicated they would take steps to minimize their overtime. However, only 13 percent of respondents stated they would reduce salary, and only 13 percent stated they would switch employees from a salary to an hourly rate.

Numerous employers and their representatives, including AH&LA, CUPA-HR, NCCR, Nebraska Furniture Mart, NRA, NRF, OneTouchPoint, Pizza Properties, Seyfarth Shaw, SHRM, SIFMA, and the Salvation Army, also commented that the employees who were reclassified to nonexempt status would be further disadvantaged because they would lose valuable fringe benefits, such as life insurance, long-term disability insurance, increased vacation time, incentive compensation, tuition reimbursement, and increased retirement contributions. They noted that many employers offer such benefits only to exempt employees, or provide them to exempt employees at a greater rate or at a reduced cost. In addition, ANCOR and others stated that nonexempt workers' fringe benefits would be negatively affected because employers would take funds away from such benefits in order to pay for the increased costs of the rule. AGC surveyed its construction contractor members, and 40 percent expected affected employees to lose some fringe benefits. With regard to those employees who remain exempt and receive a higher salary, some employer representatives, including AH&LA, NCCR, and NRF, stated that the employees would not actually benefit because employers would make other changes, such as reducing or eliminating bonuses or other incentive compensation, in order to keep their total labor costs the same. These commenters viewed this as problematic because these employees are in middle management positions that are "key steps on the ladder of professional success" and incentive

compensation is an important motivator. AH&LA stated that reducing incentive compensation "curtails the ability of employers to reward their star employees," although they acknowledged that this concern would be mitigated if incentive compensation could count toward the increased salary level. NAHB's survey results showed that 55 percent of those employers who indicated that some change for construction supervisors would be necessary would reduce or eliminate bonuses, while 33 percent stated they would reduce or eliminate other benefits.

Employer groups also stated that employees reclassified to nonexempt status and converted to hourly pay would be harmed by the loss of flexibility and the loss of the guarantee of receiving the same salary every workweek. Employers and their representatives, including AH&LA, American Bankers Association (ABA), the Chamber, FMI, IFA, New Jersey Association of Mental Health and Addiction Agencies, OneTouchPoint, PPWO, SIFMA, Seyfarth Shaw, and SHRM, asserted that exempt status gives employees the flexibility to come in late, leave early, and respond to unexpected events such as taking a sick child to the doctor. Moreover, they can do so without fear of losing pay for the time spent away from work. Newly overtime-eligible employees, these commenters asserted, will have to account for their time and they will have to think more carefully about taking unpaid time off to deal with personal and family issues. Employer representatives noted that another benefit of exempt status is that many employers allow exempt employees to perform some of their work remotely and outside of normal business hours, such as from home during the evening, as best suits the employees' personal schedules. See, e.g., AH&LA; American Staffing Association; CUPA-HR; HR Policy Association; Jackson Lewis; Maryland Chamber of Commerce; SIFMA; Women Impacting Public Policy (WIPP); YMCA. Commenters stated that many employers do not allow nonexempt employees this same flexibility in work location and in the ability to work during non-traditional hours, as it is more

difficult to monitor their hours and ensure proper compensation for all hours worked. For example, SHRM stated that 67 percent of its survey respondents indicated decreased workplace flexibility and autonomy were likely results of the Department's proposal.

Employer groups also stated that employees reclassified to nonexempt status will lose out on after-hours management training programs and committee meetings and thus have fewer opportunities for career advancement. See, e.g., AH&LA; ANCOR; Construction Industry Round Table; Credit Union National Association; CUPA-HR; Jackson Lewis; Kentucky Pharmacists Association; Maryland Chamber of Commerce; NCCR; NRF; New York State Restaurant Association; PPWO; SIFMA; SHRM. Many of these commenters also stated that newly overtime-protected workers will not be permitted to work extra hours to get the job done as a way to prove their talents and dedication, and they will not be asked to perform the most challenging and important managerial functions. Employers asserted that these changes will "hollow out" the ranks of middle management, limit existing career paths, and negatively affect the newly nonexempt employees' promotion potential and future earnings. See, e.g., Michigan Chamber of Commerce; NCCR; NRF.

Many employers and their representatives also emphasized that the loss of exempt status will have a negative impact on employee morale. They stated that employees sought out their management role and view their exempt status as an indication of the employer's recognition of their achievements and their position as part of the management team. They stated that the loss of exempt status will be perceived as a demotion and devaluation of their roles in the organization, even if other aspects of their compensation remain the same. See, e.g., ANCOR; Chamber; CUPA-HR; FMI; Jackson Lewis; NAM; NCCR; NGA; NRA; Pizza Properties; SIFMA; SHRM; Salvation Army. NRF cited a survey it commissioned of 200 salaried retail and

restaurant managers showing that the change in status would make 45 percent of managers feel like they were "performing a job instead of pursuing a career," and 31 percent would feel limited in their ability to advance in their careers.

Finally, employer representatives identified a number of other negative consequences that they believed would flow from the adoption of the proposed increase in the standard salary level. For example, some employer groups, including FMI, NRF, and WIPP, emphasized that they believed employers would eliminate full-time jobs and create part-time jobs. FMI, NGA, Seyfarth Shaw, and SHRM indicated that employers would use part-time workers to ensure that newly overtime-eligible employees did not have to work overtime hours. ANCOR, NGA, Seyfarth Shaw, and the YMCA also predicted that, as the hours of the newly nonexempt workers are restricted, employers will respond by increasing the workload burden and scope of responsibility of the managers and supervisors who remain exempt.

Employees and employee advocates, on the other hand, predicted that workers would benefit in a variety of ways from the proposed increase in the standard salary level. First, they saw direct benefits from the proposed salary because, for those who remain exempt but currently earn less than the proposed increase, they will receive additional pay each week in order to raise them to the new salary level. Employees who are reclassified to nonexempt status will get more time outside of work to spend with their families or to engage in leisure activities if their hours are reduced, and thus they will have a better work-life balance; alternatively, they will be paid time-and-a-half for any overtime hours they work. Finally, work opportunities will be spread as workers who had been unemployed or underemployed will gain additional hours. Employee advocates viewed these outcomes as consistent with the fundamental purpose of the FLSA's

overtime provision. See, e.g., AFL-CIO; American Federation of Teachers (AFT); Legal Aid Society-Employment Law Center (ELC); National Women's Law Center (NWLC); Partnership.

Some advocates, including AFL-CIO, AFT, and NELP, emphasized the benefits of spreading employment in light of the harms that come from working long hours, citing studies showing that long hours are related to stress and injuries at the workplace and increased incidences of certain chronic diseases like heart disease, diabetes, and depression. They also cited studies showing the high cost to businesses associated with absenteeism and turnover due to workplace stress and stated that productivity would improve by reducing turnover. The AFT noted that if employers cut formerly exempt workers' hours and add more nonexempt jobs, that would "likely have a salutary effect on wages since the low wage growth in our economy is related to employment slack."

EPI disputed the employers' claim that wages and hours would remain the same after employees were reclassified to nonexempt status. EPI emphasized that this view assumes that employees have no bargaining power. However, EPI stated that a "consistent finding of both labor and macroeconomics is that nominal wages are 'sticky,' meaning that employers rarely will lower them." EPI concluded this is particularly likely to be the case now, given that the unemployment rate for college graduates was just 2.6 percent in July 2015 and for those in "management, professional, and related" occupations was just 3.1 percent. Therefore, employers will not be able to reduce employees' wage rates when they are reclassified to nonexempt status to the full extent that would be necessary for the employees to receive no additional compensation for overtime hours worked. NELP similarly emphasized that, at a time when even low-wage employers are raising their starting wages in order to attract and retain a qualified

workforce, it would be “a foolhardy business practice” for employers to risk losing formerly exempt workers by decreasing their wages and hours.

Worker advocates also disputed employers’ claims that workers would lose privileges and flexibility after they were converted. For example, EPI pointed to research based on the General Social Survey showing that salaried workers and hourly workers experience similarly limited workplace flexibility at levels below $50,000 per year. The research showed that 43-44 percent of hourly workers paid between $22,500 and $49,999 were able to “sometimes” or “often” change their starting or quitting times. That percentage only increased to 53-55 percent for salaried workers in that same range. Only when salaries rose above $60,000 did 80 percent of salaried workers report being able to “sometimes” or “often” change their starting or quitting times. Employees paid hourly actually reported more flexibility in the ability to take time off during the work day to take care of personal matters or family members, with 41 percent of hourly workers earning $40,000-$49,999 stating it was “not at all hard” compared to only 34 percent of salaried workers. Finally, salaried workers reported slightly greater levels of work stress than hourly workers, and they worked mandatory overtime at the same frequency as hourly workers and more days of overtime in general.

Many of the comments from individual exempt employees similarly emphasized their lack of flexibility. For example, a retail store manager described working 55-60 hours a week, with store staffing kept at the bare minimum of two-person coverage. Therefore, the manager has little “flexibility when an employee calls out sick. I have to pick up the slack.” A chef similarly stated that he routinely works 20-30 hours of overtime per week, and has to modify his schedule to meet the demands of the business, including by filling in if an overtime-eligible cook gets sick. Another exempt employee who reported working 1136 hours of overtime in three years (an

average of approximately 49 hours of work per week) stated, "[i]f I complete my work in 30 hours I still have to stay for the required work hours of the company & longer as required or requested." A manager of a community home for the intellectually disabled concurred, stating that the homes "have to be staffed 24 hours a day, 365 day[s] per year. To reduce[ ] organizational overtime, managers are expected to work when employees call in sick, are on leave, and when a client is in the hospital and needs a 24 hour sitter. Managers also pitch in to help other homes when there is a need." Other exempt workers similarly noted that they are scheduled to staff specific shifts and also are required to fill in for hourly workers who call out sick, when positions are vacant, when extra hours are needed such as around the holidays, or when the employer has to cut payroll to meet its targets.

With regard to the loss of "status," NELP commented that, even if employers do reclassify some employees to nonexempt status, there is no reason to consider that a demotion. NELP stated the employer can continue to give nonexempt employees whatever job titles are appropriate and is not required to otherwise diminish their stature. SEIU emphasized that it is not the designation of "exempt" that provides status to workers, but rather the pay and benefits that should accompany that designation. For example, most registered nurses, who perform bona fide professional duties and whose earnings typically exceed the proposed salary, nonetheless prefer to be paid hourly and be overtime eligible. SEIU concluded that "[b]eing classified as ineligible for overtime is little comfort to a worker who routinely works more than forty hours a week and can barely afford child care for the time she is missing with her family." The UAW, representing postdoctoral scholars, made the same point regarding status, concluding that "their low pay indicates that their employers do not view them or treat them as bona fide professionals."

Numerous individual employees also stated that they would not perceive a change from exempt to overtime-protected status as a demotion. For example, one employee stated that he sometimes works seven days and more than 55 hours per week, and that he would "gladly move down to non-exempt and punch a time card. At least I would finally be paid fairly for all the hours I am putting in." A retail store manager similarly stated that he works an average of 55-60 hours per week and looks forward to either receiving an increased salary or the return of his personal life. He rejected the view that exempt employees would feel demoted by a change in status, saying he does not want a meaningless title and would not "be embarrassed if my employees find out I've been bumped to hourly again." Another store manager with 12 years of experience emphasized "I am NOT concerned with the transition from being exempt to non exempt if that were to happen." A convenience store manager who works an average of 60-65 hours per week stated that 7 of the 8 exempt employees he knows quit in the past year due to being overworked without any additional compensation, and he stated that workers feel that an exempt position is "a demotion rather than a promotion." Another exempt employee stated that he believes that businesses often use salaried positions as a way to cut down on overtime costs, and that the employers "who are bemoaning the loss of 'status' for their employees are probably those who have used this trick to get more hours worked for less money."

In response to some employers' assertions that they will reclassify many of their currently exempt employees to overtime-protected status, convert them to hourly pay, modify their pay so that they work the same number of hours and earn the same amount, and potentially reduce their hours in the long run, the Department estimates that 60.4 percent[45] of exempt affected employees

[45] The Department stated in the NPRM that 74.7 percent of all affected workers were Type 1 workers who did not regularly work overtime and did not work overtime in the survey week; therefore, we assumed they would not be paid an overtime premium despite becoming overtime

do not currently work any overtime hours. As explained in detail in the economic impact analysis in section VI.D.iv., we expect there to be relatively little change in the weekly earnings or weekly hours of such employees. We agree that for the remaining employees, who do regularly or occasionally work overtime hours, the impact of the rule will depend upon how their employers choose to respond, and we recognize there likely will be a variety of responses from which employers can choose. For example, employers will raise the salaries of some employees to the new required level; employers will reclassify some other employees to nonexempt status and provide minimum wage and overtime protections and may attempt to minimize the overall cost by modifying those employees' regular rates of pay and reducing their hours. The economic impact analysis discusses the range of possible outcomes. However, as explained in section VI.D.iv., based upon our review of the economic literature, the Department concludes that the most likely outcome is that affected workers who work overtime hours and who are reclassified to overtime-protected status on average will receive increased earnings, because employers will not be able to fully adjust their regular rate of pay to the extent necessary to provide only the same level of earnings. As further explained in the economic impact analysis, workers whose exemption status changes also will see their work hours decrease on average, and the extra hours will be spread among other workers.[46] The Department views these outcomes as fully consistent with the dual purposes of the FLSA's overtime requirement: (1) spreading employment by

---

protected. See 80 FR 38574. However, as explained in section VI.D.iv., in response to comments that the Department underestimated the number of affected workers who work overtime, the Department has now 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 who work occasional overtime. Accordingly, we now estimate that 60.4 percent of affected workers will not receive any overtime premium.

[46] Not all employers will choose to cover the additional hours by hiring new employees. Employers will balance the benefits of the additional hours of work against the costs of hiring workers for those hours. In some cases, this will result in hiring new workers; in other cases, employers will have incumbent workers provide those additional hours.

incentivizing employers to hire additional employees, but rewarding those employees who are required to work overtime with time-and-a-half pay for overtime hours; and (2) avoiding detrimental effects on the health and well-being of employees by minimizing excessive working hours.

The Department recognizes that these outcomes are averages and some employees ultimately may receive lower earnings if their employers reduce their hours more extensively in an effort to ensure that no overtime hours are worked. However, such employees will receive extra time off. Therefore, the Department partially concurs with the comments of the individual employees and employee advocates who stated that the overall impact of the rule would benefit employees in a variety of ways, whether through an increased salary, overtime earnings when they have to work extra hours, time off, and/or additional hours of work for those who were previously unemployed or underemployed.

Some employers also asserted that employees reclassified as nonexempt would lose fringe benefits such as life insurance, disability insurance, increased vacation time, and bonuses and other incentive compensation that they provide only to exempt employees. The Department notes that employers may choose to continue to provide such benefits to workers who employers like ABA and IFA described as "critically important"; the design and scope of such fringe benefit and incentive compensation programs are within the employers' control. We see no compelling reason why employers cannot redesign their compensation plans to provide such fringe benefits and bonus payments based upon, for example, the employees' job titles rather than based upon their exemption status.[47]

[47] 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 such payments in the regular rate

With regard to the employer claim that employees reclassified to overtime-protected status would lose flexibility in their schedule or the ability to take a few hours off when needed for personal purposes, the Department notes that the employees who are affected by this Final Rule currently earn a salary between $455 per week and $913 per week (or between $23,660 and $47,476 per year). The results of the General Social Survey[48] research discussed in the EPI comment indicate that hourly-paid workers and salaried workers earning between $22,500 and $49,999 have little difference in workplace flexibility with regard to an employee's ability to modify his or her starting time or quitting time; a substantial increase in such flexibility is not seen until workers earn above $60,000. Moreover, workers paid hourly who earn between $40,000 and $49,999 actually reported more flexibility to take time off during the day than salaried workers in that pay range. Many of the comments the Department received from individual exempt employees similarly reflected a lack of current flexibility, with employees indicating they were routinely scheduled to work well in excess of 40 hours per week and also had to fill in for other employees who were out sick or on vacation or when positions were unfilled. Therefore, the Department does not believe that workers will incur the significant change in flexibility that some employers envisioned if the employer reclassifies them as nonexempt.

Employers also asserted that employees whose exemption status changes would lose the ability to work from home and outside of normal business hours, and they would lose the ability

---

calculation. One way to calculate and pay such bonuses is as a percentage of the employee's total earnings. Under this method, the payment of the bonus includes the simultaneous payment of overtime due on the bonus payment. See § 778.210.

[48] The General Social Survey, which started in 1972, is the largest project funded by the Sociology Program of the National Science Foundation. Except for the U.S. Census, it is the most frequently analyzed source of information in the social sciences. See http://www3.norc.org/GSS+Website/About+GSS/.

to attend after-hours training opportunities and meetings or to stay late to "get the job done." The Department understands employers' concerns regarding the need to control and keep accurate records of the work hours of overtime-eligible employees.[49] However, this Final Rule does not prohibit employers from continuing to allow such employees flexibility in the time and location where they work; most employees affected by this Final Rule are employees who employers now trust to exercise discretion and independent judgment with respect to matters of significance on behalf of the company or to supervise other employees and play a role in hiring, firing, and promoting other employees. Employers should be able to trust such valued employees to follow the employers' instructions regarding when, where, and for how many hours they may work and to accurately record their hours worked.[50] Moreover, as noted above, an estimated 60.4 percent of employees affected by this Final Rule do not work overtime hours now; the Department believes that any changes for this substantial portion of affected workers will be minimal. Further, 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. Nonetheless, for those employees who do work overtime and who become overtime eligible, the employers will have to evaluate, for example, whether training and other activities

[49] The Department included in the fall 2015 Regulatory Agenda our intent to publish a Request for Information seeking information from stakeholders on the use of electronic devices by overtime-protected employees outside of scheduled work hours.

[50] The Department notes that there is no particular order or form of records required. See 29 CFR 516.1(a). Employers may choose whatever form of recordkeeping works best for their business and their employees. For example, employers may require their employees to record their hours worked; alternatively, some employers might decide to record the hours themselves. Where an employee works a fixed schedule that rarely varies, the employer may simply keep a record of the schedule and indicate the number of hours the worker actually worked only when the worker varies from the schedule ("exceptions reporting"). 29 CFR 516.2(c). Furthermore, the Department believes that most employers already maintain recordkeeping systems for their overtime-eligible employees and that these systems can accommodate newly overtime-eligible employees.

that currently occur outside the normal work day, and for which employees currently receive no extra pay, should be moved to within the normal work day or whether they are important enough to warrant payment for any extra hours worked. However, because the Department has concluded that white collar employees earning a salary of less than $913 per week are not bona fide EAP workers, the Department concludes that if the employees perform extra work to "get the job done" they should be paid for all such time.

Regarding the employer assertion that the change in exemption status will harm employees because they will not be able to take time off without losing pay for the time away from work, the Department notes that employers are not required to change employees' pay basis from salaried to hourly simply because they are no longer exempt. Employers may continue to pay employees a salary, even when the employees are entitled to overtime pay if they work in excess of 40 hours per week. See §§ 778.113-.114. Moreover, even if newly overtime-eligible employees are converted to hourly status, employers are not required to dock such employees for the hours they take off. Therefore, employers have the authority to determine how to structure the pay plans of the newly overtime-eligible employees, and employers need not structure their pay plans in a manner that results in the potentially adverse effects that the employers identified.

Finally, employers asserted that the loss of exempt status would have a negative impact on employees' morale. However, the Department believes that for most employees their feelings of importance and worth come not from their FLSA exemption status but from the increased pay, flexibility and fringe benefits that traditionally have accompanied exempt status, as well as from the job responsibilities they are assigned. None of these are incompatible with overtime protection. Many exempt employee commenters expressed significant concern and low morale regarding their current situation, and they looked forward to an improved situation under the new

rule. Given the employers' emphasis on the important roles that these employees play in the success of their organizations, the Department anticipates that employers will strive to adapt to this rule in a way that minimizes the financial impact on their business while providing the maximum benefits, flexibility, and opportunities to their employees. If employers make these changes in a way that communicates the value they continue to place on the contributions of newly overtime-eligible workers, we are confident that employers can prevent employees from seeing their new entitlement to overtime protection as a demotion.

6. Impacts on Litigation

The Department also received several comments predicting the impact increasing the salary level would have on litigation. Commenters representing employees, such as the International Association of Fire Fighters (IAFF), stated that increasing the threshold would more clearly demarcate between employees who are entitled to overtime and those who are not, decreasing misclassification, and therefore, litigation, involving the EAP exemption. According to the joint comment submitted by 57 labor law professors, "the excessive importance of the duties test has resulted in the relatively high volume of litigation surrounding the exemptions and the many successful claims that have been asserted against employers in recent years," so raising the salary level "will benefit employers by providing them more certainty and relieve them of the litigation and other costs of disputes over classification and misclassification." Weirich Consulting & Mediation (Weirich Consulting) commented in support of the salary level change because it will make it easier "to determine more efficiently—and without needless litigation—whether or not particular employees are exempt." Other commenters representing employers disagreed, however, with Jackson Lewis, NAM, and the Wage and Hour Defense Institute predicting that finalizing the proposed salary level would increase (rather than decrease) litigation. Jackson

Lewis commented that the duties test is the main driver of litigation over the EAP exemption, and "there will be no end to litigation" so long as employers must continue to apply the standard duties tests to employees earning above the salary threshold. Jackson Lewis and NAM further asserted that the rule will result in additional litigation brought by "very dissatisfied" newly overtime-protected employees. Finally, Fisher & Phillips commented that the "collateral results" of selecting a particular salary level, including avoiding or reducing litigation, are not appropriate factors for setting the salary level required for the EAP exemption.

As we stated in the NPRM, the number of wage and hour lawsuits filed in federal courts increased substantially in the period between 2001 and 2012, from approximately 2,000 to approximately 8,000 per year, with stakeholders advising the Government Accountability Office that one of the reasons for the increased litigation was employer confusion about which workers should be classified as EAP exempt. See 80 FR 38531. Thus, these statistics support the Department's conclusion that the current standard salary level was not effective in 2004 at distinguishing between exempt and nonexempt workers and is substantially less effective today. Litigation under the FLSA remains high, with approximately 8,000 FLSA cases continuing to be filed each year.[51]

Although we did not establish the standard salary level in this Final Rule for the purpose of reducing litigation, we believe that reduced litigation will be one of the beneficial impacts of that increase. The salary level will once again serve as a clear and effective line of demarcation, thereby reducing the potential for misclassification and litigation. See Weiss Report at 8 (the salary tests prevent "the misclassification by employers of obviously nonexempt employees, thus tending to reduce litigation. They have simplified enforcement by providing a ready method of

[51] See http://www.uscourts.gov/statistics/table/c-2/statistical-tables-federal-judiciary/2014/12/31; http://www.uscourts.gov/statistics/table/c-2/federal-judicial-caseload-statistics/2015/03/31.

screening out the obviously nonexempt employees, making an analysis of duties in such cases unnecessary.”). Given the new standard salary level, there will be 9.9 million fewer white collar employees for whom employers could be subject to potential litigation regarding whether they meet the duties test (4.2 million currently EAP-exempt employees who will be newly entitled to overtime because they earn less than the new standard salary and 5.7 million overtime-eligible white collar employees paid between $455 and $913 per week whose exemption status no longer depends on the application of the duties test).[52]

7. Comments about Non-profit Employers

A substantial number of commenters also addressed the impact that the proposed standard salary would have on non-profit employers. While many of the concerns that the non-profit employers expressed were the same as those identified by other employers, some of these commenters also addressed particular concerns that they believe they would face due to their non-profit status.

Many non-profit employers, including Habitat for Humanity, the National Multiple Sclerosis Society, the New Jersey Association of Mental Health and Addiction Agencies, Operation Smile, Catholic Charities, and the U.S. Public Interest Research Group (USPIRG), emphasized that non-profits generally pay lower salaries than for-profit employers, and therefore the proposed salary level would not serve as an effective dividing line between employees performing exempt and overtime-protected work in the non-profit sector.

For example, USPIRG stated that 75 percent of employees it has classified as exempt receive a salary below the 40th percentile of full-time salaried workers nationally. Operation Smile commented that the proposed standard salary would increase its payroll costs by nearly $1

[52] The Department estimates that 732,000 of these white collar salaried workers are overtime-eligible but their employers do not recognize them as such. See section VI.C.ii.

million per year and affect more than 50 percent of its workforce. Habitat for Humanity similarly stated that the majority of its affiliates pay their highest paid employee less than $50,440 and estimated that approximately 40 percent of its affiliates' staff members would be directly affected by the proposed salary increase.

A number of non-profit commenters, including the Alliance for Strong Families and Communities, ANCOR, Catholic Charities, Easter Seals, Habitat for Humanity, and USPIRG, emphasized that they do not have the same ability as other employers to increase prices or reduce the profits paid to shareholders to compensate for the increased costs of the proposed salary; some noted this is because the prices for the services they provide are set in government contracts or by Medicaid, or because their revenue is based on grants reflecting labor costs at the time the grant is made and there may be no option for seeking an increase in funding. Several nonprofits expressed concern that they are constrained in their ability to increase salaries for their staff because funders evaluate them based on their ability to keep overhead, including salary costs, low, or because the terms of their grants may strictly limit how much of the grant can be allocated for overhead. See, e.g., Boy Scouts of America; Food Bank of Northern Nevada; The Groundwater Foundation; Operation Smile. Based upon these funding issues, many commenters stated that the unintended consequence of the increased standard salary level would be a decline in the quantity or quality of the critical services they provide to vulnerable individuals. See, e.g., CUPA-HR; Father Flanagan's Boys' Home; Lutheran Services in America; National Multiple Sclerosis Society; Salvation Army. Therefore, many non-profit organizations requested that the Department provide special relief for non-profits such as: an exemption from the salary requirement; a reduced salary level for non-profits; an incremental phased-in increase of the salary level over a period of a year or more for non-profits; a delayed implementation date for

non-profits; and the elimination of automatic updating for non-profits. See, e.g., Alliance for Strong Families and Communities; Boy Scouts of America (BSA); Boys and Girls Clubs of America; Habitat for Humanity; Independent Sector; United Community Ministries; YWCA.

Nevertheless, despite their concerns regarding the potential impact of the proposed salary level, many non-profit employers expressed their general support for the intent and purpose of the rule. See, e.g., Catholic Charities; Easter Seals; Independent Sector; Maryland Nonprofits; PathStone Corporation; United Community Ministries; YWCA. Moreover, some non-profits, citing their role as both employers and service providers, supported the application of the NPRM to non-profits as proposed. For example, PathStone Corporation, and a comment submitted by CASA on behalf of 21 additional non-profit organizations, stated they fully supported the proposed regulation, with the joint CASA comment emphasizing that the "justice we seek for our clients in the world must also exist within our own organizations." Similarly, Maryland Nonprofits commented that "[t]he nonprofit community recognizes better than most the harsh economic realities that lead to this proposed rule, and we strongly endorse its purpose,"

Other commenters indicated that the impact on non-profit employers would not be as significant as most non-profits feared. For example, the comment submitted by 57 labor law professors noted that an economist found that management employees working for non-profits earned an average of $34.24 per hour in 2007, which far exceeds the proposed salary level, and that they presumably earn more than that now. Therefore, they concluded that the regulations "should not have a deleterious effect on these valuable organizations or their efforts to accomplish their important missions." EPI also stated that, where a non-profit is engaged in revenue-producing activities and, thus, is competing with for-profit businesses, it "is only fair" that "it should be held to the same employment standards" to achieve a level playing field with

regard to the employees who are involved with that commercial business or who are engaged in interstate commerce. Other commenters, such as the Wisconsin Association of Family and Children's Agencies, questioned the wisdom of a non-profit exemption, explaining that for-profit agencies may perform the same services as non-profits and rely on the same government funding streams and a non-profit exemption would not help the similarly situated for-profit service providers.

The Department recognizes and values the enormous contributions that non-profit organizations make to the country. Nonprofit organizations provide services and programs that benefit many vulnerable individuals in a variety of facets of life, including services that benefit the vulnerable workers who the Department also works to protect by ensuring that their workplaces are fair, safe, and secure. In response to the commenters' concerns, we note that (as discussed in detail above) we have modified the proposed salary level to account for the fact that salaries are lower in some regions than others. This change yields a salary at the low end of the historical range of short test salaries. This lower final salary level will also provide relief for non-profit employers, just as it does for employers in low-wage industries.

However, regarding the commenters' suggestions that we create a special exemption from the salary requirement, a lower salary level, a delayed implementation date, or a phase-in period for non-profits, we note that the Department's EAP exemption regulations have never had special rules for non-profit organizations; the employees of non-profits have been removed from minimum wage and overtime protection pursuant to the EAP exemptions only if they satisfied the same salary level, salary basis, and duties tests as other employees.

The Department concludes that such special treatment is not necessary or appropriate. As the comment from the 57 labor law professors noted, a study of National Compensation Survey data

showed that the average hourly wage of full-time management employees in the not-for-profit sector was $34.24 per hour in 2007 ($1,369 per 40-hour workweek), which substantially exceeds the Final Rule's required salary of $913 per week.[53] The average hourly wage for such management workers at non-profits had increased to $38.67 by 2010 ($1,547 per 40-hour week), which is more than 50 percent higher than the 2016 required standard salary.[54] Moreover, the average hourly wages of non-profit employees are not uniformly lower than those of employees in other sectors. For example, in 2007 the average hourly wages of both full-time business and financial operations employees and computer and mathematical science employees working at non-profits, $26.49 and $32.00 per hour, respectively, exceeded the average hourly earnings of such workers employed in State government.[55] Wages of full-time workers in healthcare practitioner and technical occupations for non-profits averaged $28.85 per hour in 2007, higher than those for employees in the same occupations in State and local governments ($23.89 and $27.30, respectively). Similarly, the 2007 average earnings of registered nurses were $30.80 per hour at non-profits, higher than those of registered nurses at private establishments ($30.58) and at State and local governments ($29.60).[56]

Based on CPS data, the Department projects that for FY 2017, the median weekly earnings for affected workers in non-profits will be $741.68 while the median weekly earnings of affected workers in the private sector will be $745.54. The Department recognizes however, that non-

---

[53] See http://www.bls.gov/opub/mlr/cwc/wages-in-the-nonprofit-sector-management-professional-and-administrative-support-occupations.pdf. The non-profit series was stopped in 2010 and the 2007 report on management, professional and administrative support occupations is the most recent data available.
[54] See http://www.bls.gov/ncs/ncswage2010.htm (Table 33).
[55] See http://www.bls.gov/opub/mlr/cwc/wages-in-the-nonprofit-sector-management-professional-and-administrative-support-occupations.pdf.
[56] See http://www.bls.gov/opub/mlr/cwc/wages-in-the-nonprofit-sector-healthcare-personal-care-and-social-service-occupations.pdf.

profit entities may have a higher share of affected workers than for-profit entities, but does not believe that this will unduly impact this sector. If all affected workers in the non-profit sector who regularly work overtime were increased to the new salary level this would increase the total amount that non-profits pay EAP workers by 0.5 percent, compared to an increase of 0.3 percent in other sectors.[57] Therefore, the Department concludes that treating non-profit employers differently than other employers, such as by creating a special salary level or an extended phase-in period is not appropriate and is not necessary, particularly given the fact that the Final Rule modifies the proposed rule by basing the standard salary level on salaries in the lowest-wage Census Region.

Finally, the Department also received comments from a number of non-profit higher education institutions. As discussed above, some commenters from the higher education community also asked for guidance on the application of the EAP exemption to educational institutions. Additionally, however, several commenters expressed concern about the impact that the Final Rule would have on higher education, with some suggesting a lower salary level for educational institutions. See, e.g., Iowa Association of Community College Trustees; CUPA-HR; Purdue University; South Carolina Independent Colleges and Universities. We recognize that higher education is a complex and important sector in our economy, including a variety of both private and public institutions, from small community colleges to large research institutions.

Commenters representing research institutions raised concerns about the impact of the proposed rule on postdoctoral researchers. For example, CUPA-HR noted that the National Institutes of Health (NIH) stipend levels for post-doctoral researchers are "well below" the

[57] This is an overestimate as to both the non-profit and for-profit sectors. As explained in section VI.D. iv., we anticipate employers will increase the salary level only for workers for whom it is less expensive to pay the updated salary level than pay overtime.

proposed salary level and that post-doctoral researchers with less than five years of experience would no longer meet the salary level for exemption. The Department notes that the Final Rule salary level based on the 40th percentile in the lowest-wage Census Region addresses some of these concerns and results in a salary level met by the NIH FY 2016 stipend level for post-doctoral researchers with at least three years of experience and is only $208 a year above the stipend level for a post-doctoral researcher with two years of experience.

8. Other Comments

Like non-profit employers, other commenters, including local governments,[58] Indian tribes, for-profit entities receiving government funding, and commenters writing on behalf of small businesses, asserted that they do not have the same ability as other employers to increase prices or reduce their profits.[59] See, e.g., BFT Holding; Charlotte County Government; Jamestown S'Klallam Tribe. Some commenters representing these groups, as well as other commenters, requested special treatment for certain industries or employers. For example, some small businesses and commenters representing them, including the American Association for Enterprise Opportunity, California Association for Micro Enterprise Opportunity, and WIPP, requested an exemption for small entities from the salary level or from the FLSA's requirements generally. Likewise, the Gila River Indian Community and the Ute Mountain Ute Tribe submitted comments urging the Department to "open consultation with Indian tribes on the use

[58] The Department notes that state and local governments have greater options for satisfying their overtime obligations than do private employers. In particular, under certain conditions, state or local government agencies may provide their employees with compensatory time off (comp time) instead of cash payment for overtime hours. The comp time must be provided at a rate of one-and-one-half hours for each overtime hour worked. For example, if a newly overtime-eligible state government employee works 44 hours in a single workweek, he would be entitled to 6 hours of compensatory time off. See 29 CFR part 553.

[59] Comments from state and local governments and from Indian tribes are also addressed in section VIII.

of a lower salary threshold for tribal entities" based on "the unique economic and demographic factors that tribes face." The Department did not propose special treatment for small businesses, tribal governments, or other entities, and did not request comment on these issues. The Department believes such special treatment is not necessary given that the Final Rule modifies the proposed rule by basing the standard salary level on salaries in the lowest-wage Census Region and this lower final salary level will provide relief for these stakeholders.

Conversely, some commenters requested that the Department apply the salary level test to employees who have historically not been subject to that test. For example, the Department received multiple comments from teachers, university faculty, and their representatives, asking us to repeal § 541.303(d), which provides that the salary level requirement does not apply to teaching professionals. See, e.g., National Association for the Education of Young Children (NAEYC); NWLC; New Faculty Majority Foundation; SEIU. As the NAEYC acknowledged in its comment, this request is "beyond the scope" of the NPRM, which did not propose changes to or invite comment on § 541.303(d) or on § 541.600(e), which also provides that the salary requirement does not apply to teachers and certain other professionals. See also NWLC; SEIU. The Department notes that regardless of their salary, teachers qualify for the professional exemption only if they have a primary duty of teaching, tutoring, instructing or lecturing in the activity of imparting knowledge and are employed and engaged in this activity as a teacher in an educational establishment by which they are employed.[60] See § 541.303(a).

[60] The National Head Start Association and several other commenters associated with Head Start asked the Department to consider adopting the position that all Head Start and Early Head Start facilities are "educational establishments," and therefore that teachers at these facilities can meet the professional exemption. The NPRM did not propose changes to or invite comment on § 541.303(a) or § 541.204(b) (which defines "educational establishment"), and the Final Rule makes no changes to these sections.

A number of comments, including a joint comment from the AIA-PCI, requested that the Department prorate the new salary level for part-time employees. The Department declines this request. That employers currently "can afford to pay part-time exempt employees the full salary required for exempt status, even if they work just 15 or 20 hours per week," as Seyfarth Shaw noted in support of this request, merely underscores the need to significantly increase the 2004 salary level. The Department has never prorated the salary level for part-time positions, and we considered and rejected a special rule for part-time employees performing EAP duties in 2004. See 69 FR 22171. The Department continues to believe that such a rule would be difficult to administer, and notes that the FLSA does not define full-time employment or part-time employment, but leaves this matter to be determined by employers. 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 provisions of the FLSA so long as the salary equals at least the minimum wage when divided by the actual number of hours the employee worked. See FLSA2008-1NA (Feb. 14, 2008). Employers can meet this standard with a salary of as little as $145 for twenty hours of work per week, and $217.50 for 30 hours of work per week—far below even the 2004 salary level.[61]

Finally, a small number of commenters, including the National Automobile Dealers Association, suggested that the Department should eliminate the salary level test entirely, so that the exempt status of every employee would be determined on the basis of their job duties and

[61] SIFMA noted that some employees who will not meet the salary threshold because they work part time, may nevertheless have responsibilities during certain periods (for example, tax season) that require them to work more than 40 hours in a week. In such instances, if the employee earns less than the standard salary level, the employee is eligible to receive overtime premium pay for hours worked over 40 in a week.

responsibilities alone. The Department has repeatedly rejected this approach, and we do so again in this rulemaking. The Department has long recognized that "the amount of salary paid to an employee is the 'best single test' of exempt status," and is the principal delimiting requirement preventing abuse. 69 FR 22172; Stein Report at 24. Further, as the Department explained in 2004, eliminating the salary test is contrary to the goal of simplifying the application of the exemption, which the President has directed us to do in this rulemaking, and would require a "significant restructuring of the regulations," including the "use of more rigid duties tests." 69 FR 22172.

B. Special Salary Tests

i. American Samoa

As explained in our proposal, 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. See 80 FR 38534. The Fair Minimum Wage Act of 2007, as amended, provides that industry-specific minimum wages rates in American Samoa will increase by $0.40 on September 30, 2018, and continue to increase every three years thereafter until each equals the federal minimum wage. See Sec. 1, Pub. L. 114-61, 129 Stat. 545 (Oct. 7, 2015). The minimum wage in American Samoa currently ranges from $4.58 to $5.99 an hour depending on the industry,[62] and so the disparity with the federal minimum wage is expected to remain for the foreseeable future. Accordingly, the Department proposed to continue our longstanding practice of setting the special salary level test for employees in American Samoa at approximately 84 percent of the standard salary level, which would have resulted in a salary of $816 based on fourth quarter 2015 data for full-time salaried workers nationwide.

[62] See WHD Minimum Wage Poster for American Samoa, available at: http://www.dol.gov/whd/minwage/AmericanSamoa/ASminwagePoster.pdf.

The Department received only one comment on this aspect of our proposal—Nichols Kaster supported the proposed increase. We conclude that the proposed methodology remains appropriate, and the Final Rule accordingly sets the special salary level for American Samoa at 84 percent of the standard salary level set in the rule, which equals $767 per week. The Department has revised § 541.600(a) accordingly.

ii. Motion Picture Producing Industry

The Department has permitted employers to classify as exempt employees in the motion picture producing industry who are paid at a base rate of at least $695 per week (or a proportionate amount based on the number of days worked), so long as they meet the duties tests for the EAP exemptions. See § 541.709. This exception from the "salary basis" requirement was created in 1953 to address the "peculiar employment conditions existing in the [motion picture] industry," 18 FR 2881 (May 19, 1953), and applies, for example, when a motion picture industry employee works less than a full workweek and is paid a daily base rate that would yield at least $695 if six days were worked. See id. Consistent with our practice in 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 $1,404 per week (or a proportionate amount based on the number of days worked). This method would have resulted in a base rate of $1,487 based on fourth quarter 2015 data for full-time salaried workers nationwide.

The Department did not receive any substantive comments on this subject; two commenters, Nichols Kaster and the UAW, offered general support for this proposal. The Final Rule adopts the methodology set forth in our proposal, and using the new standard salary level ($913) results

in a base rate of $1,397 per week (or a proportionate amount based on the number of days worked).[63] The Department has revised § 541.709 to incorporate this change.

iii. Other Comments Requesting Special Salary Tests

The Department also received approximately a dozen comments concerning application of the proposed salary level to Puerto Rico. Nearly all of these commenters urged the Department to either exempt Puerto Rico from the updated standard salary level requirement (thus keeping the salary level at $455) or to reinstate a special salary level test for Puerto Rico (set between the current and proposed salary levels).[64] In 1949, the Department established a special salary level for Puerto Rico because its minimum wage rate was below the FLSA minimum wage. See 14 FR 7705-06 (Dec. 24, 1949); Weiss Report at 21. The Fair Labor Standards Amendments of 1989 removed Puerto Rico from the special minimum wage provisions and instead applied the section 6(a)(1) minimum wage to Puerto Rico. See Sec. 4, Pub. L. 101-157, 103 Stat. 938 (Nov. 17, 1989). This change eliminated the justification for maintaining a special salary test in Puerto Rico, and so in the 2004 Final Rule we established that the standard salary level test applies to Puerto Rico. Puerto Rico continues to be subject to the section 6(a)(1) minimum wage, and the Department has consistently maintained a uniform salary level for all states and also for all territories subject to the FLSA minimum wage.

[63] The Department calculated this figure by dividing the new salary level ($913) by the current salary level ($455), and then multiplying this product (rounded to the nearest hundredth) by the current base rate ($695). This produces a new base rate of $1,396.95, which we rounded to the nearest whole dollar ($1397).

[64] Commenters included the Cadillac Group of Companies, Caribbean Restaurants, the Puerto Rico Bankers Association, the Puerto Rico Chamber of Commerce, the Puerto Rico Hotel & Tourism Association, the Puerto Rico Manufacturers Association, the Secretary of Labor for Puerto Rico (the Honorable Vance Thomas), the Training and Labor Affairs Advisory and Human Resources Administration Office (OCALARH, by its Spanish acronym), one individual commenter, and one anonymous commenter. Two individual employee commenters from Puerto Rico offered general support for the Department's proposal.

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

As indicated in the NPRM, the Department has consistently assessed compliance with the salary level test by looking only at actual salary or fee payments made to employees and, with the exception of the total annual compensation requirement for highly compensated employees, has not included bonus payments of any kind in this calculation. During stakeholder listening sessions held prior to the publication of the NPRM, several business representatives asked the Department to include nondiscretionary bonuses and incentive payments as a component of any revised salary level requirement. These stakeholders conveyed that nondiscretionary bonuses and incentive payments are an important component of employee compensation in many industries and stated that such compensation might be curtailed if the standard salary level was increased and employers had to shift compensation from bonuses to salary to satisfy the new standard salary level.

In recognition of the increased role bonuses play in many compensation systems, and as part of the Department's efforts to modernize the overtime regulations, the Department sought comments in the NPRM regarding whether the regulations should permit nondiscretionary bonuses and incentive payments to count towards satisfying a portion of the standard salary level test for the executive, administrative, and professional exemptions.[65] Specifically, the Department asked whether employers should be allowed to use nondiscretionary bonuses and incentive payments, paid no less often than monthly, to satisfy up to 10 percent of the standard salary level test. To ensure the integrity of the salary basis requirement, the Department stressed

[65] Promised bonuses such as those announced to employees to induce them to work more efficiently or to remain with the firm are considered non-discretionary. See 29 CFR 778.211(c). Examples include individual or group production bonuses, and bonuses for quality and accuracy of work. Incentive payments, including commissions, are also considered non-discretionary.

the importance of strictly limiting the amount of the salary requirement that could be satisfied through the payment of nondiscretionary bonuses and incentive pay, as well as the maximum time period between such payments. The Department did not propose any changes to how bonuses are treated under the "total annual compensation" requirement of the HCE test, and stated that we were not considering changing the exclusion of board, lodging, or other facilities from the salary calculation or expanding the salary level test calculation to include discretionary bonuses, payments for medical, disability, or life insurance, or contributions to retirement plans or other fringe benefits. See, e.g., 80 FR 38535-36, 38537 n.36. However, the Department did seek comment on the appropriateness of counting commissions toward the salary level requirement.

The requirement that exempt employees be paid on a salary basis has been a part of the Department's part 541 regulations since 1940. As the Department said at that time, "a salary criterion constitutes the best and most easily applied test of the employer's good faith in claiming that the person whose exemption is desired is actually of such importance to the firm" that he or she is properly within the exemption. Stein Report at 26, see also id. at 19, 36. Since 1940, therefore, the regulations have required that an exempt EAP employee be paid a predetermined and fixed salary that is not subject to reduction because of variations in the quality or quantity of work performed. More recently, the Department has noted "that payment on a salary basis reflects an employee's discretion to manage his or her time and to receive compensatory privileges commensurate with exempt status." 69 FR 22177. While, as the Department noted in the NPRM, employers are allowed to pay additional compensation beyond the required salary in the form of bonuses, those payments have not counted towards the payment of the required minimum salary level. The Department's discussion in the NPRM of including nondiscretionary

bonus payments in the standard salary level was informed by our concern that permitting the standard salary level to be satisfied by bonus payments that frequently correlate to the quantity and quality of work performed could undermine the utility of the salary basis requirement in identifying bona fide EAP employees.

The Department received a variety of comments concerning whether the regulations should permit nondiscretionary bonuses and incentive payments to satisfy a portion of the standard salary level test. Commenters representing employers generally supported this change as an improvement over the current regulations, though many objected that the option the Department was considering was too restrictive. Most of the commenters representing employees that addressed this idea opposed it on the grounds that it would complicate the test for exemption and undermine the worker protections established by the salary basis requirement.

Commenters representing employers offered a range of reasons for generally supporting the inclusion of nondiscretionary bonuses and incentive payments. Many commenters, including ACRA, the National Association of Convenience Stores (NACS), and the NRA, agreed that such payments are a key part of exempt employees' compensation in their industries. For example, EBS Building Supplies stated that its managers "can earn as much in bonus payments as they earn in regular salary during the year," and Mill Creek Companies stated that nondiscretionary performance incentives can account for "up to 40% of a person's total compensation and are a most critical part of our strategy to align the goals of first line supervisors and professionals with the goals of the company."

WorldatWork conducted a survey of its human resources manager members and found that "62% of respondents said their employers offer nondiscretionary incentive bonuses tied to productivity and/or profitability." Several trade associations reported similar feedback from their

members. The World Floor Covering Association stated that its "members have indicated that many managers and administrators receive bonuses based on the sales of the stores that they manage or oversee," and the National Pest Management Association stated that 93 percent of its member companies reported providing some form of nondiscretionary bonuses. The Chemical Industry Council of Illinois and the National Council of Farmer Cooperatives respectively emphasized that nondiscretionary bonuses "are an integral part" or "play an important role" within an employee's total compensation package. RILA noted that in the retail industry "many retail managers and other exempt employees earn bonuses or other incentive payments designed to encourage a sense of ownership consistent with their important leadership roles within the organization," and that "[c]ounting non-discretionary bonuses toward the minimum threshold for exemption is consistent with the purpose of the salary level test—the payment, criteria, or amount of these bonuses often reflects the exempt status of the recipients."

Many commenters that opposed the Department's proposed increase to the standard salary level, including CalChamber Coalition, Fisher & Phillips, FMI, Littler Mendelson, and the National Association of Professional Insurance Agents, acknowledged that allowing employers to satisfy a portion of the salary level with bonuses and incentive payments would to some extent mitigate the financial burden of the proposed increase. Other commenters, including IFA and the Sheppard Mullin law firm, stated that not allowing nondiscretionary bonuses and incentive payments to satisfy some portion of the increased salary level would likely reduce the prevalence of those forms of compensation.

Among commenters that supported the inclusion of nondiscretionary bonuses and incentive payments in the standard salary guarantee amount, many objected that the option considered in the Department's NPRM was too restrictive to be of much practical use for employers. For

example, several commenters representing employers criticized the Department's proposal to cap the crediting of nondiscretionary bonuses or incentive payments at no more than 10 percent of the standard salary level, noting that bonuses, incentive payments, and commissions often comprise a far greater portion of an exempt employee's total compensation. The Chamber stated that "unless the Department reconsiders its proposed $50,440 salary level, a limit of 10 percent (or, $5,044) is too low to provide any relief or make the additional administrative burdens worth the effort." FMI, the National Association of Truck Stop Operators, Printing Industries of America, RILA, Weirich Consulting, and a number of other commenters requested that the Department allow such compensation to count for up to 20 percent of the standard salary level. Other commenters suggested a higher percentage, including CalChamber Coalition (at least 30 percent), ACRA (at least 40 percent), and HR Policy Association (50 percent). Many commenters, including Fisher & Phillips, the National Beer Wholesalers Association, and the National Pest Management Association, opposed the imposition of any percentage cap on the proportion of the salary level test that could be satisfied with such payments. Several commenters, however, supported the Department's 10 percent limitation. See, e.g., Concord Hospitality Enterprises; Fraternity Executive Association.

Commenters also criticized the Department's decision to consider crediting nondiscretionary bonuses and incentive payments toward the salary level test only if they are paid on a monthly or more frequent basis. According to AIA-PCI and PPWO, such a limitation fails to account for the fact that bonus payments "are typically made less often than monthly because they are tied to productivity, revenue generation, profitability, and other larger and longer-term business results that can fluctuate significantly on a month-to-month basis." See also NRA. AH&LA stated that many "supplemental compensation programs in the lodging industry are not structured to be paid

with such frequency and it would place a significant administrative burden on employers to calculate and pay incentive compensation on a monthly or more frequent basis." AH&LA and many other commenters requested that the Department credit bonuses and incentive payments paid on an annual basis against the salary level. HR Policy Association pointed out that bonuses paid annually are already included within the "total compensation requirement" under the HCE test, while the Society of Independent Gasoline Manufacturers (SIGMA) stated that "permitting employers to count bonuses annually incentivizes them to hire employees on an annual basis, ultimately promoting job security and long-term employment." In the absence of crediting annual bonuses, SIGMA and several other commenters, including IABI, AIA-PCI, the American Institute of Certified Public Accountants, PPWO, and Weirich Consulting, urged the Department to credit bonuses and incentive payments paid on a quarterly basis or less frequently. Other commenters favored the quarterly frequency outright. See, e.g., American Resort Development Association; Fraternity Executives Association. Fisher & Phillips and the NACS opposed imposing any timeframe limitation, but conceded that "experience suggests [quarterly] is a not-uncommon frequency for the payment of such amounts."

Several commenters requested that the Department allow employers to make catch-up (or "true-up") payments to eliminate the risk of non-compliance in the event that an employee's bonuses or incentive payments drop such that the employee fails to satisfy the salary level requirement in a given period. For example, SIFMA wrote that they saw "no basis for distinguishing the use of true-up payments outside of the context of highly compensated employees," and remarked that "[a]llowing true-up payments to count helps ensure that exempt employees are receiving the guaranteed income they anticipated and is consistent with the historical salary basis approach of ensuring guaranteed income." If annual catch-up payments

are not permitted, NRA urged the Department "to permit employers to make catch-up payments based on when they pay the bonuses, i.e., monthly, semi-annually, or quarterly."

Many commenters that supported the crediting of incentive payments urged the Department to also allow employers to credit commissions. Several commenters agreed with PPWO that "all forms of compensation should be used to determine whether the salary level has been met," pointing out that the CPS earnings data for nonhourly employees that the Department is using to derive the standard salary level includes discretionary bonuses and commissions. Many commenters disputed the Department's observation in the NPRM that "employees who earn commissions are usually sales employees who . . . are generally unable to satisfy the standard duties test," 80 FR 38536. AT&T stated that it "has management positions whose responsibilities involve the supervision of sales teams and support sales channels that receive commissions as part of their salaries and that have been found to be exempt under the executive and administrative exemptions," and the Chamber and FMI likewise commented that in the real estate and insurance industries "[m]any exempt employees who perform little direct sales work share commissions." A few other commenters pointed to a 2006 opinion letter advising that certain "registered representatives" in the financial services industry qualify for the administrative exemption even though they receive commissions and bonuses in addition to their salary. See FLSA2006-43 (Nov. 27, 2006).

Other commenters urged the Department to count discretionary bonuses toward the salary level. For example, PPWO stated that "[s]uch payments are in many ways even more reflective of an individual employee's efforts and contributions (and by implication their exercise of independent judgment and other characteristics of the duties' test) than nondiscretionary bonuses."

Many commenters opposed permitting nondiscretionary bonuses and incentive payments to satisfy a portion of the standard salary level test. Some commenters stated that nondiscretionary bonuses and incentive payments do not indicate an employee's exempt status. For example, NELA and Rudy, Exelrod, Zieff & Lowe wrote that the types of nondiscretionary bonuses described in the Department's regulations—including "bonuses that are announced to employees to induce them to work more steadily, rapidly, or efficiently; bonuses to remain with the employer; attendance bonuses; individual or group production bonuses; and bonuses for quality and accuracy of work"—are "intended to incentivize workers of all types to perform their duties well; but, do not afford them any benefits of ownership." These commenters noted further that lower level employees whom they have represented also received these types of bonuses, and thus, the commenters concluded that such bonuses "have no bearing on whether an employee should be excluded from overtime requirements." The Georgia Department of Administrative Services and the Mississippi State Personnel Board each cautioned that there is "no guarantee that the work rewarded by the bonus or incentive payment will be FLSA exempt in nature," while KDS Consulting stated that crediting bonuses and incentive payments would undermine the premise "that management values the salaried worker's position for some reason outside of time and task."

Several commenters asserted that allowing nondiscretionary bonuses and incentive payments to satisfy a portion of the standard salary level would dramatically complicate application of the EAP exemptions, and introduce periodic uncertainty regarding the exempt status of employees who would need such payments to meet the salary level requirement. Nichols Kaster stated that allowing nondiscretionary bonuses and incentive payments to satisfy 10 percent of the standard salary level "could alter employees' exempt status on a weekly basis," and put employers in a

position where they "would incur substantial compliance costs reviewing their payroll on a weekly or monthly basis to determine which employees satisfied the salary basis test" (emphasis in comment). AFL-CIO and IAFF each wrote that the proposal would be "in direct contradiction to the purpose of the proposed rule, which is to clarify, streamline and simplify the regulations," while NELA and Rudy, Exelrod, Zieff & Lowe commented that "[a]dding this component to the threshold inquiry would only make the calculation more confusing and spur additional transaction costs to what should be a straightforward computation." Nichols Kaster, NELA, and The Labor Board, Inc., each warned that allowing bonuses to satisfy a portion of the standard salary level would likely increase FLSA litigation, while AFL-CIO noted that permitting nondiscretionary bonuses and incentive payments to satisfy a portion of the standard salary level "could lead to anomalous results" where employees with similar job duties could be classified differently depending on the criteria for the bonuses.

Commenters also contended that allowing nondiscretionary bonuses and incentive payments to satisfy a portion of the standard salary level would undermine the scheduling flexibility and income security associated with exempt status, as codified in the salary basis requirement. Nichols Kaster opined that such a change "erodes the salary basis test . . . [by] replac[ing] the certainty of a salary with the uncertainty of fluctuating compensation," and would have the practical effect of reducing the standard salary level. NELA and Rudy, Exelrod, Zieff & Lowe agreed, stating that the Department's proposal "runs contrary to the stated purpose of the salary basis test, which is to make sure exempt employees are guaranteed a minimum level of income that is dependable and predictable to meet their families' monthly expenses before they are exempted from the protections of the overtime provisions of the FLSA." These commenters further indicated that "[c]hanging the salary threshold calculation to include nondiscretionary

bonuses would also create a perverse incentive to employers to move towards implementing more deferred compensation pay structures." Nichols Kaster wrote that "an exempt employee who chooses not to leave work early for a parent-teacher conference for fear of missing a weekly production metric loses some of the benefit of her exempt status: the receipt of her full pay for any week in which she performs any work without regard to the number of days or hours worked" (internal quotation marks and citation omitted). Moreover, Nichols Kaster asserted that "an 'attendance bonus' that penalizes an employee for partial day absences would be nothing more than an end-around the existing prohibition on partial day deductions from salary."

Finally, some commenters warned of possible negative consequences that might result from allowing bonuses and incentive payments to satisfy a portion of the standard salary level. For example, the Georgia Department of Administrative Services and the New Mexico State Personnel Board stated that crediting such payments would create "a competitive disadvantage for public sector employers," because public employers are not able to provide non-discretionary bonuses and incentive payments. KDS Consulting speculated that allowing bonuses and incentive payments to satisfy a part of the standard salary level would undermine the incentivizing value of such payments, to the extent that employers must pay them to maintain the exempt status of their employees.

After considering the comments, the Department has decided to permit nondiscretionary bonuses and incentive payments (including commissions) to satisfy up to 10 percent of the standard weekly salary level test, provided these forms of compensation are paid at least quarterly. The Final Rule revises § 541.602(a) to incorporate this new flexibility.

The Department analyzed comments mindful of the need to ensure that the salary level test accounts for employer payment practices without compromising the critical function of the

salary basis test, which is to serve as a key indicator of exempt status. Commenters representing employer interests persuasively explained that nondiscretionary bonuses are an important part of many employer compensation systems that cover EAP employees. Modifying the tests for exemption to incorporate this fact is consistent with the President's directive to modernize the part 541 regulations. The Department also recognizes the concerns expressed by employee advocates, however, that in some instances nondiscretionary bonuses may not be indicative of exempt status and that counting such compensation toward the standard salary level may undermine the flexibility and income security associated with exempt status. While we share the concern that some bonus and incentive programs cover both overtime exempt and overtime-eligible employees, and the correlation of those programs with exempt status is therefore questionable, we are persuaded overall that the provision of nondiscretionary bonus and incentive payments has become sufficiently correlated with exempt status (for example, as evidence of the overtime exempt employee's exercise of management skill or exercise of independent judgment) that its inclusion on a limited basis in the standard salary requirement is appropriate. However, because such payments also correlate directly or indirectly in many instances with either the quantity or quality of work performed, we believe that careful limits must be set on how nondiscretionary bonuses and incentive pay are applied to the salary level test.

The Department also sought comments on the appropriateness of including commissions as part of nondiscretionary bonuses and other incentive payments that could partially satisfy the standard salary level test. In the NPRM, we raised the concern that it may be inappropriate to count commissions toward the salary level because employees who earn commissions are usually sales employees who—with the exception of outside sales employees—are generally unable to

satisfy the duties test for the EAP exemptions. Comments from the Chamber, FMI, AT&T, and others have convinced us that it is not uncommon for employees who are not sales personnel, such as supervisors of a sales team, to earn commissions based on the sales of the employees they supervise. Since such supervisors may satisfy the duties test, the Department has concluded that it is appropriate to treat commissions like other types of nondiscretionary bonuses and permit them to be used to satisfy a portion of the salary level test. Accordingly, we have concluded that permitting commissions to count against a limited portion of the standard salary will not undermine the effectiveness of the salary basis test in identifying exempt employees. This change will also ensure that exemption status does not depend on (and that this rulemaking does not interfere with) whether an employer chooses to label or structure a nondiscretionary incentive payment as a "bonus" or as a "commission." This change is also consistent with the Department's position that certain "registered representatives" in the securities and financial services industry who receive commissions may qualify for the administrative exemption. See FLSA2006-43 (Nov. 27, 2006).

In the NPRM, the Department stated that we were not considering expanding the salary level test calculation to include discretionary bonuses or changing the exclusion of board, lodging, or other facilities from the salary calculation, a position that the Department has held consistently since the salary requirement was first adopted. The Department also declined to consider including in the salary requirement payments for medical, disability, or life insurance, or contributions to retirement plans or other fringe benefits. The Department reemphasizes here that such forms of compensation remain excluded from the salary level test calculation.

Many commenters asked the Department to increase beyond 10 percent the portion of the standard weekly salary level employers could satisfy using nondiscretionary bonuses and

incentive payments. After consideration, the Department declines these requests. Because the Department has long found that the payment of a fixed predetermined salary not subject to change based on the quantity or quality of work is a strong indicator of exempt EAP status, it is important to strictly limit the percentage of the salary requirement that nondiscretionary bonuses and incentive payments can satisfy. Accordingly, setting the limit above 10 percent could undermine the premise of the salary basis test by depriving workers of a predetermined salary that does not fluctuate because of variations in the quality or quantity of their work and thus is indicative of their exempt status.[66] We believe that a 10 percent limit is also appropriate given that we are including nondiscretionary bonuses, incentive payments, and commissions as part of the salary level test for the first time and the full impact of this change on determination of EAP status is not yet known. Because this is the first time we have included nondiscretionary bonuses, incentive payments, and commissions, the Department may revisit this threshold if future experience supports additional changes to § 541.602(a)(3).

The Department takes note of comments from government employers that expressed their view that inclusion of nondiscretionary bonuses and incentive payments in the salary level creates a competitive disadvantage for them. The Department believes that by limiting to 10 percent the amount of nondiscretionary bonuses and commissions that can count toward the required weekly minimum salary level, we strike an appropriate balance which allows employers to use expanded sources of income to meet the required salary level, does not unduly harm government employers, and ensures that the salary basis requirement remains "a valuable and

[66] This 10 percent limit concerns an employer's ability to count nondiscretionary bonuses, incentive payments, and commissions toward the salary level requirement without violating the salary bases requirement. This limit does not impact an employer's continued ability to provide an exempt employee with additional compensation without losing the exemption or violating the salary basis requirement, provided the employment arrangement also includes a guarantee of at least the minimum weekly-required amount paid on a salary basis. See § 541.604 (a).

easily applied criterion that is a hallmark of exempt status." 69 FR 22175. The Department also acknowledges the concern articulated by AFL-CIO that this change to the part 541 regulations may result in employees with similar job duties being classified differently depending on the criteria for the bonuses. However, such discrepancies are unavoidable with a salary requirement and already exist, for example, when regional differences in pay structure result in two employees performing the same job in different locations having different exemption status.

The Department also requested comments on whether payment on a monthly basis is an appropriate interval for nondiscretionary bonuses to be credited toward the weekly salary requirement. Numerous commenters stated that a policy requiring payment no less frequently than on a monthly basis would fail to reflect current bonus payment practices and would make it difficult for employers to utilize the new regulation. The Department believes it is appropriate to increase the permissible bonus payment interval, and is persuaded by comments from PPWO and others suggesting that quarterly (as opposed to monthly) payments of nondiscretionary bonus and commission income give employers sufficient opportunity to measure, quantify, and calculate payments tied to productivity or profits. This lengthened interval should also limit the compliance costs that some commenters suggested employers would incur from having to review payroll on a monthly (or more frequent) basis to determine which employees satisfied the salary level test. Accordingly, § 541.602(a)(3) establishes that in order for nondiscretionary bonuses and incentive payments (including commissions) to satisfy a portion of the standard salary level test for the executive, administrative, and professional exemptions, such compensation must be paid at least quarterly.

In response to commenter concerns, the Department has also determined that it is appropriate to permit a "catch-up" payment at the end of each quarter. This will help decrease the

administrative burden on employers and ensure that exempt employees receive the compensation to which they are entitled. The Department declines to permit employers to make a yearly catch-up payment like under the test for highly compensated employees, as this would significantly undermine the integrity of the salary basis requirement, which ensures that exempt workers receive the standard salary level on a consistent basis so that it serves as the hallmark of their exempt status. This concern is not implicated in the HCE context because such employees must receive the entire standard salary amount each pay period on a salary or fee basis and the annual catch-up payment applies only to that part of total annual compensation in excess of the standard salary amount.

The Final Rule permits employers to meet the standard salary level requirement for executive, administrative, and professional exempt employees by making a catch-up payment within one pay period of the end of the quarter. In plain terms, each pay period an employer must pay the exempt executive, administrative, or professional employee on a salary basis at least 90 percent of the standard salary level required in §§ 541.100(a)(1), 541.200(a)(1), or 541.300(a)(1), and, if at the end of the quarter the sum of the salary paid plus the nondiscretionary bonuses and incentive payments (including commissions) paid does not equal the standard salary level for 13 weeks, the employer has one pay period to make up for the shortfall (up to 10 percent of the standard salary level). Any such catch-up payment will count only toward the prior quarter's salary amount and not toward the salary amount in the quarter in which it was paid. For example, assume Employee A is an exempt professional employee who is paid on a weekly basis, and that the standard salary level test is $913 per week. In January, February, and March, Employee A must receive $821.70 per week in salary (90 percent of $913), and the remaining $91.30 in nondiscretionary bonuses and incentive payments (including commissions) must be

paid at least quarterly. If at the end of the quarter the employee has not received the equivalent of $91.30 per week in such bonuses, the employer has one additional pay period to pay the employee a lump sum (no greater than 10 percent of the salary level) to raise the employee's earnings for the quarter equal to the standard salary level.[67] The Department recognizes that some businesses pay significantly larger bonuses; where larger bonuses are paid, however, the amount attributable toward the EAP standard salary level is capped at 10 percent of the required salary amount.

The Department reemphasizes 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 few commenters addressed this precise issue, the Clearing House Association urged the Department to permit all types of bonuses and incentive payments to satisfy the entire HCE total compensation requirement, including the standard salary amount due each pay period. 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 payment forms toward the standard salary requirement. We conclude that permitting employers to use nondiscretionary bonuses and incentive payments to satisfy the standard salary amount is not appropriate because employers are already permitted to fulfill almost two-thirds 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

[67] If the employer chooses not to make the catch-up payment, the employee would be entitled to overtime pay for any overtime hours worked during the quarter.

HCE analysis employers must remain mindful that employees 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, as noted in the NPRM, overtime-eligible (i.e., nonexempt) employees may also receive bonuses and incentive payments. Where nondiscretionary bonuses or incentive payments are made to overtime-eligible 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 highly compensated exemption for certain EAP employees. Section 541.601(a) provides that such employees are exempt if they earn at least $100,000 in total annual compensation and customarily and regularly perform any one or more of the exempt duties or responsibilities of an executive, administrative, or professional employee. Section 541.601(b)(1) states that employees must receive at least $455 per week on a salary or fee basis, while the remainder of the total annual compensation may include commissions, nondiscretionary bonuses, and other nondiscretionary compensation. The regulation also clarifies that total annual compensation does not include board, lodging, and other facilities, and does not include payments for medical insurance, life insurance, retirement plans, or other fringe benefits. Pursuant to § 541.601(b)(2), an employer is permitted to make a final "catch-up" payment during the final 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. If an employee does

not work for a full year, § 541.601(b)(3) permits an employer to pay a pro rata portion of the required annual compensation, based upon the number of weeks of employment (and one final payment may be made, as under paragraph (b)(2), within one month after the end of employment).

The Department stated in the NPRM that we continue to believe that an HCE test for exemption is an appropriate means of testing whether highly compensated employees qualify as bona fide executive, administrative, or professional employees, but we proposed to increase the total annual compensation requirement and update it automatically on an annual basis. In the 2004 Final Rule, the Department concluded that the requirement for $100,000 in total annual compensation struck the right balance by matching a much higher compensation level than was required for the standard salary level test with a duties test that was significantly less stringent than the standard duties test, thereby creating a test that allowed only appropriate workers to qualify for exemption. See 69 FR 22174. This total annual compensation requirement was set more than four times higher than the standard salary requirement of $455 per week, which totals $23,660 per year. See id. at 22175. Such a balancing of a substantially higher compensation requirement with a minimal duties test still is appropriate, so long as the required annual compensation threshold is sufficiently high to ensure that it continues to cover only employees who "have almost invariably been found to meet all the other requirements of the regulations for exemption." Id. at 22174.

In the NPRM, the Department proposed to update § 541.601 by increasing the total annual compensation required for the highly compensated test in order to ensure that it remains a meaningful and appropriate standard when matched with the minimal duties test. The Department noted that over the past decade, the percentage of salaried employees who earn at

least $100,000 annually has increased substantially to approximately 17 percent of full-time salaried workers, more than twice the share who earned that amount in 2004; therefore, we proposed to increase the total annual compensation requirement to the annualized weekly earnings of the 90th percentile of full-time salaried workers nationally ($122,148 in 2013) to bring the annual compensation requirement more in line with the level established in 2004. Consistent with the 2004 regulations, the Department also proposed that at least the standard salary requirement must be paid on a salary or fee basis. The Department did not propose any changes to the HCE duties test.

Commenters provided both support for, and opposition to, the Department's proposal to increase the total annual compensation requirement for the HCE exemption, with some commenters preferring a higher compensation level and others preferring a lower level. Additionally, some commenters suggested that the HCE exemption should be eliminated entirely, while others suggested that the HCE duties test should be modified or eliminated. Both commenters representing employers and those representing employees generally provided much less comment on, and analysis of, the HCE proposal than they did regarding the other issues raised in the NPRM, however, with many commenters mentioning the HCE proposal only in passing or not at all.

Among those who supported the proposal as written, the American Federation of Government Employees (AFGE) indicated that the "new salary threshold for the HCE exemption provides a more accurate representation of which employees might be classified as exempt from the FLSA based on their salary," and stated that the 90th percentile of annual earnings of full-time salaried workers "provides an objective basis for determining which employees are truly 'highly-compensated' and likely to meet the qualifications of exemption from the FLSA." The Printing

Industries of America also supported the proposal, stating that "we believe this is an appropriate level for this particular test." The Partnership indicated that increasing the HCE compensation threshold to the 90th percentile accounts for the fact that its 2004 value has eroded over time and "is appropriate to ensure that only the most highly paid employees are categorically excluded from overtime requirements, as was the rule's intent when it was adopted in 2004."

Some commenters stated that the proposed HCE total annual compensation requirement should be increased so that the percentage of employees falling within the new compensation level matched the percentage covered in 2004. For example, NELA and Rudy, Exelrod, Zieff, & Lowe indicated that "[i]n 2004, 6.3 percent of full-time salaried workers earned a salary higher than the HCE compensation level of $100,000 . . . [so in] order to maintain the . . . 93.7 percentile figure, the Department would need to increase the HCE compensation level to $150,000 per year."[68] These commenters asserted that such a level "is the proper approach if the exemption truly is going to exclude only those at the very top of the ladder," and indicated that a substantial increase from the current HCE compensation level is warranted to "reflect the purpose of this test." The commenters also cited to the 2004 Final Rule in which the Department stated that "virtually every salaried 'white collar' employee with a total annual compensation of $100,000 per year would satisfy any duties test." 69 FR 22174. Nichols Kaster similarly stated that the 90th percentile of salaried earnings is "too low to offset the minimal duties test of the HCE exemption." Nichols Kaster favored eliminating the HCE exemption entirely and stated

[68] In the 2004 Final Rule, the Department set the total annual compensation amount at a level approximating the highest 10 percent of likely exempt employees. In the NPRM, we noted that the HCE total annual compensation level covered approximately the highest 6.3 percent of all full-time salaried employees at the time it was set. 80 FR 38562; see 69 FR 22169 (Table 3). In commenting on the current proposal, some commenters addressed the proposal in terms of likely exempt employees (10 percent) while other commenters addressed the proposal in terms of all salaried employees (6.3 percent).

that the "statutory text of the FLSA does not contain an exemption for highly compensated employees (HCEs)." This commenter also stated that there "is no causal connection between high compensation and exempt job duties," and thus expressed the view that "[s]uch a test does not accurately define or delimit bona fide exempt employees." However, Nichols Kaster stated that if the Department retains the HCE exemption, the compensation level should be increased to the 95th percentile, should not include "catch-up" pay, and should be based only on salary payments.

Other commenters opposed the Department's proposed increase to the HCE exemption's total annual compensation requirement. Tracstaffing opined that there "is no compelling reason to increase the minimum salary level for highly compensated salaried employees." H-E-B similarly stated that "[t]here is no public policy justification for paying overtime to an individual receiving a six figure annual income." SIFMA advocated "maintaining the $100,000 threshold for the highly compensated test, as the 'bright line' $100,000 mark furthers the goal of simplifying the analysis of who qualifies for the test." The Chamber, the National Lumber and Building Material Dealers Association, NSBA, PPWO, Seize This Day Coaching, and several other commenters all similarly commented that the compensation level should remain the same for the HCE exemption test. The Clearing House Association and SIFMA commented that the HCE exemption should not have an associated duties test.

The Department has considered the comments regarding the HCE test for exemption and revises § 541.601 to set the total annual compensation required for the highly compensated exemption at the annualized weekly earnings of the 90th percentile of full-time salaried workers nationally as proposed ($134,004 based on the fourth quarter of 2015). The Department disagrees with comments asserting that the HCE exemption compensation level should not be

increased. The highly compensated earnings level should be set high enough to avoid the unintended exemption of employees who clearly are outside the scope of the exemptions and are entitled to the FLSA's minimum wage and overtime pay protections.[69] See 69 FR 22174.

The Department notes that it has been 12 years since the HCE annual compensation level was set and, as with the standard salary level, the 2004 value has eroded over time. In FY2017, approximately 20 percent of full-time salaried workers are projected to earn at least $100,000 annually, about three times the share who earned that amount in 2004. See section VI.C.iv. In order to ensure that the HCE compensation level remains a meaningful and appropriate standard when matched with the minimal duties test, the Department is increasing the HCE compensation level to the annualized weekly earnings of the 90th percentile of full-time salaried workers nationally. This level, which is generally consistent with the level established in the 2004 Final Rule, is an appropriate proxy for identifying those white collar workers who may qualify as bona fide EAP workers without sweeping in overtime-eligible workers in high-wage regions. In response to the comments from employee representatives suggesting the new HCE compensation level should be even higher, the Department does not agree that a compensation level higher than the 90th percentile is necessary to ensure that virtually every salaried white collar employee would satisfy any duties test. The Department notes that the value of tying the HCE compensation level to wage data is that it will keep the HCE compensation level in tandem with increases in actual wages and therefore not grow either too slowly or too quickly. Therefore, the

[69] As the Department has previously noted this includes employees such as secretaries in high-wage markets. Courts have also found that real estate appraisers and chief inspectors also do not qualify for the HCE exemption. See Boyd v. Bank of America Corp., 109 F.Supp.3d 1273 (C.D. Ca. 2015) (real estate appraisers); Zubair v. EnTech Engineering P.C., 808 F.Supp.2d 592 (S.D.N.Y. 2011) (chief inspector who tested "concrete and paint sample and recommended project improvement to the overall paint systems").

Final Rule increases the total annual compensation requirement to the annualized weekly earnings of the 90th percentile of full-time salaried workers nationally, which based on fourth quarter of 2015 data is $134,004.[70]

Additionally, the Department proposed to maintain the requirement that at least the standard salary amount must be paid on a salary or fee basis. Under the current rule, employees for whom the HCE exemption is claimed must receive the full standard salary amount of $455 weekly on a salary or fee basis. See § 541.601(b). The Department proposed to maintain this requirement, updating the amount that must be paid on a salary or fee basis to the 40th percentile of weekly earnings of full-time salaried employees nationally. The Final Rule maintains this requirement, but modifies the amount of the standard salary to the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region. The Department further stated that should it adopt a provision in the Final Rule permitting employers to take a credit against the payment of the standard salary level for nondiscretionary bonuses, that credit would not be applicable to the HCE exemption. 80 FR 38537 n.36. As previously discussed in section IV.C., the Department received almost no comments addressing the exclusion of bonus payments from satisfaction of the salary requirement for HCE employees. The Final Rule maintains the requirement that employees for whom the HCE exemption is claimed must receive the standard weekly salary amount on a salary or fee basis and does not permit employers to credit nondiscretionary bonuses for up to 10 percent of that salary payment as is permitted under this Final Rule under the standard salary test. Employers can already credit such payments toward the portion of the HCE total compensation requirement in excess of the standard salary level; the

[70] See www.bls.gov/cps/research_series_earnings_nonhourly_workers.htm.

Department does not believe that allowing such payments to also satisfy a portion of the standard salary level for HCE employees would be appropriate.

A few commenters requested a regional adjustment for the HCE salary level. The Chamber stated that the "Department should set the highly compensated test using actual salary levels of exempt employees working in the South and in the retail sector that would meet the highly compensated exemption requirements." The Department notes that no regional adjustment has been made to the HCE compensation level in this Final Rule, just as this was not part of the 2004 Final Rule's determination of the compensation level required for the HCE exemption. The HCE exemption must use a national wage rate to effectively ensure that workers such as secretaries in high-wage areas, such as New York City and Los Angeles, are not inappropriately exempted based upon the HCE exemption's minimal duties test.

The Department proposed in the NPRM to annually update the HCE total annual compensation requirement. As explained in greater detail in the automatic updating section, the Department will automatically update the HCE compensation level every three years, beginning on January 1, 2020.

The Department did not propose any changes to the HCE duties test created in 2004 and makes no change to the HCE duties test in this Final Rule. With respect to the call by some commenters to eliminate the duties test for the HCE exemption, the Department notes that we have consistently declined to adopt a salary-only test, because our statutory authority is to define and delimit who is employed in a bona fide executive, administrative or professional capacity, and salary alone is not an adequate definition. In the 2004 Final Rule, the Department expressed our agreement with commenters "that the Secretary does not have authority under the FLSA to adopt a 'salary only' test for exemption, and reject[ed] suggestions from employer groups to do

so," and further noted that "[t]he Department has always maintained that the phrase 'bona fide executive, administrative, or professional capacity' in the statute requires the performance of specific duties." See 69 FR 22173. The Department continues to require, as we did in the 2004 Final Rule, that an employee have a primary duty that includes performing office or non-manual work to qualify for the HCE exemption, and workers such as "carpenters, electricians, mechanics, plumbers, iron workers, craftsmen, operating engineers, longshoremen, construction workers, laborers, and other employees who perform work involving repetitive operations with their hands, physical skill and energy are not exempt under this section no matter how highly paid they might be." § 541.601(d).

With respect to Nichols Kaster's comment asserting that the HCE exemption lacks a meaningful duties test, the Department notes that pursuant to § 541.601(a), HCE employees must customarily and regularly perform any one or more of the exempt duties or responsibilities of an executive, administrative, or professional employee as identified in the regulations. As noted in the 2004 Final Rule, the "Department continues to find that employees at higher salary levels are more likely to satisfy the requirements for exemption as an executive, administrative, or professional employee." 69 FR 22174. Therefore, "the purpose of section 541.601 was to provide a short-cut test for such highly compensated employees who have almost invariably been found to meet all the other requirements of the regulations for exemption." Id. (internal quotation marks omitted). As we noted in the 2004 Final Rule, the "Department has the authority to adopt a more streamlined duties test for employees paid at a higher salary level." 69 FR 22173. We continue to believe that the existing HCE duties test is appropriate for those earning at the 90th percentile of full-time salaried workers, especially in light of the fact that the

required compensation level will be routinely updated and, therefore, will remain a meaningful test.

E. Automatic Updates

As the Department noted in the NPRM, even a well-calibrated salary level that is fixed becomes obsolete as wages for nonexempt workers increase over time. Lapses between rulemakings have resulted in EAP salary levels that are based on outdated salary data, and thus are ill-equipped to help employers assess which employees are unlikely to meet the duties tests for the exemptions. To ensure that the salary level set in this rulemaking remains effective, the Department proposed to modernize the regulations by establishing a mechanism for automatically updating the standard salary test, as well as the total annual compensation requirement for highly compensated employees. The Department explained that the addition of automatic updating would ensure that the salary test level is based on the best available data (and thus remains a meaningful, bright-line test), produce more predictable and incremental changes in the salary required for the EAP exemptions, and therefore provide certainty to employers, and promote government efficiency.

The Department sought comments on two alternative automatic updating methodologies. One method would update the threshold based on a fixed percentile of earnings of full-time salaried workers. The other method would update the threshold based on changes in the Consumer Price Index for All Urban Consumers (CPI-U). The Department also proposed to automatically update the total annual compensation requirement for the HCE exemption with the same method chosen to update the standard salary test. Regardless of the method selected, the Department proposed that automatic updating for both thresholds would occur annually, but invited comment regarding whether a different updating frequency would be more appropriate. Finally, the

Department proposed to publish the updated rates at least 60 days before they take effect, and invited comment regarding whether the updated rates should take effect based on the effective date of the Final Rule, on January 1, or on some other specified date. The Department received many comments in response to these proposals.

The Final Rule establishes that the Department will automatically update the standard salary level test by maintaining the salary level at the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region. The Department will update the annual compensation requirement for highly compensated employees by maintaining this level at the annualized value of the 90th percentile of the weekly earnings of full-time salaried workers nationwide. In response to commenter concerns, the Department has modified the frequency and advance-notice elements of the updating mechanisms. The Final Rule establishes that automatic updates to the standard salary level and the HCE annual compensation requirements will occur every three years on the first of the year, and that the Department will publish the updated rates in the Federal Register at least 150 days before their effective date, and post the updated salary and compensation levels on the WHD website. The first automatic update will take effect on January 1, 2020. The automatic updating provision is set forth in new § 541.607.

i. The Department's Legal Authority to Automatically Update the Salary Level

Most commenters that addressed automatic updating focused on the merits of the Department's proposal, but some discussed our authority to automatically update the salary level.[71] Commenters that opposed automatic updating discussed this issue more frequently and in much greater detail than those that favored the Department's proposal.

[71] Some commenters, like the Equal Employment Advisory Council (EEAC), addressed the Department's authority to automatically update the HCE compensation requirement by noting that its reservations regarding automatic updating of the standard salary level apply equally to the

Organizations representing employee interests, including AFL-CIO and NWLC, asserted that the Department has authority to establish an automatic updating mechanism through notice and comment rulemaking. These commenters stated that just as the Department has authority under 29 U.S.C. 213(a)(1) to establish the salary level test, we likewise have authority to automatically update the salary level to ensure it remains effective. Several commenters emphasized that Congress has never limited the Department's ability to update the salary level. For example, EPI stated that "Congress in 1938 gave the authority to define and delimit the terms 'bona fide executive, administrative, or professional' to the Secretary of Labor and has never taken it back, except with respect to very particular occupations," and a comment from 57 labor law professors similarly stated that automatic updating is "within [the Department's] discretion and authority" because "Congress granted the agency wide discretion in implementation of the statutory language." Other commenters, including AFSCME and NELP, highlighted that automatic updating is consistent with the FLSA's purpose.

In contrast, a number of organizations representing employer interests challenged the Department's authority to add an updating mechanism. Many of these commenters, including ABC, ALFA, CUPA-HR, NRA, PPWO, and Seyfarth Shaw, stated that Congress has never granted the Department authority to institute automatic updating, and asserted that section 13(a)(1)'s silence on this issue reflects that Congress did not intend the salary level test to be automatically updated. These and other commenters stressed that whereas Congress has never amended section 13(a)(1) to expressly include automatic updating, Congress has expressly

---

Department's proposal to automatically update the HCE exemption's threshold. We do not separately address this issue since, like the standard salary level, our authority to automatically update the HCE threshold is grounded in section 13(a)(1), and the discussion in this section therefore applies equally to our adoption of a mechanism to automatically update the HCE total compensation requirement.

authorized indexing under other statutes. Many commenters, including the Chamber, CUPA-HR, and FMI, highlighted that Congress has never provided for automatic increases to the FLSA minimum wage, and the Chamber added that Congress has not indexed the minimum hourly wage for exempt computer employees under section 13(a)(17) of the FLSA, the cash wage for tipped employees under section 3(m) of the FLSA, or any of the FLSA's subminimum wages.

These comments reveal disagreement about the scope of the Department's delegated authority under section 13(a)(1) to define and delimit the EAP exemptions. The Department disagrees with the position that section 13(a)(1)'s silence on automatic updating forecloses the Department from establishing an updating mechanism. While it is true that section 13(a)(1) does not reference automatic updating, it also does not reference a salary level or salary basis test, a duties test, or other longstanding regulatory requirements. Rather than set precise criteria for defining the EAP exemptions, Congress delegated that task to the Secretary by expressly giving the Department the broad authority to define and delimit who is a bona fide executive, administrative, or professional employee. As we explained in the NPRM, since 1938 the Department has used this authority to promulgate many significant regulatory changes to the EAP exemptions, including adding a separate salary level for professional employees and a separate duties test for administrative employees in 1940, adopting separate short and long test salary levels in 1949, and eliminating the long duties test and creating a single standard salary level test and a new HCE exemption in 2004. These changes were all made without specific Congressional authorization. Despite numerous amendments to the FLSA over the past 78 years, Congress has not altered the Department's authority to promulgate, update, and enforce the salary test regulations. The Department concludes that just as we have authority under section 13(a)(1) to establish the salary level test, we likewise have authority to adopt a methodology

through notice and comment rulemaking for automatically updating the salary level to ensure that the test remains effective. This interpretation is consistent with the well-settled principle that agencies have authority to "'fill any gap left, implicitly or explicitly, by Congress.'" Long Island Care at Home, Ltd. v. Coke, 551 U.S. 158, 165 (2007) (quoting Chevron, U.S.A., Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837, 843 (1984)).

That other statutes expressly provide for indexing does not alter our interpretation of the FLSA. The Department's authority to set and update the salary level test is based in the language of the FLSA, and the fact that there are indexing provisions in other statutes does not limit that authority. Moreover, three of the four non-indexed FLSA wage rates that the Chamber and other commenters referenced—the section 6(a)(1) minimum wage, the minimum hourly wage for exempt computer employees under section 13(a)(17), and the cash wage for tipped employees under section 3(m)—are set by statute.[72] In contrast, the salary level is purely a creature of regulation. Whether Congress has indexed statutorily-established rates within the FLSA does not inform, let alone undermine, the Department's authority to use notice and comment rulemaking to create a mechanism for keeping the regulatory salary level up to date.

The Department also received several comments stating that automatic updating violates section 13(a)(1)'s mandate that the Secretary define and delimit the EAP exemption from "time to time." For example, the Chamber commented that this statutory language gives "no indication that Congress wanted to put these regulations on auto-pilot," but instead supports that "Congress wants the Department to 'continually revisit' the Part 541 regulations" (emphasis in comment) (quoting 80 FR 38537). However, promulgating an automatic updating mechanism does not

[72] The Chamber also referenced the FLSA's subminimum wage rates. While the Secretary sets some subminimum wage rates, the FLSA establishes the existence of such rates. See, e.g., 29 U.S.C. 214(a) (minimum wage for learners, apprentices, and messengers).

conflict with section 13(a)(1)'s "time to time" language. The salary level percentile adopted in this rulemaking reflects the Department's analysis of the appropriate line of demarcation between exempt and nonexempt workers; providing that this dividing line will continue to remain up to date over time fulfills the Department's obligation to ensure that only "bona fide" EAP workers qualify for exemption. Moreover, maintaining the salary level at the 40th percentile of salaries in the lowest-wage Census Region by updating it every three years in no way precludes the Department from revisiting this methodology from "time to time" should cumulative changes in job duties, compensation practices, and other relevant working conditions indicate that changes to the salary level calculation method may be warranted.

The Department also received several comments asserting that automatic updating violates the APA and section 13(a)(1)'s requirement that the EAP exemption be defined and delimited by regulations of the Secretary subject to the provisions of the APA. These commenters asserted, albeit on slightly different grounds, that notice and comment rulemaking must precede any salary level change. CUPA-HR emphasized that under section 13(a)(1) any updating must be done by regulation, and EEAC asserted that "the FLSA exemptions have the full force and effect of law" and the "APA requires notice-and-comment rulemaking each time an agency issues, repeals, or amends a legislative rule." NRF stated that any increase should be "based on an individualized evaluation of economic conditions rather than an automatic arbitrary formula," and several commenters stressed that the Department must consider prevailing conditions and provide for public comment before updating the salary level. See, e.g., Jackson Lewis; NAM; PPWO.

The Department believes that automatically updating the salary level fully complies with the APA and section 13(a)(1). Through this rulemaking the Department is promulgating an automatic updating mechanism by regulation and in accordance with the APA's notice and

comment requirements. The updating mechanism is not an "arbitrary formula," but the product of an exhaustive rulemaking process that took into consideration the views of thousands of commenters. These comments raised a wide range of relevant issues, including the impact of an updating mechanism, and greatly influenced the content of the Final Rule. For example, in response to these comments (and as discussed in detail below) the Department adopted a fixed percentile approach to automatic updating, changed the updating frequency from annually to every three years, increased the period between announcing the updated salary level and the effective date of the update from 60 days to at least 150 days, and set January 1 as the effective date for future salary level updates. As to commenter concerns about accounting for prevailing economic conditions, both the NPRM and this Final Rule contain detailed 10-year projections of the costs and transfers associated with automatic updating. See section VI.D.x.; 80 FR 38586-89. Moreover, maintaining the salary level at a fixed percentile of earnings will help ensure the test continues to reflect prevailing wage conditions, and does not preclude the Department from revising the updating mechanism in the future through notice and comment rulemaking if we determine that conditions warrant. We disagree with commenter statements that notice and comment rulemaking must precede every salary level update when the underlying salary setting methodology is unchanged and reject the notion that in directing the Department to define and delimit the EAP exemption by regulations, Congress intended to prohibit the Department from establishing an automatic updating mechanism through notice and comment rulemaking.

Relatedly, a few commenters interpreted our NPRM statement that automatic updating would remove "the need to continually revisit this issue through resource-intensive notice and comment rulemaking," 80 FR 38537, as an attempt to impermissibly circumvent the APA. See, e.g., Chamber; NRA. This statement was not an attempt to sidestep the APA, but rather part of our

explanation for seeking comment on the merit of using an updating mechanism to keep the salary level test current. The Department has dedicated considerable resources toward this rulemaking, including conducting extensive outreach prior to issuing the NPRM, drafting a comprehensive NPRM, receiving and reviewing more than 270,000 timely comments, and drafting a Final Rule addressing these comments. The Department recognizes and appreciates the commenters' views. We disagree, however, that section 13(a)(1) or the APA prohibits us from establishing a mechanism to keep the salary level up to date so that it continues to work effectively with the duties test. Instead, we conclude that introducing an updating mechanism that ensures that the EAP exemptions remain up to date is a reasonable exercise of the Department's statutorily-established authority to define and delimit the EAP exemptions.[73]

The Department also received several comments highlighting that in two prior rulemakings we rejected commenter requests to automatically update the salary level. Specifically, some commenters raised that in our 1970 rulemaking we stated, in response to a comment, that automatic updating would "require further study," 35 FR 884, and that we declined a similar request in 2004. See, e.g., Chamber; FMI. The Department acknowledged these prior statements in the NPRM. While we agree with commenters that our decision to institute automatic updating in this Final Rule departs from our 1970 and 2004 rulemakings, these past statements in no way foreclose our current action. The 1970 rulemaking stated that the request to automatically update the salary level "appears to have some merit, particularly since past practice has indicated that approximately 7 years elapse between amendment of the salary level

[73] This approach is consistent with the Department's approach taken when issuing regulations to establish required wage rates in other programs for which we have enforcement responsibility. See 20 CFR 655.120 (describing method for updating adverse effect wage rates for H-2A visa program); 20 CFR 655.211 (using Employment Cost Index to update required wage for employees engaged in herding or the production of livestock under the H-2A program).

requirements." 35 FR 884. The time between rulemakings has increased since 1970 (this will be the third salary level update in 46 years), underscoring the merit of automatic updating. Consistent with our earlier statement that automatic updating "would require further study," the Department has proposed the addition of an updating mechanism in this rulemaking and considered the wide-range of comments received on the issue. While in the 2004 Final Rule we declined to institute automatic updating and instead expressed our intent "in the future to update the salary levels on a more regular basis, as [we] did prior to 1975," 69 FR 22171, our subsequent experience has prompted us to reexamine this matter.

Several commenters, including IFA and Littler Mendelson, specifically referenced our refusal to institute inflation-based indexing in the 2004 Final Rule. In that rulemaking we stated, in response to a comment, that "the Department has repeatedly rejected requests to mechanically rely on inflationary measures when setting the salary levels in the past because of concerns regarding the impact on lower-wage geographic regions and industries." 69 FR 22172. We then stated that such "reasoning applies equally when considering automatic increases to the salary levels" and that "the Department believes that adopting such approaches in this rulemaking is both contrary to congressional intent and inappropriate." Id. In its comment, the Chamber interpreted this language as expressing our conclusion "that Congress did not give the Department authority to provide automatic increases to the salary level" and stated that "the Chamber is unaware of any legislative or legal development that would justify [our purported] reversal."

These commenters' reading of the 2004 Final Rule is overly broad, as we did not conclude that the Department lacks legal authority to institute automatic updating. Our reference to automatic updating simply reflected our conclusion at that time that an inflation-based updating

mechanism, such as one based on changes in the prices of consumer goods, that unduly impacts low-wage regions and industries would be inappropriate. As explained in the NPRM, closer examination reveals that concerns raised when setting a new salary level using an inflation index are far less problematic in the automatic updating context. See 80 FR 38540. For example, in the automatic updating context there is little risk of using an outdated salary level as a baseline for inflation-based adjustments, and the inability of inflation-based indicators to account for changes in working conditions is therefore less concerning. See id. Regardless, our prior concerns about inflation-based updating are not implicated here because the Department has chosen to automatically update the salary level based on a fixed percentile of earnings of full-time salaried workers. As explained in detail in section IV.A., in response to commenter concerns that setting the salary level using the 40th percentile of a nationwide data set would adversely impact low-wage regions and industries, the Department is setting the salary level at the 40th percentile of full-time salaried workers in the lowest-wage Census Region, which yields a lower salary level that will exclude fewer employees performing EAP duties in low-wage regions and industries. Tying the salary level and updating mechanism to a fixed percentile of earnings in the lowest-wage Census Region squarely addresses the concern we raised in the 2004 Final Rule, and ensures that our updating mechanism is appropriate for all areas and industries.

Several commenters, including CUPA-HR and FMI, also deemed the Department's proposal inconsistent with our statement in the 2004 Final Rule that "the Department finds nothing in the legislative or regulatory history that would support indexing or automatic increases." 69 FR 22171. But as explained in our proposal, the lack of on-point legislative history—either favoring or disfavoring automatic updating—is unsurprising given the origin and evolution of the salary level test. Congress did not set forth any criteria, such as a salary level test, for defining the EAP

exemptions, but instead delegated that task to the Secretary. The Department established the first salary level tests by regulation in 1938, using our delegated authority to define and delimit the EAP exemptions. See 29 U.S.C. 213(a)(1). The fact that the salary level tests were created by regulation after the FLSA was enacted accounts for the lack of legislative history addressing the salary level tests or updating methods. As previously discussed, despite numerous amendments to the FLSA over the past 78 years, and the Department making many significant changes to the EAP exemptions, Congress has not altered the Department's authority to promulgate, update, and enforce the salary test regulations. We agree with commenters that instituting an automatic updating mechanism departs from the Department's past practice, but believe this is an appropriate modernization and within the Department's authority.

The Department also received several comments addressing the impact of automatic updating on compliance with the Regulatory Flexibility Act ("RFA") and Executive Order 13563, Improving Regulation and Regulatory Review. Seyfarth Shaw urged the Department to not proceed with automatic updating in part because this mechanism would "effectively bypass[]" these authorities. PPWO raised similar RFA concerns and characterized the Department's rulemaking as a "'super-proposal,' deciding once and for all what (in the Department's belief) is best without consideration of its impact now or in the future." PPWO further stated that "it would not be possible for the Department to accurately estimate the impact of the automatic increases in future years as the workforce and the economy are always changing."

The RFA requires a regulatory flexibility analysis to accompany any agency rule promulgated under 5 U.S.C. 553. See 5 U.S.C. 603-604. In accordance with this requirement, this rulemaking estimates the future costs of automatic updating using the fixed percentile approach. The RFA only requires that such analyses accompany rulemaking, and commenters have not

cited any RFA provision that would require the Department to conduct a new regulatory flexibility analysis before each automatic salary level update. In response to PPWO's concern about this rulemaking setting the salary level updating process "once and for all," we reiterate that this Final Rule does not preclude further rulemaking should the Department determine that future conditions indicate that revisions to the salary level updating methodology may be warranted.

Similarly, Executive Order 13563 directs agencies to take certain steps when promulgating regulations, including using the "best available techniques to quantify anticipated present and future benefits and costs as accurately as possible" and adopting regulations "through a process that involves public participation." 76 FR 3821 (Jan. 18, 2011). The current rulemaking fully satisfies all aspects of Executive Order 13563, see section VI; 80 FR 38545, and commenters have cited no portion of this directive that would require notice and comment rulemaking to precede future automatic salary level increases made through the updating mechanism established in this rulemaking.

Finally, Fisher & Phillips and the Southeastern Alliance of Child Care Associations stated that because the Department did not propose specific regulatory text concerning automatic updating, "adoption of any such indexing mechanism would be unlawful and without effect" under the APA. These commenters did not specify the provision of the APA that is purportedly violated. The APA requires that the notice of proposed rulemaking published in the Federal Register include either the terms or substance of the proposed rule or a description of the subjects and issues involved. See 5 U.S.C. 553(b)(3). The Department's proposal fully satisfies this standard, which does not require the NPRM to "contain every precise proposal which (the agency) may ultimately adopt as a rule," much less the specific regulatory text. Ethyl Corp. v. EPA, 541 F.2d

1, 48 (D.C. Cir. 1976) (en banc) (internal quotation marks and citations omitted). The proposed regulatory text for each exemption states that the salary level will be updated annually (on a to-be-determined date) and that the Department will publish a notice with the updated levels at least sixty days before these rates become effective. See 80 FR 38610-11. The proposal also explains why, rather than propose regulatory text for a specific updating method, the Department sought comments on two alternatives (each of which we discussed in depth). See 80 FR 38539. The Department's NPRM fully satisfies the APA.

ii. Rationale for Automatically Updating Salary Levels

The Department proposed to establish automatic updating mechanisms to ensure that the standard salary test and the HCE total annual compensation requirement remain meaningful tests for distinguishing between bona fide EAP workers who are not entitled to overtime and overtime-protected white collar workers, and continue to work effectively with the duties tests. The Department's proposal explained that this change would ensure that these thresholds are based on the best available data and reflect prevailing salary conditions, and will produce more predictable and incremental changes in the salary required for the EAP exemptions. The Department received numerous comments addressing our automatic updating proposal.

Commenters were sharply divided over whether the Department should automatically update the salary level.[74] Employees and commenters representing employee interests overwhelmingly supported this change, while most employers and commenters representing employer interests opposed automatic updating. Overall, those supporting automatic updating generally agreed

[74] Relatively few commenters specifically addressed the proposal to automatically update the HCE total annual compensation level, and those that did generally stated that their views mirrored their comments on the proposal to automatically update the standard salary level. Accordingly, this discussion focuses on the standard salary level but also applies to the Department's adoption of an automatic updating mechanism for the HCE compensation requirement.

with the Department's rationale presented in the NPRM and emphasized the benefits to employees and employers of maintaining an up-to-date salary level, while those in opposition challenged the Department's rationale and emphasized the burdens annual updating would impose on employers. Several employers favored automatic updating, but requested that updates occur less frequently than on an annual basis. Additionally, some commenters that opposed automatic updating nonetheless expressed a preference for a particular updating methodology should the Department go forward with this aspect of our proposal.

Commenters that supported automatic updating focused primarily on the benefits of maintaining an up-to-date salary level. Many commenters agreed with the Department's proposal, stating that automatic updating is a transparent way to maintain an effective salary level and avoid the negative effects of infrequent salary level updates. For example, NELP stated that automatic updating "is by far the most reasonable, efficient and predictable way to ensure that the standard for exemption remains true to the statute's intended purposes," AFL-CIO stated that a "transparent updating process would provide greater certainty and predictability for employers and workers alike," and Bend the Arc, Employment Justice Center, Maintenance Cooperation Trust Fund, and several other worker advocacy groups stated that indexing "the salary threshold to an objective measure provides a predictable and efficient way to ensure that those workers intended to be covered by the [FLSA] get its protections." Many other commenters made similar statements. See, e.g., AARP; AFT; EPI; the Gillespie Sanford law firm; Labor and Employment Committee of the National Lawyers Guild-New York City Chapter; NWLC.

Commenters supporting automatic updating also frequently discussed, and viewed the Department's proposal as a solution to, the Department's past inability to regularly update the

salary level. These commenters emphasized that automatic updating would increase predictability in both the frequency and size of salary level changes, benefiting employers and employees. See, e.g., Comment from 57 labor law professors; AFL-CIO; Partnership. Several commenters representing employer interests viewed automatic updating as a means of producing more predictable salary level changes. See, e.g., American Council of Engineering Companies; CVS Health. Similarly, SIGMA supported automatic updating because "[s]udden, large adjustments to the threshold without warning can cause dislocation in the industry, increase compliance costs, and provide disincentives to employing people on a salaried rather than an hourly basis." ANCOR stated that "steadier, more predictable" salary level changes would "likely benefit providers who will be able to adjust to smaller, more frequent changes better than to larger, less frequent ones."

Some commenters that supported automatic updating, including Athens for Everyone, NELA, Rudy, Exelrod, Zieff & Lowe, and many others, stressed that a fixed salary level harms employees because inflation causes the salary threshold's real value to decline over time. AFSCME submitted campaign comments from 24,122 of its members who agreed that "overtime protections have been eroded by inflation," and highlighted the "need to index these protections to keep them from being eroded again in the future." NELA and Rudy, Exelrod, Zieff & Lowe also stated that this decline particularly harms workers earning just below the fixed salary level when it is first set, because they will "soon see that figure fall below their salary" and lose overtime protection even if "the real value of their salary stays entirely constant." Likewise, Nichols Kaster stated that infrequent salary level updates have harmed workers earning just above the salary threshold when it is first set, as these workers have "no protection against working long hours for diminishing returns."

A number of commenters also raised the related view that automatic updating would decrease inappropriate classification of lower salaried white collar employees as exempt. AFGE, IAFF, and others noted that the salary level's effectiveness at distinguishing between exempt and nonexempt workers diminishes over time as the wages of employees increase and the real value of the salary threshold falls. SEIU and a number of worker advocacy groups, including Equal Justice Center, NDWA, and Texas RioGrande Legal Aid, asserted that infrequent salary level updates have permitted employers to sweep too many low-salaried workers into the exemption, with NELP citing the proximity of the current salary threshold to the poverty level as a "potent example" of how the "current method of setting fixed levels results in outdated thresholds and ballooning numbers of workers improperly subject to employer classification as exempt." Some commenters, including AFL-CIO and UFCW, asserted that failing to regularly update the standard salary level also exposes growing numbers of workers who fail the standard duties test to the "risk of misclassification."

The Department received numerous comments from employers and groups representing employers opposing the introduction of an automatic updating mechanism. These commenters raised a variety of concerns and urged the Department not to finalize this aspect of our proposal. Consistent with how many commenters organized their comments, these views are aptly separated into two broad categories: those addressing whether automatic updating is appropriate as a general matter, and those discussing potential financial and administrative effects of automatically updating the salary levels on an annual basis. Both of these broad categories of comments are discussed below.

Some commenters cited the Department's past refusal to institute automatic updating and emphasized that the part 541 regulations have benefited from the rulemaking process. For

example, the Chamber, FMI, and others stated that rulemaking has generated vigorous public debate about the salary levels, and that the Department has increased and decreased proposed salary levels in response to public comment—including in 2004 when the Department increased the proposed salary level and HCE compensation requirements in our final rule. PPWO stated that the "Department's own actions in reaching out to the regulated community before publication of the NPRM, as well as soliciting input on the salary level in the NPRM itself, demonstrate the importance of notice-and-comment on the salary level."

Many commenters stated that the Department should only update the salary level when conditions warrant, not automatically. CUPA-HR commented that the rates of increase and the duration between updates have always varied as the Department has tailored the salary levels "to ensure that the exemptions remained true to their purpose in the face of changing workforces and changing economic circumstances." NGA cited the statement in the 2004 Final Rule that "salary levels should be adjusted when wage survey data or other policy concerns support such a change," 69 FR 22171, and stated that the Department should only change the salary level when changes in earnings are substantial. Similarly, AH&LA, Island Hospitality Management, NCCR, and NRF all stated that a salary increase "should be based on an individualized evaluation of economic conditions rather than an automatic arbitrary formula." Other commenters expressed similar views. See, e.g., Agricultural Retailers Association and the Fertilizer Institute; National Council of Farmers Cooperatives. PPWO contended that the salary level needs to be "fixed" only "when it approaches the end of its usefulness." EEAC and Fisher & Phillips stated that the Department could simply reallocate resources as necessary to maintain an appropriate salary level without automatic updating.

Several commenters raised the related concern that automatic updating could harm the economy by increasing the financial burden on employers during economic downturns. The Chamber stated that either proposed updating method would be slow to reflect actual economic conditions, and would prevent employers from "lowering salaries to quickly respond to decreased revenue experienced in bad economic times." Fisher & Phillips stated that automatic updating during periods of high inflation could "contribute to a serious inflationary spiral." Analogizing to the minimum wage context, CalChamber Coalition stated that automatic updates during economic downturns may lead employers to reclassify more employees as nonexempt, reduce hours, and increase layoffs.

Some commenters worried that automatic updating would create an untenably high salary level that would harm low-income regions and industries, and small businesses. For example, Alpha Graphics stated that automatic updating would produce "an inappropriately high level in a matter of a few years," and NGA stated that salary level increases would harm independent grocers with low profit margins because the updating mechanism "would not provide the necessary protection for low-wage industries and geographic areas." See also, e.g., ALFA; NFIB. SHRM expressed concern that automatic updating based on a national salary level would not account for the fact that salaries in all regions and industries do not rise at the same pace, and it questioned whether the Department could realistically use additional rulemaking to correct for regional disparities that may arise in the future.

Several commenters asserted that updating is problematic regardless of the updating method the Department chooses, with some suggesting that the salary level and automatic updating are incompatible concepts. Seyfarth Shaw stated that any updating method "would establish an ad hoc, artificially-created level determined by statistical assumptions." See also Wendy's

(describing the updating methods as "based on untested and complicated methodologies"). EEAC expressed concern that if the salary-setting methodology in this rulemaking results in an incorrect salary level (as the Department now states was the case in 2004) automatic updating would compound this error indefinitely. NACS, the Southeastern Alliance of Child Care Associations, and others stated that establishing an automatic updating mechanism is inconsistent with the Department's recognition that "the line of demarcation" provided by the salary test "cannot be reduced to a standard formula."

As to the effect of automatic updating on salary level predictability, PPWO stated that "it will be difficult, if not impossible, for employers and employees to determine with precision each year's new salary level in advance of the Department's pronouncement in the Federal Register," and AIA-PCI and the Clearing House Association agreed that this uncertainty is demonstrated by the Department's statement in the NPRM that "the public will not be able to exactly replicate the weekly earnings and percentiles" used to calculate the salary level, 80 FR 38528 n.24.

The Department recognizes that our automatic updating proposal has elicited strong and diverse reactions from stakeholders. After review of submitted comments, the Department remains convinced that instituting an automatic updating mechanism is the best means of ensuring that the salary level test continues to provide an effective means of distinguishing between overtime-eligible white collar employees and those who may be bona fide EAP employees, and continues to work appropriately with the duties test.

The Department shares commenters' concerns that a fixed and outdated salary level increases the number of low-salaried employees at risk of being inappropriately classified as exempt as the real value of the salary threshold falls, and that workers earning near the fixed salary level when it is set are particularly vulnerable. The Department also agrees with commenters that the

updates to the salary level should reflect prevailing economic conditions. The Department's updating mechanism directly addresses both of these issues by ensuring that the salary test level is based on the best available data and reflects current salary conditions. As explained in more detail below, the Department will use the updating mechanism established under new § 541.607 to reset the salary level using the most recent BLS data on earnings for salaried workers. Linking the salary level to earnings ensures that economic changes that impact employee salaries are reflected in the salary level test. Also, because regular updates will ensure that the salary level is in step with prevailing economic conditions, the Department does not believe that the updating mechanism will lead to undue salary level increases during economic downturns or other inopportune times. Salary level changes will occur at regular intervals using a set methodology and a publicly available data source. This improvement to the current regulations will benefit employers and employees by replacing infrequent, and thus more drastic, salary level changes with gradual changes occurring at predictable intervals.

The Department is committed to ensuring that the updating mechanism yields a salary that is appropriate for low-wage industries and geographic areas. As previously discussed in section IV.A.iv., in response to commenters' concerns, the Department is setting the salary level at the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (currently the South). Commenters raised similar concerns about using a nationwide data set for automatic updating. The reasons that supported changing from a national to a regional data set in the standard salary level setting context apply equally in the salary updating context, and new § 541.607 accordingly incorporates this data set change.[75] The Department recognizes

[75] Similarly, for the same reasons that the Department declines commenter requests to institute a special salary level for non-profit employers, we also decline to exempt non-profit employers from automatically updated salary levels.

that salaries do not change at the same rate nationwide, and this modification will ensure that any future increase in earnings will only impact the standard salary level to the extent that those gains are also realized by employees in the lowest-wage Census Region. This change will also further guard against commenter concerns that using a nationwide data set could lead to a standard salary level increase that does not reflect the prevailing economic climate.[76]

Experience has shown that the salary level test is only a strong measure of exempt status if it is up to date, and that left unchanged the test becomes substantially less effective as wages for overtime-protected workers increase over time. As we explained in the NPRM, competing regulatory priorities, overall agency workload, and the time-intensive nature of notice and comment rulemaking have all contributed to the Department only having updated the salary level once since 1975 (in 2004). In the 2004 Final Rule the Department expressed the intent to "update the salary levels on a more regular basis," 69 FR 22171, yet more than a decade has passed since the last update. While some commenters viewed this inaction and the Department's past decision not to institute automatic updating as reason for withdrawing our current proposal, we believe this history underscores the appropriateness of adding an automatic updating provision to the regulations.

Contrary to several commenters' concerns, prior Department statements about the salary level test in no way undermine the Department's decision now to incorporate an automatic updating mechanism into the regulations. The Department's statement that the "line of demarcation" between exempt and nonexempt employees "cannot be reduced to a standard formula," 80 FR

[76] As explained in section IV.D., as in the 2004 Final Rule, the Department is using a nationwide data set to set the HCE compensation level in this rulemaking, and we will use nationwide data to update the HCE compensation level. The use of nationwide data is necessary to ensure that overtime-eligible workers in high-wage areas are not inappropriately exempted based upon the HCE exemption's minimal duties test.

38527, simply reflects our continued belief that no single formula can unerringly separate exempt and nonexempt employees, and that the salary test must therefore work in tandem with the duties test for the EAP exemption to function effectively. The salary level test remains the "best single test" of exempt status, Stein Report at 19, and the method for setting and updating the salary level adopted through this rulemaking represents the Department's best determination of the appropriate dividing line between exempt and nonexempt workers, when paired with the standard duties test. While the precise updating "formula" chosen—the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region—is new, the underlying methodology is broadly consistent with the Department's past salary setting methods, see section IV.A.i., and the salary setting and updating methodology have been promulgated through notice and comment rulemaking.

The Department agrees with commenters that stated that automatic updating will increase predictability in both the frequency and size of salary level changes, benefiting employers and employees alike. We find to be unfounded comments that salary level unpredictability is evident from our statement that "the public will not be able to exactly replicate the weekly earnings and percentiles [used to calculate the salary level] from the public-use files made available by BLS." 80 FR 38528 n.24. This explanatory footnote addressed the public's ability to duplicate BLS' deciles table using the public-use data. The referenced discrepancy is very small, and in no way compromises the public's ability to estimate future salary level changes based on the trend in quarterly earnings data published by BLS.[77] As discussed in the NPRM and above in section

[77] As we noted in the NPRM, to ensure the confidentiality of survey respondents the data in all BLS public-use files use adjusted weights and therefore minor discrepancies between internal BLS files and public-use files exist. See 80 FR 38528 n.24. This means that the public will be able to estimate future salary levels based on BLS' regularly published regional deciles, but will

IV.A.iv., the Department will update the salary level using the deciles table for Census Regions as published by BLS, without modifying the data in any way or otherwise engaging in complex data analysis. This process is transparent, predictable, and straightforward.

The essentially ministerial act of applying the updating mechanism to maintain the salary level underscores why the Department does not share commenter concerns about resetting the salary level without further rulemaking. The Department agrees with commenters that past salary level changes have benefited from (and required) notice and comment rulemaking. This rulemaking is no exception, as public feedback was critical to finalizing the new standard salary level and the automatic updating mechanism. In response to public comments, the Department has changed the data set used for setting and updating the salary level, and (as discussed in greater detail below) chosen to update the salary using the "fixed percentile" approach, increased the period between notice of the updated salary level and its effective date, and changed the updating frequency. But unlike salary updates made up to this point, which have all involved some change to the salary setting methodology, salary level updates under new § 541.607 will use a fixed methodology that (through this rulemaking) has already been subject to notice and comment. Public feedback was critical to finalizing the updating mechanism, but is unnecessary when simply maintaining the salary level using this mechanism. Of course, should the Department choose to make any changes to the updating methodology in the future, such changes would require notice and comment rulemaking.[78]

---

not be able to precisely recreate the salary amounts in the published deciles due to minor adjustments in the publically available data.

[78] Additionally, and as acknowledged in the NPRM, 80 FR 38522, the Department will consider conducting a retrospective review of this Final Rule at an appropriate future time. See Executive Order 13563 (Jan. 18, 2011); see also 5 U.S.C. 610.

The Department also disagrees with commenters that stated that we should simply reallocate agency resources as necessary to maintain an updated salary level. Whereas most regulations require a one-time expenditure of resources to promulgate, and then once issued can remain both unchanged and forceful for many years if not decades, without automatic updating the Department would have to engage in nearly continuous rulemaking to ensure that the salary test accurately reflects employee salary levels. The new automatic updating mechanism will enable the Department to maintain an effective and up-to-date salary level, while preserving our ability to revisit the underlying salary setting methodology through rulemaking as future conditions warrant. For the above reasons, the Department is finalizing our proposal to institute a regulatory mechanism for automatically updating the salary level.

The Department received many comments expressing concern about the financial and administrative burden that annual updating would impose on employers. In particular, many commenters stated that annual updating would require employers to conduct a yearly "classification analysis"—to assess employee exemption status and determine whether salary increases to preserve exempt status are warranted—and then incur additional costs implementing any changes. AIA-PCI; see also, e.g., Business Roundtable; Maryland Chamber of Commerce; PPWO. Several commenters described these costs in detail. For example, the Chamber's comment identified many common concerns:

> The annual salary increase proposed by the Department will require an employer to: Analyze whether business conditions allow a salary increase or whether they need to reclassify employees as non-exempt; prepare new compensation plans for reclassified employees; develop materials to explain the reclassification to employees; review timekeeping and payroll systems to ensure compliance with the FLSA recordkeeping requirements and compliant overtime calculations; review or adopt new policies for the reclassified employees, including policies prohibiting off-the-clock work, when employees will be permitted to work overtime, payment for waiting time, training time and travel time, etc.; train the reclassified employees, and the managers who supervise them on recording time

> and other wage-hour topics. If the salary change is implemented as proposed, a large number of workers will have to be added to timekeeping systems. This may require server and system upgrades to account for the additional users. Best practices take time.

Additionally, ABA stated that automatic updating would require employers to consider whether to restructure the duties of newly nonexempt employees, and NFIB stated that it would require employers to annually "reassess potential raises, bonuses, or promotions" for employees. Seyfarth Shaw and others stated that the Department significantly underestimated the cost and time obligations associated with these actions.

Multiple commenters also emphasized that annual updating would negatively impact employer budgets and budget planning. NALP, NGA, NRF, Wendy's, and others stated that not knowing employee exemption status from year to year would make it more difficult for employers to forecast costs or profit margins. CUPA-HR stated that in response to a survey of its members about the Department's proposal, 91 percent of respondents stated that automatic updating as proposed would negatively impact their budgets, while 63.6 percent said this change would negatively impact financial planning ability. The California State Association of Counties stated that annual updating would be especially hard for public entities because "public sector salaries are generally not as flexible as private sector salaries and have many additional constraints, including bargaining agreements, restricted sources of revenue, and civil service rules." Similarly, several commenters stated that updating would be particularly difficult for non-profit employers that have limited ability to increase revenue in response to increased labor costs. See, e.g., American Academy of Otolaryngic Allergy; BSA; USPIRG. WorldatWork stated that budget overruns resulting from annual salary increases could deplete capital available for other business areas such as research and development, business equity for future growth, or voluntary employer contributions to retirement plans, and FMI stated that budgetary uncertainty and the

"specter of unexpected cost increases provides disincentives for businesses to engage in capital spending and increase hiring and thereby grow the economy."

Several commenters expressed concern that updating could create "salary compression" issues and impede employers' ability to give merit-based salary increases. To illustrate these interrelated concerns, SHRM provided a hypothetical in which ten exempt employees earn $975 per week (above the 2016 salary level of $970 predicted in the NPRM), and an employer budgets for a three percent annual salary increase (totaling $15,210). SHRM contended that without automatic updating the employer could reward better performing employees with large raises and give lower raises or no raise to average or poor performers. If, however, the salary level were automatically increased by two percent, the employer "would be required to adjust all ten salaries up to $989 per week in order to maintain their exempt status," significantly reducing the total amount available for merit increases. SHRM concluded that after several automatic updates "the gap in pay between more senior and less senior, more experienced and less experienced, or more productive and less productive employees will become smaller over time, creating significant morale problems and other management challenges." AIA-PCI stated that automatic updating would in many instances place "an artificial obligation on the company to provide a salary increase to an underperforming employee . . . simply to maintain the employee's exempt status," and NGA stated that if "managers know they will receive an automatic raise each year by meeting minimum performance standards, they have little incentive to work increased hours and take on more responsibility while also maintaining a high performance level." Relatedly, several commenters, including IFA, Littler Mendelson, and Fisher & Phillips, stated that in addition to raising employee salaries to maintain their exempt status, employers will have to

raise the salaries of those earning above the salary threshold to avoid compression in compensation scales among exempt employees.

Some commenters stated that automatic updating would also adversely impact employees. AH&LA, NRF, and others stated that annual updating would create instability in employee compensation and benefits (which are often tied to exempt status) and that employers would likely reduce exempt employee benefits to cover annual updating's administrative costs. Similarly, AT&T stated that uncertainty about employees' year-to-year exemption status will likely cause companies to "hedge against unanticipated overtime payments, thereby putting downward pressure on annual salary increases." Other commenters stated that possible changes in exempt status and employers' inability to provide merit increases will undermine employee morale. See, e.g., CUPA-HR; Seyfarth Shaw. IFA asserted that such complexities illustrate that an automatic updating mechanism is inconsistent with the President's directive to "modernize" the EAP regulations.

The Department acknowledges employers' strong views on the financial and administrative considerations associated with annual automatic updating, and we agree that updating the salary level annually may increase the impact on employers. In particular, we agree that this change may require employers to reassess employee exemption status more frequently and in some instances to more closely monitor hours of newly overtime-eligible employees. These costs are discussed in greater detail in the Department's economic impact analysis, see section VI.D.x. However, the link between automatic updating and other costs commenters have raised is less clear and was generally not supported by data in the comments. Moreover, many commenters did not address the fact that the alternative to automatic updating is not a permanent fixed

standard salary level, but instead larger changes to the standard salary level that would occur during irregular future updates.

The Department believes that in several respects commenters overstated the impact of automatic updating on employers. In some instances commenters failed to account for existing employer practices. For example, the concern that automatic updating will require employers to develop policies and trainings to explain reclassification to newly overtime-eligible employees ignores that employers already have overtime-eligible employees and thus typically have these procedures in place. Additionally, many commenters conflated the distinction between costs associated with the current salary increase (to $913), and those due to future automatic updates. For example, the cost of adding newly overtime-eligible workers to timekeeping systems and reviewing timekeeping and payroll systems to ensure compliance with FLSA recordkeeping requirements are likely overstated. These costs are primarily incurred when employees are initially reclassified, and the Department predicts that the number of reclassified employees at future updates will be much smaller than the number reclassified at the initial salary increase since the updating mechanism will change the salary level regularly and incrementally, and the salary level is based on actual wages of salaried workers.

The Department is also not persuaded that automatic updating (at any frequency) will force employers to reward underperforming employees, impede merit-based pay increases, or create salary compression issues. These interrelated concerns arise from the faulty premise that the automatic updating mechanism will in effect require employers to increase salaries of all affected workers. This is not the case as employers have many options for managing their workforces. The updating mechanism simply adjusts the salary level to ensure that it reflects prevailing salary conditions and can effectively work in combination with the duties test to identify exempt and

nonexempt employees. Because any increase in the salary level is based on actual increases in workers' salaries, employers may find that they are already paying their exempt employees wages above the updated salary level. Where this is not the case, employers can respond to salary level updates by (for example) increasing employee pay to retain overtime exempt status, reclassifying employees to overtime-eligible status, decreasing hours of newly overtime-eligible employees to avoid overtime, paying overtime to newly overtime-eligible workers, redistributing hours among the workforce, and/or hiring new employees. Similarly, employers are under no obligation to reward underperforming employees with a raise (a concern discussed in a number of comments). Employers can reclassify such employees to nonexempt status, redistribute employee workloads, or take any number of other managerial actions in lieu of increasing their salary to maintain the exemption.

The Department is more persuaded by commenter concerns that annual updating would inject uncertainty into the annual employer budgeting process. While the ripple effects of this uncertainty on employee compensation are open to debate, the immediate impact on employers is clear. Although commenters often raised budgeting concerns as part of their general opposition to automatic updating, closer examination reveals that these concerns are closely linked to the updating frequency. For example, comments that updating would impact employers' ability to forecast profit margins, determine store and supply chain labor costs, and plan and implement yearly salary increases, are all most directly implicated by annual updating, as are government and non-profit commenter concerns tied to the lack of short-term control over revenue streams and employee costs. Even some of the commenters that opposed automatic updating agreed that lengthening the period between updates would help alleviate some employer concerns. See, e.g., CUPA-HR (updating every five years "could avoid many of the negative consequences

associated with automatic annual increases"); BSA. Accordingly, the Department is modifying our proposal, which would have updated the salary level annually.

Commenters that favored automatic updating often also favored annual updates. See, e.g., Nichols Kaster; UFCW. Commenters that opposed automatic updating expressed more varied opinions. AT&T, CUPA-HR, SIFMA, and others favored updating no more frequently than every five years, with some noting that this was the shortest interval between the Department's past salary level updates (since 1940). Notably, several of the commenters representing employer interests that supported some form of automatic updating favored revisiting the salary level every three years, see American Council of Engineering Companies; American Resort Development Association; WMATA, as did several commenters that opposed updating generally, see BSA (no more than every two or three years); Fisher & Phillips ("not less than every three years"). Other commenters favored other updating periods. See, e.g., Association of Regional Center Agencies ("no more frequently than biennially").

In response to commenter concerns about the burdens of annual updating, and mindful of the range of views expressed on the appropriate updating frequency, new § 541.607 provides that updating will occur every three years. This change from the Department's proposal strikes an appropriate balance between ensuring that the salary level remains an effective "line of demarcation" and not burdening employers or their workforces with possible changes to exemption status on a yearly basis. Increasing the time period between updates will also decrease the direct costs associated with updating because regulatory familiarization costs are only incurred in years in which the salary is updated and the number of affected workers will drop in years in which the salary is unchanged leading to lower managerial costs in those years. Triennial updates using a fixed and predictable method should significantly mitigate the annual

budget planning concerns that commenters raised. Additionally, employers will always know when the salary level will be updated, and between updates can access BLS data to estimate the likely size of this change. Lengthening the updating frequency to three years also responds to commenter concerns that minor year-to-year fluctuations in employee earnings should not trigger reclassification analyses.

iii. Automatic Updating Method

The Department's proposal discussed and requested comments on two alternative updating methodologies—updating using a fixed percentile of full-time salaried employee earnings or using the CPI-U. As we explained in our proposal, the fixed percentile approach would allow the Department to reset the salary level test by applying the same methodology proposed to set the initial salary level, whereas the CPI-U approach would update the salary amount based on changes to the CPI-U—a commonly used economic indicator for measuring inflation. The Department's proposal did not express a preference for either updating method and instead sought comments on these two alternatives.

The Department received numerous comments addressing these two proposed updating methods, although many commenters that supported automatic updating did not express a methodology preference. See, e.g., AARP; American Association of University Women; Legare, Atwood & Wolfe law firm; Santa Clara County Probation Peace Officers' Union. Commenters that favored automatic updating and expressed a preference for a methodology generally preferred the fixed percentile approach, although some favored the CPI-U method. Both of these groups of commenters preferred either method to no automatic updating. Commenters that opposed any form of automatic updating generally expressed concerns with both updating methods. In some instances, however, these commenters preferred a particular

method (typically the CPI-U) should the Department institute automatic updating. Additionally, a few commenters suggested automatic updating methods not included in the Department's proposal.

The majority of commenters that supported automatic updating and expressed a methodology preference favored the fixed percentile approach. Many of these commenters explained that the reasons for initially setting the salary level at a fixed percentile of earnings of full-time salaried workers also supported updating using the same method. For example, NWLC stated that just as the Department determined that "looking to the actual earnings of workers provides the best evidence of the rise in prevailing salary levels and, thus, constitutes the best source for setting the proposed salary requirement," 80 FR 38533, automatic updating should be based on changes in earnings rather than changes in prices. AFGE, EPI, IWPR, NEA, and many others agreed that salary level updates should reflect changes in wages and not prices, and thus favored updating using a wage index (i.e., the fixed percentile approach) rather than a price index (i.e., the CPI-U). NELP, the Partnership, and others added that a wage index is more appropriate because wages are less volatile than prices and increase in a more consistent and predictable fashion.

Commenters that favored the fixed percentile approach also highlighted the link between wages and the EAP exemptions' purpose and function. NELP stated that using a wage index is consistent with the fact that the exemptions are intended to cover higher-paid employees in the workforce, and NELA stated that this method reflects "the fact that the EAP exemption is, in many respects, premised on an employee's relative position in the workplace" and "is the fairest way to maintain consistency in workers' FLSA eligibility in light of inevitable economic change."

Of the relatively few commenters representing employer interests that supported some form of automatic updating, several favored the fixed percentile method. For example, SIGMA (which favored automatically updating a salary level based on the 2004 method every three to five years) stated that this approach "will help the threshold keep pace with actual wage changes in the market," while an inflation-based index "will risk harming workers and businesses" because inflation and wages "can increase at very different rates." Printing Industries of America and at least eight of its member businesses agreed that "[a]ny indexing should reflect wage changes." Similarly, CVS Health and several non-profit commenters (which incorporated or referenced a comment submitted by ANCOR) favored the fixed percentile approach over the CPI-U, provided in part that the Department account for regional salary level disparities and update the salary level on a less frequent basis than annually.

Most commenters representing employers opposed any form of automatic updating, and many of these commenters strongly opposed automatic updating using the fixed percentile method. The predominant concern among commenters that opposed the fixed percentile approach was that this method would produce drastic increases in the salary threshold level arising from the updating method itself, rather than from market forces. Some of these commenters predicted that employers will respond to each salary level update by converting all or a certain percentage of all full-time salaried employees earning below the new EAP salary level to hourly status. See, e.g., Dollar Tree; HR Policy Association. Others predicted employers would convert all or a certain percentage of affected employees (i.e., those EAP employees earning between the old and new salary levels) to hourly status. See, e.g., Chamber; FMI; Jackson Lewis; NAM; Small Business Legislative Council. Both of these groups of commenters stated that such conversion would decrease the number of salaried workers in the CPS data set by removing those at the lower end

of the salary distribution, which would produce an upward shift (or "ratcheting") of the salary level with each successive update. CUPA-HR, Fisher & Phillips, and others further stated that if employers increase employee salaries to preserve exempt status, this would apply further upward pressure on the 40th percentile, and CUPA-HR and Seyfarth Shaw added that this effect would also occur to the extent employers paid overtime to newly nonexempt salaried workers but did not convert them to hourly pay.

Given these predictions, several commenters estimated the impact that automatic updating using the fixed percentile approach would have on the salary level. Many stated that salary level growth would far exceed the 2.6 percent average annual growth rate for the 40th percentile of full-time salaried workers' weekly earnings that the Department estimated occurred between 2003 and 2013, 80 FR 38587. See, e.g., IFA; Littler Mendelson; Seyfarth Shaw. Other commenters, including the Chamber and FMI, submitted an Oxford Economics letter (prepared for the NRF) which projected that by 2016 annual updating would produce a salary level of approximately $1,400 per week assuming all salaried employees below the standard salary level would be converted to hourly. The Chamber and PPWO referenced (but did not submit) an article from Edgeworth Economics, an employer consulting firm, which stated that if 25 percent "of the full-time nonhourly workers earning less than [the 40th percentile salary level] were re-classified as hourly workers," after five annual updates the salary level would equal $72,436 annually ($1,393 per week). Other commenters provided their own projections of salary level test growth. For example, WorldatWork stated that after five annual updates the salary level would reach $233,217, and HR Policy Association stated that if "the bottom 20 percent of salaried employees" are converted to hourly status the salary level would increase on average by 18 percent per year over five years. Such projections led several commenters to conclude that

automatic updating using the fixed percentile approach would render the duties test increasingly obsolete and in effect eliminate the availability of the EAP exemptions in many regions and industries. See, e.g., NRA; Seyfarth Shaw. ABA captured the views of several employer representatives in stating that, because of concerns that the fixed percentile method would unduly accelerate salary level test growth, automatic updating using the CPI-U is a "less harmful approach to a bad idea." See also NRA.

Most commenters representing employee interests did not discuss whether automatic updating using the fixed percentile approach would lead employers to convert large numbers of newly nonexempt employees to hourly status. One exception was EPI, which stated that employer projections of accelerated salary growth due to mass conversion of employees to hourly pay were inaccurate because they underestimated employee bargaining power by failing to account for low unemployment rates and the fact that "nominal wages are 'sticky,' meaning that employers rarely will lower them." EPI added that employers will have a difficult time converting salaried workers to hourly status because the new salary level will "establish a clearly observable new norm in the workplace" and so it will "be obvious to employees that any reclassification will be done to disadvantage them." For these reasons, EPI concluded that the "wholesale reclassification of current salaried workers to hourly status . . . seems an unlikely outcome."

While employer commenters that opposed the fixed percentile approach generally focused on the concerns discussed above, some commenters also objected to this approach based on the same concerns they raised with respect to the underlying salary level. Commenters criticized the CPS data set, see, e.g., Fisher & Phillips, expressed concern that the proposed methodology results in too high a salary level for low-wage areas, see, e.g., ACRA, and asserted that updating using the same methodology would "compound the Department's error," see PPWO, in setting

the salary level. These commenters opposed any form of automatic updating, but deemed the fixed percentile method particularly troubling.

The Department also received many comments from organizations and individuals favoring automatic updating using the CPI-U. Overall, these commenters addressed this issue in less detail than those that favored the fixed percentile approach, often only stating that the salary level should be updated based on inflation. While the majority of these comments favoring updating using the CPI-U came from individuals, a few employers and commenters representing them also supported this approach. For example, HMR Acquisition Company favored indexing the salary level to inflation (provided the Department also lowers and phases in the new salary level requirement). Many individual commenters also recommended updating using the CPI-U. For example, one human resources professional suggested increasing the salary biennially "with the national rate of inflation," another human resources professional favoring this method stated that changes in the CPI-U are "smaller and easier for employers to absorb," and one individual stated that updating using the CPI-U "will make sure that the rises in the salary level and highly compensated level will mirror economic changes, rather than create a base percentile change yearly that may or may not work for all regions of the country." Board Game Barrister stated that updating using the CPI-U "is both predictable and fair in preventing erosion of the salary test," while the Illinois Credit Union League stated that credit unions are "familiar with the CPI-U and utilize this standard when considering salary increases."

As previously discussed, among commenters representing employer interests that opposed any form of automatic updating, concerns that the fixed percentile approach would quickly escalate the salary level led some commenters to reluctantly prefer the CPI-U. However, these commenters often stressed that they only preferred this method if the Department refused to

withdraw the automatic updating proposal, and they generally did not provide any additional grounds for supporting use of the CPI-U as an updating mechanism. The Colorado Youth Corps Association and Firehouse Subs appeared to support automatic updating using the CPI-U provided that the Department set the initial salary level lower. NRA (which opposed either updating method) provided similar qualified support, stating that "for CPI-U indexing to be considered reasonable, the salary level itself needs to be reasonable."

Other commenters representing employer interests that opposed any form of automatic updating provided reasons not to update the salary level using the CPI-U. The Chamber, FMI, and others stressed that prices and salaries are only correlated in the long-run. Seyfarth Shaw opined that the "CPI-U is a volatile index" and that the basket of goods used to calculate the CPI-U is "not tied in any direct way to employees' wages rates" and is "not an appropriate indicator of wage growth (or decline)." Relatedly, ACRA stated that the fact that there have "been periods where the CPI-U has outpaced wages and other periods where wages have grown faster than CPI-U" illustrates that the CPI-U is "an unreliable benchmark for wages."

Several commenters worried that updating using the CPI-U would have an adverse impact on low-wage regions and industries because inflation does not impact all regions uniformly. For example, Dollar Tree observed that the CPI-U "focuses exclusively on urban areas, and therefore fails to account for the rural economy and cost of living," and Lutheran Services in America Disability Network stated that this updating method "will disproportionately impact different regions, potentially worsening the income disparity and inadvertently harming workers." See also, e.g., ACRA; ANCOR; SIGMA. Other commenters referenced the Department's past decision not to automatically update the salary level using an inflationary index. Although this fact was usually raised to assert that the Department lacked authority to automatically update the

salary level, Fisher & Phillips referenced the Department's recognition in the NPRM that "inflation has been used as a method for setting the precise salary level only in the breach," (emphasis in comment), as indicating that the CPI-U would not be an appropriate updating methodology. 80 FR 38533.

Finally, a few commenters suggested that the Department automatically update the salary level using methods other than those discussed in the NPRM. For example, AFL-CIO and AFSCME urged the Department to consider updating the salary level using BLS' Employment Cost Index for total compensation of management, professional, and related workers. See also UFCW. Many commenters, including several disability services providers, favored updating using "regional salary data." See, e.g., Lutheran Services in America. WMATA stated that automatic updates affecting government entities should be tied to "the federal government's adjustments to General Schedule pay schedules," and the American Resort Development Association favored a fixed annual increase of, for example, two percent. Fisher & Phillips, which opposed both methods, wanted the Department to issue a new proposal to update the salary level using internal Department data on likely exempt workers.

The Department recognizes commenters' strong views on the proposed automatic updating alternatives and has considered the comments concerning this issue. The Department has determined that automatically updating the salary level using a fixed percentile of earnings will best ensure that the salary level test effectively differentiates between bona fide EAP workers who are not entitled to overtime and overtime-eligible white collar workers and continues to work effectively with the duties test. Accordingly, new § 541.607 will reset the salary level triennially using the same methodology used in this rulemaking to set the initial salary level—the

40th percentile of earnings of full-time salaried workers in the country's lowest-wage Census Region.

The Department agrees with the view of many commenters that the same reasons that justify setting the salary level at a fixed percentile of earnings of full-time salaried workers also support updating using this method. As explained at length in section IV.A., setting the initial salary level equal to the 40th percentile of earnings of full-time salaried workers in the South reflects the Department's best determination of the appropriate line of demarcation between exempt and nonexempt workers. This method provides necessary protection for workers by accounting for the elimination of the more stringent long duties test, while at the same time not excluding from exemption too many employees performing EAP duties in low-wage geographic areas, and yielding a lower salary that is appropriate across industries. Likewise, applying this same methodology for automatic updating is the most effective and transparent way to ensure that future salary levels continue to fulfill these objectives and work appropriately with the duties test.

Unlike the CPI-U method, updating the salary level based on the 40th percentile of earnings of full-time salaried workers in the country's lowest-wage Census Region also eliminates the risk that future salary levels will deviate from the underlying salary setting methodology established in this rulemaking. Ensuring that the salary level does not depart from the designated percentile ensures that the salary level does not become too low—leading to an increased risk of inappropriate classification of low-salaried employees as exempt—or too high—depriving employers of the exemption for employees performing bona fide EAP duties, and also ensures that the standard salary level continues to work effectively with the standard duties test. For the same reasons, the Department also declines to automatically update the salary level using any of

the suggested alternatives (such as the Employment Cost Index, GS-Pay Scale, and others). These methods would result in different salary level setting and updating methodologies and thus increase the risk of future salary levels diverging from the appropriate line of demarcation between exempt and nonexempt workers, which would in turn necessitate additional rulemaking to reset the salary level or updating methodology.

The Department also concludes that it is preferable to update the salary level based on changes in earnings rather than changes in prices. As many commenters observed, a wage index provides the best evidence of changes in prevailing salary levels. While wages and prices may be correlated in the long-run, linking the salary level to earnings is the most direct way to ensure that the salary level reflects prevailing economic conditions and can thus fulfill its intended function. This approach is also consistent with the Department's longstanding practice of basing the salary requirement on actual salaries paid to workers. The salary level test works in tandem with the duties test to operate effectively, and we agree with the Chamber, FMI, and others that changes in job duties are more closely correlated with changes in wages than in prices. Similarly, using an earnings index for automatic updates is most consistent with the Department's long-held view that "the best single test of the employer's good faith in attributing importance to the employee's service is the amount [the employer] pays for them." Stein Report at 19. New § 541.607 provides that automatic updates will be based on CPS data for the 40th percentile of earnings of full-time salaried workers in the country's lowest-wage Census Region. This data will be readily available and transparent, and at the designated percentile is representative of those employees who may be bona fide executive, administrative, or professional workers.

Commenters that opposed the fixed percentile approach focused primarily on their concern that this methodology would lead to drastic salary level increases that would render the EAP exemptions virtually obsolete in certain industries and geographic areas. The linchpin of this "ratcheting" argument—and the crux of most opposition to the fixed percentile updating method—is the belief that employers will respond to an automatically updated salary level by converting newly nonexempt workers to hourly status, thus removing them from the data set of full-time salaried workers. The Department examined this issue closely and concludes that past experience and the comments themselves do not substantiate commenter concerns.

To evaluate the likelihood that salary level increases will lead employers to convert affected employees to hourly pay status, the Department first examined historical data concerning how employers responded to the 2004 Final Rule's salary increase. This prior rulemaking raised the standard salary level to 182 percent of the short test salary level—from $250 to $455.[79] As discussed in more detail in section VI.D.ix., if the salary level increase in 2004 led employers to convert significant numbers of workers to hourly status (as commenters assert will result from this rulemaking), then we would expect to see a notable increase in the share of workers earning just below the new threshold ($455) who are paid hourly relative to the share of workers earning just above the new threshold who are paid hourly. The Department looked at the share of full-time white collar workers paid on an hourly basis before and after the 2004 Final Rule (January – March 2004; January – March 2005) both below and above the standard salary level (at least $250 but less than $455 per week; at least $455 but less than $600 per week). The Department

[79] The 2004 Final Rule increased the salary level from the previous long test level of $155 per week (executive and administrative exemptions) or $170 per week (professional exemption) to $455 per week. For purposes of this analysis, the Department compared the increase from the short test salary level ($250 per week) since the long test was no longer operative due to increases in the minimum wage.

found that following the 2004 Final Rule, the share of full-time white collar workers being paid hourly actually decreased marginally in the group below the standard salary level and increased slightly in the group above the standard salary level. See section VI.D.ix. These results do not suggest that the 2004 salary level increase caused an increase in the share of workers paid hourly below the new threshold, and thus provide no evidence that salary level increases due to automatic updating will result in employers converting significant numbers of affected EAP workers to hourly pay status.[80]

In addition to the lack of historical data supporting commenters' concerns, commenters failed to persuasively support their key assumption that automatically updated salary levels will lead to widespread conversion of employees to hourly pay status. Most of these commenters, including Dollar Tree, Jackson Lewis, and several others simply stated—without citing any supporting data—that automatic updating would produce this effect, with several commenters mistakenly contending that such a conversion to hourly status was automatic. Even those commenters that provided more detailed economic analyses often rested their views on the same faulty assumption. For example, the submitted Oxford Economics letter assumed "that the lowest 40% of the salaried full-time wage distribution in 2016 were converted to hourly status." Some commenters predicted the impact of automatic updating on the salary level if a set percentage of employees were converted to hourly pay. For example, HR Policy Association predicted the

[80] To further test whether the widespread conversion to hourly pay status of newly nonexempt employees predicted by some commenters would occur, the Department also performed a similar analysis of increases in the state EAP salary level in California in 2007-2008 and 2014. In 2007-2008, the results showed a decrease in the share of full-time white collar workers paid on an hourly basis below the new salary level, thus providing no evidence of a "ratcheting" effect. In 2014, the share of full-time white collar workers paid on an hourly basis below the salary level increased marginally, but this impact was not significantly different from the change in the rest of the U.S and thus provides no evidence that this effect was caused by changes to the salary level.

effect if "the bottom 20 percent of salaried employees" were converted to hourly status, and the Chamber and PPWO (quoting an article from Edgeworth Economics) commented on the impact if 25 percent "of the full-time nonhourly workers earning less than [the 40th percentile salary level] were re-classified as hourly." But while these commenters stressed the purported impact of these employee conversion rates on the salary level, none explained why these rates are accurate estimates of employer responses.[81]

The Department believes that commenters that asserted that "ratcheting" will occur have greatly overestimated the number of employees that employers may convert to hourly status, and the impact that any such conversion would have on the salary level. Some commenters assumed that all (or a certain percentage of all) full-time salaried workers earning below the salary level would be converted to hourly status and dropped from the data set. This assumption is plainly erroneous because it fails to account for whether the employees perform white collar work and are subject to the EAP exemption. Of the 18.6 million full-time salaried white collar workers earning below the $913 salary level, only 4.2 million are currently exempt and earn between the current and new salary levels. The remaining 14.4 million workers are not currently classified as exempt under the EAP exemption, and so there is no reason to believe that their employers will convert them to hourly pay status as a result of this rulemaking. Accordingly, salary level predictions that are grounded in the belief that a certain percentage of all salaried workers will no longer be included in the BLS data set because they will be converted to hourly pay status regardless of whether or not they are affected by the rule are unsupported.

[81] Oxford Economics stated that its model was "not meant as a literal prediction of what the new rule would mean, since some non-exempt workers still report salaried status in the Current Population Survey, and since the process would be iterative." However, Oxford Economics did not attempt to quantify these other factors to produce a more accurate estimate.

Other commenters predicted that employers would convert all (or a significant percentage of) affected EAP employees to hourly status. The Department believes that these predications are also inaccurate because they fail to account for whether the affected employees work overtime. As discussed in the economic impact analysis of this Final Rule, the majority of workers affected by this rulemaking do not work more than 40 hours per week, and so employers will have no need to change their compensation and can continue to pay them a salary. Even as to those affected EAP workers who will become nonexempt and regularly or occasionally work overtime (which the Department estimates will be approximately 39 percent of the total number of affected EAP workers when the salary level is updated to $913), there is no reason to believe that employers will engage in wholesale conversion of these employees to hourly status. Employers commented at great length during outreach discussions prior to the publication of the NPRM and in the submitted comments that employees desire to be salaried because of status concerns. Also, the FLSA and regulations promulgated under it expressly permit paying nonexempt employees a salary so long as they receive overtime compensation when they exceed 40 hours during a workweek. See §§ 778.113-.114. The Department therefore anticipates that employers will continue to pay many affected EAP workers who work overtime on a salary basis, and these workers therefore will remain part of the distribution of full-time salaried workers. As discussed in detail later, our analysis of the impacts of the 2004 Final Rule further supports our assumption that employers will not convert large numbers of newly overtime-eligible salaried employees to hourly pay status. Accordingly, the pool of workers who are likely to be converted to hourly pay is much smaller than supposed by those commenters that assert that the fixed percentile approach will lead to drastic salary level increases.

To the extent that some affected EAP workers are converted to hourly status and not included in the BLS data set of all salaried workers, the Department believes this will have a negligible impact on the salary level because this group would not constitute more than a small fraction of the population of full-time salaried workers that comprises the data set used to calculate the salary level. The Department believes that employers will have little incentive to change the pay status of those affected employees who do not work overtime (60.4 percent of affected employees); similarly, employers will not change the salaried status of those employees who work overtime and whose salary is raised to maintain their exempt status (2.3 percent of affected employees). The Department therefore believes that an upper bound estimate of any potential "ratcheting" effect would assume the conversion to hourly pay status of all newly nonexempt employees working either occasional or regular overtime (approximately 37.3 percent of affected employees). Based on this assumption, the Department estimated that the salary level as set in this Final Rule (based on weekly earnings of full-time salaried workers in the South) could be approximately two and a-half percent higher due to this effect in 2026, after three updates. This estimate is significantly smaller than the estimates provided by commenters that argued use of a fixed percentile for updating would lead to widespread conversion of salaried employees to hourly pay status. See section VI.D.ix.

The sample used to set the standard salary level—full-time salaried workers in the South—represents 20 million workers, including, for example, blue-collar salaried workers to whom this rulemaking does not apply and overtime-eligible white collar employees. The Department estimates that 671,000 affected EAP employees in the South regularly or occasionally work overtime, which represents just 3.3 percent of the sample. For the reasons discussed above, many of these workers are likely to remain salaried. But as noted above, even if we assume that

all affected employees who occasionally or regularly work overtime are converted to hourly pay status (and therefore are no longer part of the sample), the impact on the salary level will be minimal because they constitute such a small percentage of the sample. For the same reasons, the Department does not share commenter concerns that the salary level will drastically increase if employers raise affected employees' salaries to preserve their exempt status. The Department estimates that approximately 43,000 affected employees in the South will fall into this category, constituting just 0.2 percent of the 20 million workers in the sample.

For the above reasons, the Department concludes that automatically updating the salary level using a fixed percentile of earnings will not cause the salary level to diverge from prevailing economic conditions, and thus we do not share commenters' concerns about "ratcheting" or believe that they provide a basis for declining to adopt the fixed percentile updating method. Moreover, the Department's decision to reset the salary level triennially (instead of annually) would further minimize any ratcheting if such an effect were to occur.

Beyond concerns about a possible ratcheting effect, commenters raised relatively few additional objections to the fixed percentile method of automatic updating. The Department agrees with commenters that updating the salary level using an inappropriate earnings percentile would produce an improper salary level. However, for the reasons previously discussed at length, the Department has concluded that setting the salary level at the 40th percentile of earnings of full-time salaried workers in the lowest-wage Census Region produces the appropriate line of demarcation between exempt and nonexempt workers. Similarly, the Department's decision to change the updating mechanism from a nationwide to a regional data set addresses commenter concerns about the impact of the fixed percentile approach on low-wage regions and industries.

The Department believes that the chosen updating method is also responsive to many of the reasons that commenters provided for supporting updating using the CPI-U. For example, some commenters lauded the CPI's familiarity and widespread acceptance. The CPS data set is publicly available, as is BLS' deciles table for Census Regions that the Department will use for automatic updates. Other commenters stressed that updating using the CPI-U would ensure that the salary level keeps pace with inflation. These commenters were generally concerned with the adverse effect of a fixed salary level, as opposed to the effect of updating using the CPI-U versus another approach. The Department believes that a regularly updated salary level reflecting changes in salaries paid will largely alleviate this inflation concern, particularly to the extent that changes in wages and prices are correlated over time. For all the above reasons, the Department has decided to automatically update the salary level using the 40th percentile of earnings of full-time salaried workers in the country's lowest-wage Census Region.

The Department's proposal also sought public comment on whether automatic updates to the salary level should take effect based on the effective date of the Final Rule, on January 1, or on some other specified date. The majority of commenters that addressed this issue favored January 1. For example, Tinker Federal Credit Union stated that this date corresponds with when their internal pay changes become effective, and AH&LA stated that updating the salary level mid-year could cause newly nonexempt employees to "lose eligibility for a bonus and fringe benefits that he or she was counting on when the year began." Other commenters, including Nichols Kaster, Quicken Loans, and several small businesses, also favored January 1. In contrast, other organizations favored a July 1 effective date for automatically updated salary levels. ANCOR and numerous other non-profit organizations favored this date because their funding is linked to state budget cycles, and the "majority of states have a budget cycle that ends in June."

As multiple commenters observed, employers operate on varying fiscal calendars, and so it is impossible for the Department to select an effective date for automatically updated salary levels that will suit everyone. After reviewing commenter submissions on this issue, the Department has determined that future automatic updates to the salary level will take effect on January 1. The Department believes this effective date aligns with the pay practices of many employers and, when combined with the 150-day advance notice period, will best promote a smooth transition to new salary levels. While we recognize that some commenters favored new rates taking effect on July 1 to account for state budgeting cycles, any disruption caused by the January 1 effective date is mitigated by the Department's decision to update the salary level every three years and increase the amount of notice before automatically updated rates take effect. These changes ensure that those who favored a different effective date have ample notice of both when the Department will issue new salary levels and when these rates will apply.[82]

The Department also proposed to publish a notice with the new salary level in the Federal Register at least 60 days before the updated rates would become effective. Commenters that explicitly addressed this issue generally favored a longer notice period. For example, the American Council of Engineering Companies supported automatic updating but stated that "120 days' notice would be more workable for employers." Many commenters that opposed automatic updating similarly sought more advance notice should the Department go forward with

[82] The U.S. Department of Treasury-Office of Human Capital Strategic Management asked that each automatically updated salary level become effective at "the start of the pay period following the date of the annual adjustment" in order to avoid having a new salary level take effect in the middle of a pay period. We appreciate this comment, but have decided not to institute this requested change. The Department has always made new salary levels effective on a specific date, rather than in relation to employer pay periods. We believe this practice remains appropriate, and that any administrative burden on employers will be minimal given that salary level changes will occur triennially and the Department will publish the new salary level in the Federal Register at least 150 days before it takes effect.

the proposal. See, e.g., ABA (at least six months); CUPA-HR (at least one year); SHRM (at least one year). Finally, some commenters deemed 60 days of notice inadequate, but did not suggest an alternative. See, e.g., Credit Union National Association; NFIB; Seyfarth Shaw; University of Wisconsin.

In response to commenter concerns, the Department is increasing from 60 to at least 150 days the amount of notice provided before the updated salary level takes effect. The Department believes that this change will provide employers sufficient time to adjust to the new salary level, especially since (as previously discussed) between updates employers will be able to access BLS data to help anticipate the approximate size of the salary level change, while also ensuring that salary level updates are based on the most recent available data. This increase to 150 days is also more than the amount of notice the Department has provided in each of our prior rulemakings increasing the salary threshold. Accordingly, § 541.607(g) states that the Department will publish notice of the new salary level no later than 150 days before the updated rate takes effect.

As discussed in more detail in the economic impact analysis, the Department will set the new salary level using BLS' deciles table of Census Regions, without modifying the data in any way.[83] In order to ensure that the updated salary level is based on the most recent data, the Department will use data from the second quarter (April - June) of the year prior to the update. For example, the salary level that will take effect on January 1, 2020 will be published in the Federal Register on or before August 4, 2019, and will be based on BLS data for the second quarter of 2019.

The Department also proposed to update the HCE total annual compensation requirement with the same method and frequency used to update the standard salary level test. Relatively few

[83] This deciles table is currently available at: http://www.bls.gov/cps/research_series_earnings_nonhourly_workers.htm.

commenters specifically addressed this aspect of the Department's proposal, and those that did generally supported updating using the same method—the fixed percentile approach or the CPI-U—used for updating the standard salary level. See, e.g., NEA; NELA; Partnership; and several individual commenters. Similarly, those that opposed automatically updating the standard salary level also opposed automatically updating the HCE total annual compensation requirement. See, e.g., PPWO; Seyfarth Shaw. In light of these comments, and given our decision to update the standard salary level using the fixed percentile method, the Final Rule provides that the Department will automatically update the HCE total annual compensation level triennially to keep it at the annualized value of the 90th percentile of the weekly earnings of full-time salaried workers nationwide. This updating methodology will ensure that only those who are "at the very top of [the] economic ladder" satisfy the total annual compensation requirement and are thus subject to a minimal duties test analysis. 69 FR 22174. The Department also finalizes our proposal to update the portion of the total annual compensation level that employers must pay on a salary basis ($913 as of the effective date of this rule) so that it continues to mirror the amount of the standard salary requirement as it is updated. As previously discussed in sections IV.C., 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.

Finally, the Department proposed to automatically update the special salary level test for employees in American Samoa by keeping it at 84 percent of the standard salary level, and to automatically update the base rate test for motion picture industry employees by changing the base rate proportionately to the change in the standard salary level. See 80 FR 38541. The

Department did not receive any comments opposing these proposed updating mechanisms, and new §§ 541.607(b) and (c) finalize these proposals.

F. Duties Requirements for Exemption

Examination of the duties performed by the employee has always been an integral part of the determination of exempt status, and employers must establish that the employee's "primary duty" is the performance of exempt work in order for the exemption to apply. Each of the categories included in section 13(a)(1) has separate duties requirements. As previously discussed, from 1949 until 2004 the regulations contained two different duties tests for executive, administrative, and professional employees depending on the salary level paid—a long duties test for employees paid a lower salary, and a short duties test for employees paid at a higher salary level. The long duties test included a 20 percent limit on the time spent on nonexempt tasks (40 percent for employees in the retail or service industries). In the 2004 Final Rule, the Department replaced the differing short and long duties tests with a single standard test for executive, administrative, and professional employees that did not include a cap on the amount of nonexempt work that could be performed.

The Department has always recognized that the salary level test works in tandem with the duties requirements to identify bona fide EAP employees and protect the overtime rights of nonexempt white collar workers. The Department has often noted that as salary levels rise a less robust examination of the duties is needed. This inverse correlation between the salary level and the need for an extensive duties analysis was the basis of the historical short and long duties tests. While the salary provides an initial bright-line test for EAP exemption, application of a duties test is imperative to ensure that overtime-eligible employees are not swept into the

exemption. While the contours of the duties tests have evolved over time, the Department has steadfastly maintained that meeting a duties test remains a core requirement for the exemption.

As explained in the NPRM, however, the Department is concerned that under the current regulations employees in lower-level management positions may be classified as exempt and thus ineligible for overtime pay even though they are spending a significant amount of their work time performing nonexempt work. In such cases, there is a question as to whether the employees truly have a primary duty of EAP work. The Department believes that our pairing in the 2004 rulemaking of a standard duties test based on the less stringent short test for higher paid employees, with a salary level based on the long test for lower paid employees, has exacerbated these concerns and led to the inappropriate classification as EAP exempt of employees who pass the standard duties test but would have failed the long duties test. As we noted in the NPRM, this issue can arise when a manager is performing exempt duties less than 50 percent of the time, but it is argued that those duties are sufficiently important to nonetheless be considered the employee's primary duty. It can also arise when a manager who is performing nonexempt duties much of the time is deemed to perform exempt duties concurrently with those nonexempt duties, and it is argued the employee is exempt on that basis.

While the Department believed that the proposed salary level increase, coupled with automatic updates to maintain the effectiveness of the salary level test, would address most of the concerns relating to the application of the EAP exemption, we invited comments on whether adjustments to the duties tests were also necessary. The Department did not propose any specific changes to the duties tests, but instead requested comment on a series of specific issues:

A. What, if any, changes should be made to the duties tests?

B. Should employees be required to spend a minimum amount of time performing work that is their primary duty in order to qualify for exemption? If so, what should that minimum amount be?

C. Should the Department look to the State of California's law (requiring that 50 percent of an employee's time be spent exclusively on work that is the employee's primary duty) as a model? Is some other threshold that is less than 50 percent of an employee's time worked a better indicator of the realities of the workplace today?

D. Does the single standard duties test for each exemption category appropriately distinguish between exempt and nonexempt employees? Should the Department reconsider our decision to eliminate the long/short duties tests structure?

E. Is the concurrent duties regulation for executive employees (allowing the performance of both exempt and nonexempt duties concurrently) working appropriately or does it need to be modified to avoid sweeping nonexempt employees into the exemption? Alternatively, should there be a limitation on the amount of nonexempt work? To what extent are exempt lower-level executive employees performing nonexempt work?

Finally, the Department solicited feedback regarding whether to add additional examples of specific occupations to the regulations to provide guidance in administering the EAP exemptions, particularly for employees in the computer and information technology industries. See 80 FR 38543.

After considering the comments received in response to the questions posed in the NPRM, the Department has decided against making any changes to the standard duties test or adding new examples to the regulations at this time. The Department recognizes that stakeholders have strong and divergent views about the standard duties test. We also recognize that changes to the

duties test can be more difficult for employers and employees to both understand and implement. As explained in greater detail below, the Department believes that the standard salary level adopted in this Final Rule coupled with automatic updating in the future will adequately address the problems and concerns that motivated the questions posed in the NPRM about the standard duties test.

As an initial matter, many commenters asserted that the Department lacks the legal authority to enact any changes to the job duty requirements in this Final Rule without first proposing specific regulatory changes in a new NPRM. As we explained earlier with respect to our automatic updating mechanism, nothing in the APA or other referenced laws requires an agency's proposal to include regulatory text for all provisions that may appear in a final rule. See section IV.E.i.

There were some areas of agreement among the commenters in response to the questions posed in the NPRM. For example, a wide cross-section of commenters opposed the idea of reintroducing the long test/short test structure that existed before the 2004 rulemaking. A joint comment submitted by 57 labor law professors stated "it is now true that reimplementation of the two-tiered standards would serve to complicate, rather than simplify, the test for the exemption currently in use." Commenters representing employers stated that resurrecting the pre-2004 long test/short test structure would contravene the President's expressed intent to modernize and simplify the FLSA's overtime regulations, and expressed concern about the burden such an approach would impose. See, e.g., Fisher & Phillips; FMI; Littler Mendelson; RILA; Seyfarth Shaw; Sheppard Mullin. Commenters representing employee interests, such as NELA, explained that "having two tests resulted in inefficient litigation as to which test applied to which employees for which periods of time," concluding that "it is best to proceed with a standard

duties test supported by a realistic and fully indexed salary level test." See also Employee Rights Advocacy Group; Rudy, Exelrod, Zieff & Lowe.

Many commenters also seemed to appreciate the inverse relationship between the duties test and the salary level test. For example, although it disagreed with the Department's proposed standard salary level, HR Policy Association stated it "strongly agrees with the Department that the proposed salary level increase addresses the concerns relating to executive employees performing nonexempt duties." See also Employers Association of New Jersey. EEAC noted that "a robust salary threshold and strict duties tests" (emphasis in comment) would inappropriately screen out employees who should be classified as exempt. Commenters including AFL-CIO and the Alaska Department of Labor and Workforce Development, however, asserted that the proposed salary level was not sufficiently high to work with the current duties test and therefore the duties test needed to be strengthened.

Comments on the merits of changing the current duties requirements were sharply divergent, with many employee advocates supporting additional requirements to strengthen the standard duties test and most employer organizations strongly opposing any changes. Commenters representing employees generally asserted that changes to the standard duties test are needed to narrow the scope of an FLSA exemption they believe has been applied too broadly, as well as to reduce litigation and compliance costs attributable to the ambiguity and subjectivity of the primary duty test. Commenters representing employers generally opposed changes to the current duties test on the grounds that the kind of changes contemplated by the Department in the NPRM would be excessively burdensome and disruptive for employers and undermine the President's goal of modernizing the EAP regulations.

As a general matter, commenter views on the adequacy of the regulation's existing duty requirements reflected their broader disagreement over whether employees who pass the primary duty test but perform substantial amounts of nonexempt work should qualify as "bona fide" EAP workers. AFL-CIO, AFT, and SEIU, for example, stated that the standard duties test undermines the breadth of coverage critical to the success of the FLSA by allowing employers to exempt too many workers performing substantial amounts of nonexempt work, including workers earning more than the standard salary level proposed in the Department's NPRM. In contrast, the American Staffing Association and NSBA stated that the standard duties test appropriately emphasizes the importance of an employee's primary duty, not incidental nonexempt tasks he or she may also perform. Several commenters representing employers asserted that the duties test must account for the fact that exempt employees now perform more of their own clerical duties without the support of nonexempt administrative support staff. See, e.g., Joint Comment of the International Public Management Association for Human Resources and the International Municipal Lawyers Association.

Employee and employer organizations similarly disagreed over whether the current standard duties test adequately works to prevent the misclassification of workers who do not meet the duties test and thus should receive overtime pay. Commenters representing employees, like NELP, stated that ambiguities in the existing duty requirements "enable employers to easily and successfully manipulate employee job titles to sweep more workers into the EAP exemptions." Some employers, however, disagreed that non-compliance by employers is prevalent, with SHRM asserting that there is no evidence that the standard duties test leads to "mass misclassification of employees." The New Jersey Employers Association commented that

purported non-compliance in specific industries like restaurant or retail does not justify imposing burdensome new requirements on all employers throughout the entire economy.

Commenter views diverged even more sharply in response to the specific issues raised for consideration. Many employee advocates supported the introduction of a minimum requirement for time spent on an employee's primary duty to the standard duties test. A large number of these commenters endorsed the adoption of a California-style rule, which would require at least 50 percent of an employee's time to be spent exclusively on work that is the employee's primary duty. See, e.g., AFSCME; Bend the Arc; ELC; Employment Justice Center; IWPR; Moreland law firm; National Women's Law Center; NDWA; NELP; Northwest Workers Justice Project; Partnership; SEIU; Shriver Center; Women Employed; Workplace Fairness. Other employee advocates expressed the point as a preference for a 50 percent limit on nonexempt work. See, e.g., AFL-CIO; EPI; Nichols Kaster; Outten & Golden law firm. UFCW supported a 40-percent limit on the performance of nonexempt work, while Legare, Attwood & Wolfe supported reinstatement of the 20-percent limit on nonexempt work that existed under the former long duties test.

In support of such requirements, AFL-CIO, EPI, NELA, Nichols Kaster, and several other commenters asserted that employees who spend a majority of their time performing nonexempt duties should not qualify under the law as "bona fide" EAP workers. Legare, Attwood & Wolfe stated that while the percentage of time an employee spends performing duties is not a perfect indicator of her primary duty, it is a "very good proxy." ELC, the Moreland law firm, NELA, and several others asserted that adding a "bright-line" quantitative component to the standard duties test would simplify compliance or reduce FLSA litigation attributable to the subjectivity

of the primary duty test, while AFL-CIO stated that implementing a more objective duties test would lead to fewer "anomalous outcomes" from court decisions analyzing similar sets of facts.

Several commenters representing employers addressed the issue of concurrent duties—that is, the provision in the executive duties test that permits employees to perform nonexempt duties while simultaneously performing exempt management duties. See § 541.106. A number of employer representatives noted that the Department examined this issue in 2004 when the concurrent duties regulation was promulgated as a separate provision and asserted that there was no need for the Department to alter the conclusions we reached at that time. See, e.g., Chamber; FMI; IFA; Littler Mendelson. Other commenters discussed how the regulation applied to particular work environments. See, e.g., ACRA ("Managers and assistant managers employed by ACRA's members often 'lead by example' by illustrating to subordinate employees how to provide top-notch customer service and take pride in all aspects of one's job."); RILA ("Leading by example by lending a hand at the cash register or on the sales floor is essential to employee training and morale, as well as good customer service."); Southeastern Alliance of Child Care Associations ("The 'concurrent duties' concept is of particular relevance to the child care industry. Consider, as an illustration, a director who, in cleaning and/or feeding a young student, simultaneously trains a new teacher on how students are to be cleaned and/or fed in compliance with state regulatory requirements."). UFCW, however, questioned whether employees were, in fact, leading by example and pitching-in or, instead, were being required by their employers to perform such large quantities of nonexempt work that their primary duty could not be said to be management. See UFCW ("many employers maintain policies which require exempt managers to spend substantial periods of time performing nonexempt hourly work" because they "do not budget sufficient hours for nonexempt employees to complete the work."). Some individual

commenters echoed this concern. For example, a retail store manager described working 55-60 hours a week and because of low staffing noted that he has little "flexibility when an employee calls out sick. I have to pick up the slack." Similarly, a manager of a community home for the intellectually disabled stated that "[t]o reduce organizational overtime, managers are expected to work when employees call in sick, are on leave, and when a client is in the hospital and needs a 24 hour sitter."

While few commenters representing employees specifically addressed the concurrent duties provision, many endorsed California's duties test, which NWLC observed does not allow employers to credit "time during which non-exempt work is performed concurrently." See Heyen v. Safeway Inc., 157 Cal. Rptr. 3d 280, 299-304 (Cal. Ct. App. 2013). AFL-CIO explained that it "is not enough to require that 'bona fide' EAP employees spend 50 percent of their time doing exempt work: they must spend 50 percent of their time exclusively on exempt work." (emphasis in comment); see also NELA; UFCW. Outten & Golden explicitly requested the Department to rescind the concurrent duties provision, asserting that it contributes to the confusion surrounding the application of the executive exemption and fails to account for instances "when the amount of non-exempt work overwhelms [an executive's] capacity to perform their supervisory functions."

Commenters representing employers strongly opposed the addition of any kind of limitation on the performance of nonexempt work to the standard duties test and any revisions to the concurrent duties regulation, stating that such changes would fail to account for the realities of the modern workplace. See, e.g., Chamber; HR Policy Association; NCCR; NRF; NSBA; SIGMA. Further, many commenters, including AH&LA, NRA, Petroleum Marketers Association of America, PPWO, and SHRM, stated that imposing any quantitative restrictions or

eliminating the concurrent duties regulation would prevent exempt employees from "pitching in" during staff shortages or busy periods, increasing labor costs or negatively affecting business efficiency and customer service. A few commenters representing employers also asserted such changes would undermine the sense of teamwork in the workplace. See, e.g., American Resort Developmental Association; NCCR; Weirich Consulting.

AIA-PCI, NFIB, PPWO, and many others objected that introducing a cap on nonexempt work to the standard duties test would also impose significant recordkeeping burdens on employers, and several commenters, including the Chamber, Littler Mendelson, and RILA, noted that the Department previously acknowledged such concerns in the 2004 Final Rule. See 69 FR 22127. Some commenters, including AH&LA and NFIB, also asserted that the recordkeeping burden would at least partially fall onto exempt employees themselves. In addition, many commenters representing employers asserted that introducing a quantitative component to the duties test would increase FLSA litigation due to the administrative difficulties associated with tracking the hours of exempt employees. See, e.g., AIA-PCI; CalChamber Coalition; Seyfarth Shaw; Weirich Consulting. FMI, IFA, Littler Mendelson, and the Chamber all noted that departing from the holistic approach to the standard duties test would "result in the upheaval of the past decade of case law and agency opinions."

After considering the comments, the Department has decided against adding a quantitative limitation on the performance of nonexempt work in the standard duties test, or making any other revisions to the duties test in this rulemaking. The Department continues to believe that, at some point, a disproportionate amount of time spent on nonexempt duties may call into question whether an employee is, in fact, a bona fide EAP employee. We also understand the concerns of some commenters that contend that the qualitative nature of the primary duty test may allow the

classification of lower-level employees as exempt and thus ineligible for overtime pay even though they are spending a significant amount of work time performing nonexempt work. The Department expects that setting the standard salary level at the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region and updating that salary level on a regular basis going forward will address these concerns, which we believe are most prevalent among low-salaried white collar employees. While this salary level is lower than that proposed in the NPRM, the Department believes that it is sufficient to work effectively in combination with the current duties test. The Department will consider the impact of this rule going forward to ensure that the salary level and the duties test continue to work together to appropriately distinguish between exempt EAP employees and overtime-protected white collar workers.[84]

The Department also understands the concerns of employers and their advocates that prohibiting managers from "pitching-in" could negatively affect the workplace. The Department believes, however, that there is an important difference between a manager who occasionally demonstrates how to properly stock shelves to instruct a new employee, or who occasionally opens an additional cash register to assist in clearing a line of waiting customers, and a manager who must routinely perform significant amounts of nonexempt work because her employer does not provide appropriate staffing on all shifts. See AH&LA ("In short, when an exempt manager

[84] Some commenters, including AT&T, the Brevard Achievement Center, Eden Financial, and the Nixon Peabody law firm, suggested eliminating the duties test entirely, making exempt status dependent on the amount of an employee's salary alone. As we have done in prior rulemakings, we again reject such an approach as precluded by the FLSA. As the Department said in 1949, the "Administrator would undoubtedly be exceeding his authority if he included within the definition of these terms craftsmen, such as mechanics, carpenters, or linotype operators, no matter how highly paid they might be." Weiss Report at 23. Most recently, in the 2004 Final Rule, we stated "the Secretary does not have authority under the FLSA to adopt a 'salary only' test for exemption." 69 FR 22173. Our conclusion that there is a necessity for the duties tests in order to define who is a bona fide exempt EAP employee has not changed.

makes the decision that he or she needs to perform non-exempt duties to help the operation run smoothly, the manager's primary duty continues to be managing his or her staff and the operations of their department."); NRA ("Performing hands-on work at the manager's own discretion to ensure that operations are successfully run in no way compromises the fact that the manager's primary responsibility is performing exempt work."). In those situations such as those described by employee commenters above, where managers as a practical matter must perform significant amounts of nonexempt work, the Department does not believe that the manager is in any meaningful sense able to "make the decision regarding when to perform nonexempt duties" and a close examination of the specific facts must be made of whether the employee's primary duty is, in fact, the performance of exempt work. § 541.106(a).

In the NPRM, the Department also sought feedback regarding whether additional occupation examples should be added to the regulations, and, if so, which specific examples would be most helpful to include. Some commenters, including the American Staffing Association, the Maryland Chamber of Commerce, and the Poarch Band of Creek Indians, agreed that adding new examples to the regulations would be helpful in applying the EAP exemption. The American Trucking Association stated that additional regulatory examples would be particularly useful for clarifying the administrative employee exemption, which many commenters asserted is more ambiguous than the executive or professional exemptions. A number of commenters offered specific suggestions of occupations they would like to see addressed in the regulations. See, e.g., American Staffing Association (staffing firm recruiters and account managers); American Trucking Association (truck company dispatchers); Information Technology Alliance for Public Sector (employees performing various computer-related duties); Joint Comment of Postdoctoral Associations and individuals (postdoctoral fellows); Printing Industries of America

(customer service representatives). The Fraternity Executives Association, the International Association of Fire Chiefs, and the Michigan Society of Association Executives, requested regulatory examples relevant to associations, membership organizations and charitable foundations.

ABA and several commenters representing employees, including AFL-CIO, however, asserted that regulatory examples distract from the longstanding principle that job titles alone are insufficient to establish the exempt status of an employee. Nichols Kaster stated that regulatory examples of exempt occupations "encourage employers to manipulate job descriptions to classify non-exempt employees as exempt." Finally, AFL-CIO and NELA each stated that including additional examples of generally exempt or generally nonexempt occupations is neither helpful nor necessary.

Upon further consideration, the Department has decided against introducing any new examples to the existing regulations in this rulemaking. We note that the existing examples in the regulations do not provide categorical exemptions for certain occupations but instead set out typical job duties associated with specific occupations which if performed by an employee generally would, or generally would not, qualify the employee for exemption. In all instances, it is the application of the duties test to the specific facts of the employee's work that determines whether the employee satisfies the requirements for the EAP exemption. Although the Department received feedback on suggested regulatory examples from some commenters, the stakeholder input we received overall did not justify the introduction of any new examples into the EAP regulations at this time.

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, requires 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 July 6, 2015, see 80 FR 38516, 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 September 29, 2015, 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 dated July 6, 2015.

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 the both minimum wage and overtime provisions). Additionally, the changes adopted in this Final Rule may cause an initial increase in burden if more employees file a complaint 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. Several employer commenters and those representing them stated that employers would need to maintain records of hours worked for more employees as a result of our proposal to increase the salary level. See, e.g., American Feed Industry Association; National Roofing Contractors Association; Nebraska Furniture Mart. Many of these comments came from individual employers as part of a campaign organized by the National Automatic Merchandising Association (NAMA), stating that the Department's proposal to raise the salary threshold would "create a challenge by placing a burden on the employers to closely track nonexempt employees' hours to ensure compliance with overtime pay and other requirements," and this "tracking of hours would also produce increased human resources paperwork." The Office of Advocacy of the U.S. Small Business Administration asserted that increasing the salary level as the Department proposed would add "significant" paperwork burdens on small entities, "particularly businesses in low wage regions and in industries that operate with low profit margins." In addition, some commenters expressed concern that the Department's cost estimates related to recordkeeping were too low, given that employers would need to set up revised recordkeeping and payroll systems for newly overtime-eligible employees. See, e.g., NSBA; Reid Petroleum; SA Photonics; Seyfarth Shaw; Surescan Corporation. The National Association for Home Care and Hospice asserted that if the Department were to adopt the proposed salary level, home care and hospice companies would

need to "completely modify their recordkeeping on worker time," and "such changes will double payroll management costs." In response to these comments, the Department notes that we believe 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 methodology for the PRA burdens. The actual recordkeeping requirements are not changing in the Final Rule. However, the pool of workers for whom an employer 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.

A number of commenters also expressed concern about potential changes to the duties tests. Some commenters specifically articulated concern about implementing a percentage duties test. See, e.g., American Society of Association Executives (ASAE); Community Bankers Association; International Franchise Association; Lutheran Services of America; Society for Human Resources Management. For example, Walmart stated that it "would be concerned if such a proposal includes any quantitative or time based assessment of an exempt employee's duties or further, a prohibition on concurrent duties. Such changes would require employers to undertake significant recordkeeping burdens and add to the uncertainty over classifications." Other commenters expressed their view that the Department would violate the PRA by making any changes to the duties tests, because the Department did not provide specific proposed changes to the duties tests in the NPRM. See, e.g., ASAE; Christian Camp and Conference Association, International; Community Bankers Association; Diving Equipment and Marketing

Association; Equal Employment Advisory Committee; International Bancshares Corporation, International Dairy Foods Association; Island Hospitality Management; National Council of Chain Restaurants; National Retail Federation; New Jersey Association of Mental Health and Addiction Agencies; Recreational Diving Industry; WorldatWork; YMCA-USA. Since the Department has decided against enacting any changes to the standard duties test or adding new examples to the current regulatory text at this time, these commenters' concerns have been addressed.

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.

OMB Control Number: 1235-0018.

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

Total Respondents: 5,511,960 (2,506,666 affected by this Final Rule).

Total Annual Responses: 46,057,855 (2,552,656 from this Final Rule).

Estimated Burden Hours: 3,489,585 (2,506,666 from this Final Rule)

Estimated Time per Response: various.

Frequency: various.

Total Burden Cost (capital/startup): 0.

Total Burden Costs (operation/maintenance): $126,392,768 ($90,791,443 from this Final Rule).

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: 37,367 (2,017 added by this rulemaking)

Estimated Number of Responses: 37,367 (2,017 added by this rulemaking)

Estimated Burden Hours: 12,456 (672 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, of reducing costs, of harmonizing rules, and of promoting flexibility.

Under Executive Order 12866, the Office of Management and Budget (OMB) must determine whether a regulatory action is a "significant regulatory action," which includes an 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. Therefore, the Department has prepared a Regulatory Impact Analysis (RIA)[85] in connection with this Final Rule as required under section 6(a)(3) of Executive Order 12866, and OMB has reviewed the rule.

A. Introduction

i. Background

The Fair Labor Standards Act (FLSA or Act) 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. It is widely recognized that the general requirement that employers pay a premium rate of pay for all hours worked over 40 in a workweek is a cornerstone of the Act, grounded in two policy objectives. The first is to spread employment (or, in other words, reduce involuntary unemployment) by incentivizing employers to hire more employees rather than requiring existing employees to work longer hours. The second policy objective is to reduce overwork and its detrimental effect on the health and well-being of workers.

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. Such employees perform work that cannot easily be spread to other workers after 40

[85] The terms "regulatory impact analysis" and "economic impact analysis" are used interchangeably throughout this Final Rule.

hours in a week and that is difficult to standardize to any timeframe; they also typically receive more monetary and non-monetary benefits than most blue collar and lower-level office workers. 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 part 541.

For an employer to exclude an employee from minimum wage and overtime protection pursuant to the EAP exemption, the employee generally must 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 Department has periodically updated the regulations governing these tests since the FLSA's enactment in 1938, most recently in 2004 when, among other revisions, the Department created the standard duties test and paired it with a salary level test of $455 per week. The Department also established an abbreviated duties test for highly compensated employees (HCE)—i.e., white collar workers with a total annual compensation of at least $100,000. To satisfy the total annual compensation requirement, an employee must earn at least $455 per week on a salary or fee basis, and total annual compensation may also include commissions, nondiscretionary bonuses, and other nondiscretionary compensation.

As a result of inflation, the real value of the standard salary and HCE compensation thresholds have fallen significantly since they were set in 2004, making them inconsistent with Congress'

intent to exempt only "bona fide" EAP workers, who typically earn salaries well above those of any workers they may supervise and presumably enjoy other privileges of employment such as above average fringe benefits, greater job security, and better opportunities for advancement. Stein Report at 21-22. For example, the annualized equivalent of the standard salary level ($23,660, or $455 per week for 52 weeks) is now below the 2015 poverty threshold for a family of four ($24,036).[86] Similarly, by October 1, 2016, approximately 20 percent of full-time salaried workers are projected to earn at least $100,000 annually, almost three times the share who earned that amount when the HCE test was created.

The premise behind the standard salary level test and the HCE total annual compensation requirement is that employers are more likely to pay higher salaries to workers in bona fide EAP jobs. A high salary is considered a measure of an employer's good faith in classifying an employee as exempt, because an employer is less likely to have misclassified a worker as exempt if he or she is paid a high wage. Stein Report at 5; Weiss Report at 8.

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. Throughout the regulatory history of the FLSA, the Department has considered the salary level test the "best single test" of exempt status. Stein Report at 19. This bright-line test is easily observed, objective, and clear. Id.

[86] This is the 2015 poverty threshold for a family of four with two related people under 18 in the household. Available at: http://www.census.gov/hhes/www/poverty/data/threshld/index.html.

ii. Need for Rulemaking

The salary level test has been updated seven times since it was implemented in 1938. Table 1 presents the weekly salary levels associated with the EAP exemptions since 1938, organized by exemption and long/short/standard duties test.[87]

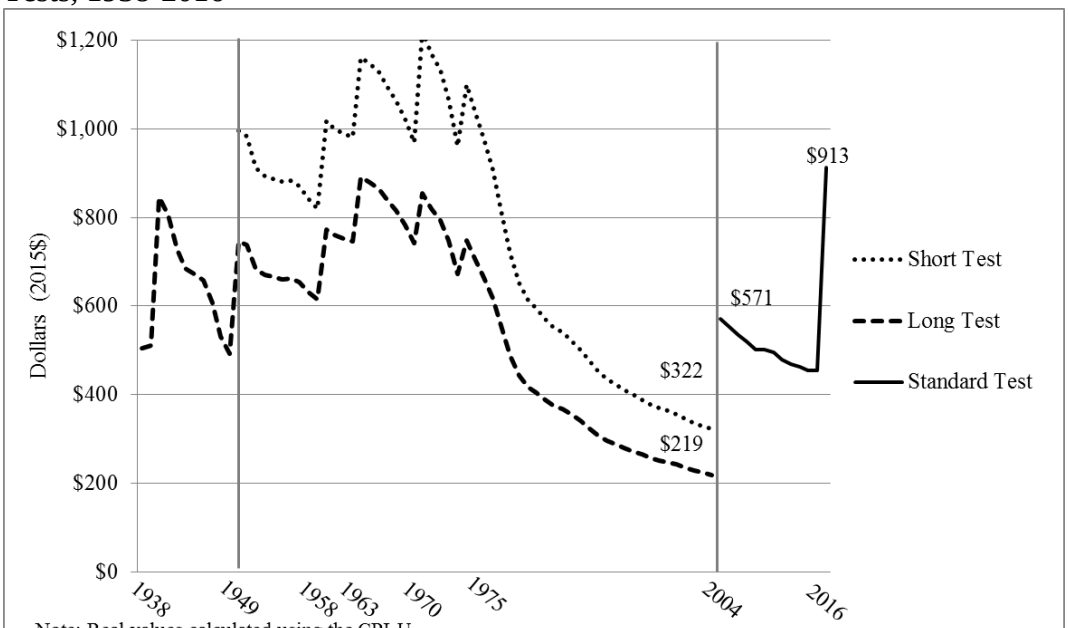
Table 1: Historical Salary Levels for the EAP Exemptions

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			

In 2004, the Department set the standard salary level at $455 per week. Following more than ten years of inflation, the purchasing power, or real value, of the standard salary level test has eroded substantially, and as a result increasingly more workers earn above the salary threshold. Between 2004 and 2015, the real value of the standard salary level declined 20.3 percent, calculated using the Consumer Price Index for all urban consumers (CPI-U).[88] The decline is even larger when comparing the salary level in 2015 with 1975 levels. Figure 1 demonstrates how the real values of the salary levels have changed since 1938, measured in 2015 dollars. The Final Rule's standard salary level is below the real value of the short test salary level in all previous years when it was updated.

[87] From 1949 until 2004 the regulations contained two different tests for exemption—a long duties test for employees paid a lower salary, and a short duties test for employees paid at a higher salary level.
[88] CPI-U data available at: http://data.bls.gov/cgi-bin/cpicalc.pl.

Figure 1: Real Values of the Salary Level Tests using the Long, Short, and Standard Duties Tests, 1938-2016



Note: Real values calculated using the CPI-U.
Note: For the long test, if executive, administrative, and professional have different levels then the highest level is used. If the level was altered during the calendar year, then the updated level is reported.

As a result of the erosion of the real value of the standard salary level, more and more workers lack the clear protection the salary level test is meant to provide. Each year that the salary level is not updated, its utility as a distinguishing mechanism between exempt and nonexempt workers declines. The Department has revised the levels just once in the 41 years since 1975. In contrast, in the 37 years between 1938 and 1975, salary test levels were increased approximately every five to nine years. In our 2004 rulemaking, the Department stated the intention to "update the salary levels on a more regular basis, as it did prior to 1975," and added that the "salary levels should be adjusted when wage survey data and other policy concerns support such a change." 69 FR 22171. Now, in order to restore the value of the standard salary level as a line of demarcation between those workers for whom Congress intended to provide minimum wage and overtime protections and those workers who may be performing bona fide EAP duties, and to maintain its continued validity, in this Final Rule the Department is setting the standard salary

level equal to the 40th percentile of weekly earnings of all full-time salaried workers in the lowest-wage Census Region. The Department determined the "lowest-wage Census Region" by examining Current Population Survey (CPS) data for each Census Region to find the region having the lowest salary amount at the 40th percentile of weekly earnings of full-time salaried workers, which currently is the South.[89] Based on the fourth quarter of 2015 CPS data, the 40th percentile for the South Census Region is $913 per week. To bring the HCE annual compensation requirement in line with the level established in 2004, the Department, in this Final Rule, is setting the HCE total annual compensation level at the 90th percentile of annualized weekly earnings of full-time salaried workers nationally. Based on the fourth quarter of 2015 CPS data, the HCE compensation level is $134,004 annually.

In addition, this Final Rule has introduced a mechanism to automatically update the standard salary and HCE total annual compensation levels every three years, with the first update taking effect on January 1, 2020. This triennial automatic updating will preserve the effectiveness of the salary level as a dividing line between nonexempt workers and workers who may be exempt, eliminate the volatility associated with previous changes in the thresholds, and increase certainty for employers with respect to future changes. It will also simplify the updating process, as the Department will simply publish a notice in the Federal Register with the updated salary and compensation thresholds at least 150 days in advance of the update, and post the updated salary and compensation levels on the Wage and Hour Division (WHD) website. Should the Department determine in the future that changes in the updating methodology may be warranted, the Department can engage in notice and comment rulemaking.

[89] For simplicity, in this rulemaking we refer to the lowest-wage Census Region and the South interchangeably.

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. To produce these estimates, the Department used data from the CPS, a monthly survey of 60,000 households conducted by the U.S. Census Bureau. Many of the data variables used in this analysis are from the CPS's Merged Outgoing Rotation Group (MORG) data. The impacts calculated by the Department in this analysis are based on FY2013-FY2015 data projected to reflect FY2017. The Department used the same data available to the public to analyze the impact of this Final Rule.[90] Data for FY2015 were the most recently available at the time of writing.[91] However, the Department pooled three years of data in order to increase the sample size. Additionally, because the rulemaking will take effect December 1, 2016, the Department has projected the data to represent FY2017 as Year 1 (the fiscal year most similar to the first year of implementation).

Some commenters, such as the United States Chamber of Commerce (Chamber), National Retail Federation (NRF), and the Florida Department of Economic Opportunity (FL DEO), expressed concern that the estimated impacts in the Preliminary Regulatory Impact Analysis (PRIA) are not replicable. To the extent that these commenters suggested that the entire PRIA was based on non-public data, the Department emphasizes that we used the non-publicly available data only for determining percentiles of the earnings distribution. As we noted in the NPRM, the public will not be able to precisely recreate the salary amounts in the published deciles because to ensure the confidentiality of survey respondents, the data in BLS public-use files use adjusted weights and therefore minor discrepancies between internal BLS files and

[90] To ensure the confidentiality of survey respondents, data in the public-use files use adjusted weights and top-coded earnings.
[91] FY2015 includes October 1, 2014 through September 30, 2015.

public-use files exist. See 80 FR 38528 n.24. Some commenters also asserted that the methodology used in the PRIA to estimate the impact of this rulemaking could not be replicated because the Department did not sufficiently explain our analysis. The Department believes that the analytic methodology was thoroughly described throughout the NPRM, PRIA and Appendix A, 80 FR 38545-601. Nevertheless, we have provided additional details in this RIA to address concerns about replicability.

The Department estimates that in FY2017, there will be 44.8 million white collar salaried employees who do not qualify for any other FLSA exemption and therefore may be affected by a change to the Department's part 541 regulations (Table 7). Of these workers, the Department estimates that 29.9 million would be exempt from the minimum wage and overtime pay provisions under the part 541 EAP exemptions (in the baseline scenario without the rule taking effect). The other 14.9 million workers do not satisfy the duties tests for EAP exemption and/or earn less than $455 per week (Table 7).[92] However, of the 29.9 million EAP-exempt workers, 7.4 million are in "named occupations" and thus need only pass the duties tests to be subject to the standard EAP exemptions.[93] Therefore, these workers are not considered in the analysis, leaving 22.5 million EAP-exempt workers potentially affected by this Final Rule.

In Year 1, an estimated 4.2 million workers will be affected by the increase in the standard salary level test (Table 2). This figure consists of currently EAP-exempt workers subject to the salary level test who earn at least $455 per week but less than the 40th percentile of full-time salaried workers in the South ($913). Additionally, an estimated 65,000 workers will be affected

[92] 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 total or the calculation shown due to rounding of components.

[93] Workers not subject to the EAP salary level test include teachers, academic administrative personnel, physicians, lawyers, judges, and outside sales workers.

by the increase in the HCE compensation test.[94] Finally, 732,000 white collar, salaried workers making between $455 and $913 who do not meet the duties test are already overtime eligible but do not receive overtime pay because they are misclassified. While these workers are not "affected" by the Final Rule because their entitlement to overtime will not change, as a result of the change in the salary level their exemption status will be clear based on the salary test alone and they will no longer be misclassified due to misapplication of the duties test. In Year 10, with automatic updating,[95] 5.0 million workers are projected to be affected by the change in the standard salary level test and 217,000 workers will be affected by the change in the HCE total annual compensation test.

Three direct costs to employers are quantified in this analysis: (1) regulatory familiarization costs; (2) adjustment costs; and (3) managerial costs. Regulatory familiarization costs are the costs incurred to read and become familiar with the requirements of the rule. Adjustment costs are the costs accrued to determine workers' new exemption statuses, notify employees of policy changes, and update payroll systems. Managerial costs associated with this Final Rule occur because hours of workers who are newly entitled to overtime may be more closely scheduled and monitored to minimize or avoid overtime hours worked.

The costs presented here are the combined costs for both the change in the standard salary level test and the HCE annual compensation level (these will be disaggregated in section

[94] In later years, earnings growth will cause some workers to no longer be affected in those years because their earnings will exceed the 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. In order to estimate the total number of affected workers over time, the Department accounts for both of these effects. Thus, in Year 2, an estimated 4.0 million workers will be affected, and by Year 10, an estimated 5.3 million workers will be affected.

[95] Future automatic updates to the standard salary and HCE compensation level requirements will occur in Years 4, 7, and 10.

VI.D.iii.). Total average annualized direct employer costs over the first 10 years are estimated to be $295.1 million, assuming a 7 percent discount rate; hereafter, unless otherwise specified, average annualized values will be presented using the 7 percent real discount rate (Table 2). Deadweight loss (DWL) is also a cost but not a direct employer cost. DWL is a function of the difference between the wage employers are willing to pay for the hours lost, and the wage workers are willing to take for those hours. In other words, DWL represents the decrease in total economic surplus in the market arising from the change in the regulation. The Department estimates average annualized DWL to be $9.2 million.[96]

In addition to the costs described above, this Final Rule will also transfer income from employers to employees in the form of wages. The Department estimates average annualized transfers will be $1,189.1 million. The majority of these transfers are attributable to the FLSA's overtime provision; a far smaller share is attributable to the FLSA's minimum wage requirement. Transfers also include additional pay to increase the salaries of some affected EAP workers who remain exempt.

Employers may incur additional costs, such as hiring new workers. These other potential costs are discussed in section VI.D.iii. Benefits of this Final Rule are discussed in section VI.D.vii.

Table 2: Summary of Regulatory Costs and Transfers, Standard and HCE Salary Levels (Millions 2017$)

Impact	Year 1	Future Years [a]	Average Annualized Value

[96] The estimate of DWL assumes the market meets the theoretical conditions for an efficient market in the absence of this intervention (e.g., all conditions of a perfectly competitive market hold: full information, no barriers to entry, etc.). Since labor markets are generally not perfectly competitive, this is likely an overestimate of the DWL.

		Year 2	Year 10	3% Real Rate	7% Real Rate
Affected Workers (1,000s)					
Standard	4,163	3,893	5,045	--	--
HCE	65	73	217	--	--
Total	4,228	3,965	5,261	--	--
Costs and Transfers (Millions 2017$) [b]					
Direct employer costs	$677.9	$208.0	$284.2	$288.0	$295.1
Transfers [c]	$1,285.2	$936.5	$1,607.2	$1,201.6	$1,189.1
DWL	$6.4	$8.7	$11.1	$9.3	$9.2

[a] These costs/transfers 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 that we primarily describe as being from employers to workers. There may also be transfers of hours and income from some workers to others. Moreover, some of these transfers may be intrapersonal, for instance, higher earnings may be offset by increased hours worked for employees who remain overtime-exempt or may be supplemented by reduced hours for some newly overtime-protected employees.

iv. Terminology and Abbreviations

The following terminology and abbreviations will be used throughout this RIA.

Affected EAP workers: 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 the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (currently the South) ($913 in Year 1), or pass only the HCE duties test and earn at least $100,000 but less than the annualized earnings of the 90th percentile of full-time salaried workers nationally ($134,004 in Year 1). This is estimated to be 4.2 million workers.[97]

[97] Setting the standard salary level at the 40th percentile of weekly earnings of full-time salaried workers in the South is estimated to affect 4,163,000 workers. See Table 2. The estimate is based on the effect of the change in overtime protection under the FLSA from this Final Rule. It includes workers who may currently be overtime-eligible under more protective state EAP laws and regulations, such as some workers in Alaska, California, and New York. Additionally,

Baseline EAP exempt workers: The projected number of workers who would be EAP exempt in FY2017 if the rulemaking did not take effect.

BLS: Bureau of Labor Statistics.

CPI-U: Consumer Price Index for all urban consumers.

CPS: Current Population Survey.

Duties test: To be exempt from the FLSA's minimum wage and overtime requirements under section 13(a)(1), the employee's primary job duty must involve bona fide executive, administrative, or professional duties as defined by the regulations. The Department distinguishes among four such tests:

Standard duties test: The duties test 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, but its criteria closely follow those of the former short test.

HCE duties test: The duties test 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.

Long duties test: One of two duties tests used from 1949 until 2004; this more restrictive duties test had a greater number of requirements, including a limit on the amount of

---

65,000 workers are potentially affected by the change in the HCE exemption's total compensation level. Id. Accordingly, throughout this RIA we refer to the total affected workers as 4.2 million (4,163,000 + 65,000, rounded to the nearest 100,000 workers).

nonexempt work that could be performed, and was used in conjunction with a lower salary level to determine eligibility for the EAP exemptions (see Table 1).

Short duties test: One of two duties tests used from 1949 to 2004; this less restrictive duties test had fewer requirements, did not limit the amount of nonexempt work that could be performed, and was used in conjunction with a higher salary level to determine eligibility for the EAP exemptions (see Table 1).

DWL: Deadweight loss; the loss of economic efficiency that can occur when the perfectly competitive equilibrium in a market for a good or service is not achieved.

EAP: Executive, administrative, and professional.

FY: Fiscal year. The federal fiscal year is from October 1 through September 30.

HCE: Highly compensated employee; a category of EAP exempt employee, established in 2004 and characterized by high earnings and a minimal duties test.

Hourly wage: For the purpose of this RIA, the amount an employee is paid for an hour of work.

Base hourly wage: The hourly wage excluding any overtime payments. Also used to express the wage rate without accounting for benefits.

Implicit hourly wage: Hourly wage calculated by dividing reported weekly earnings by reported hours worked.

Straight time wage: Another term for the hourly wage excluding any overtime payments.

MORG: Merged Outgoing Rotation Group supplement to the CPS.

Named occupations: Workers in named occupations are not subject to the salary level or salary basis tests. These occupations include teachers, academic administrative personnel,[98] physicians,[99] lawyers, judges,[100] and outside sales workers.

Overtime workers: The Department distinguishes between two types of overtime workers.

Occasional overtime workers: The Department uses two steps to identify occasional overtime workers. First, all workers who report they usually work 40 hours or less per week (identified with variable PEHRUSL1 in CPS MORG) but in the survey (or reference) week worked more than 40 hours (variable PEHRACT1 in CPS MORG) are classified as occasional overtime workers. Second, some additional workers who do not report usually working overtime and did not report working overtime in the reference week are randomly selected to be classified as occasional overtime workers so that the proportion of workers who work overtime in our sample matches the proportion of workers, measured using SIPP data, who work overtime at some point in the year.

Regular overtime workers: Workers who report they usually work more than 40 hours per week (identified with variable PEHRUSL1 in CPS MORG).

---

[98] Academic administrative personnel (including admissions counselors and academic counselors) need to be paid either (1) the salary level or (2) a salary that is at least equal to the entrance salary for teachers in the educational establishment at which they are employed (see § 541.204). Entrance salaries at the educational establishment of employment cannot be distinguished in the data and so this alternative is not considered (thus these employees were excluded from the analysis, the same as was done in the 2004 Final Rule).

[99] The term physician includes medical doctors including general practitioners and specialists, osteopathic physicians (doctors of osteopathy), podiatrists, dentists (doctors of dental medicine), and optometrists (doctors of optometry or with a Bachelor of Science in optometry). § 541.304(b).

[100] Judges may not be considered "employees" under the FLSA definition. However, since this distinction cannot be made in the data, all judges are excluded (the same as was done in the 2004 Final Rule). Including these workers in the model as FLSA employees would not impact the estimate of affected workers.

Pooled data for FY2013-FY2015: CPS MORG data from FY2013-FY2015 adjusted to represent FY2015 with earnings inflated to FY2017 dollars and sample observations weighted to reflect projected employment in FY2017. Pooled data were used to increase sample size.

Potentially affected EAP workers: EAP exempt workers who are not in named occupations and are included in the analysis (i.e., white collar, salaried, not eligible for another (non-EAP) overtime pay exemption). This is estimated to be 22.5 million workers.

Price elasticity of demand (with respect to wage): The percentage change in labor hours demanded in response to a one percent change in wages.

Real dollars (2017$): Dollars adjusted using the CPI-U to reflect the purchasing power they would have in FY2017.

Salary basis test: The EAP exemptions' requirement that workers be paid on a salary basis, that is, a pre-determined amount that cannot be reduced because of variations in the quality or quantity of the employee's work.

Salary level test: The salary a worker must earn in order to be subject to the EAP exemptions. The Department distinguishes among four such tests:

Standard salary level: The weekly salary level associated with the standard duties test that determines eligibility for the EAP exemptions. The standard salary level was set at $455 per week in the 2004 Final Rule.

HCE compensation level: Workers who meet the standard salary level requirement but not the standard duties test nevertheless are exempt if they pass a minimal duties test and earn at least the HCE total annual compensation required amount. The HCE required compensation level was set at $100,000 per year in the 2004 Final Rule, of which at least $455 per week must be paid on a salary or fee basis.

Short test salary level: The weekly salary level associated with the short duties test (eliminated in 2004).

Long test salary level: The weekly salary level associated with the long duties test (eliminated in 2004).

SIPP: Survey of Income and Program Participation.

Workers covered by the FLSA and subject to the Department's part 541 regulations: Includes all workers except those excluded from the analysis because they are not covered by the FLSA or subject to the Department's requirements. Excluded workers include: members of the military, unpaid volunteers, the self-employed, many religious workers, and federal employees (with a few exceptions).[101]

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

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 EAP exemptions. 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.[102] The methodology described here is

[101] Employees of firms with annual revenue less than $500,000 who are not engaged in interstate commerce are also not covered by the FLSA. However, these workers are not excluded from this analysis because the Department has no reliable way of estimating the size of this worker population, although the Department believes it composes a small percent of workers. These workers were also not excluded from the 2004 Final Rule.

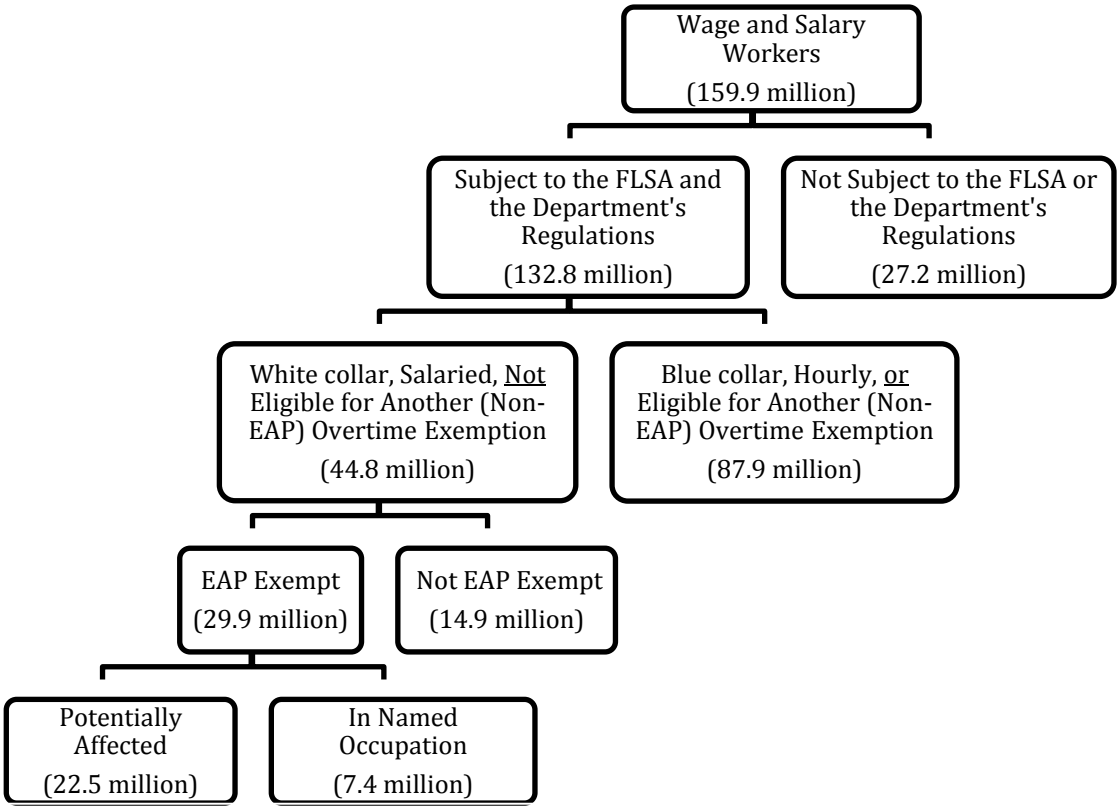
[102] RAND recently released results from a survey conducted to estimate EAP exempt workers. However, this survey does not have the variables or sample size necessary for the Department to

largely based on the approach the Department used in the 2004 Final Rule. 69 FR 22196-209. All tables include projected estimates for FY2017, which begins on October 1, 2016. Some tables also include estimates for FY2005 (the first full fiscal year after the most recent increase to the salary level was implemented) to demonstrate how the prevalence of the EAP exemption has changed in the 12 years since our last rulemaking. We note that the PRIA used calendar year 2005 whereas this Final Rule uses FY2005. Therefore, the numbers have changed slightly. Figure 2 illustrates how the U.S. civilian workforce was analyzed through successive stages to estimate the number of potentially affected EAP workers.

---

base the RIA on this analysis. These survey results were submitted by the authors as a comment on the proposed rule. 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.

Figure 2: Flow Chart of FLSA Exemptions and Estimated Number of Potentially Affected Workers, Projected for FY2017



ii. Data

The estimates of EAP exempt workers are based on data drawn from the CPS MORG, which is sponsored jointly by the U.S. Census Bureau and the 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.[103] This supplement contains the detailed information on earnings necessary to

[103] 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.

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 is a large scale survey, administered to 60,000 households 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 (FY2013 through FY2015). Earnings for each FY2013 and FY2014 observation were inflated to FY2015 dollars using the CPI-U, and 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 FY2015 CPS MORG. Thus, the pooled CPS MORG sample uses roughly three times as many observations to represent the same total number of workers in FY2015. The additional observations allow the Department to better estimate certain attributes of the potentially affected labor force.

Next, this pooled sample was adjusted to reflect the FY2017 economy by further inflating wages and sampling weights to project to FY2017. The Department applied two years of wage growth based on the average annual growth rate in median wages. The wage growth rate is calculated as the geometric growth rate in median wages using the historical CPS MORG data for occupation-industry categories from FY2006 to FY2014.[104,105] The geometric growth rate is

[104] In order to maximize the number of observations used in calculating the median wage for each occupation-industry category, three years of data were pooled for each of the endpoint years. Specifically, data from FY2005, FY2006, and FY2007 (converted to FY2006 dollars) were used to calculate the FY2006 median wage and data from FY2013, FY2014, and FY2015 (converted to FY2014 dollars) were used to calculate the FY2014 median wage.

[105] In the NPRM only wage growth rates for exempt workers were used; therefore, growth was based on historical wage growth for exempt workers. Since the Final Rule projects all workers' earnings for Year 1, wage growth was estimated for all workers based on the historical growth

the constant annual 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. This method only depends on the value of the wage in the first available year and the last available year.[106]

The geometric wage growth rate was also calculated from the BLS' Occupational Employment Statistics (OES) survey and used as a validity check.[107] Additionally, 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 the OES data.[108] 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.

The employment growth rate is the geometric annual growth rate based on the ten-year employment projection from BLS' National Employment Matrix (NEM) for 2014 to 2024 within an occupation-industry category. An alternative method is to spread the total change in the level of employment over the ten years evenly across years (constant change in the number

---

rate for all workers. Additionally, for the Final Rule, the Department projected earnings prior to determining which workers are exempt, necessitating a change in the methodology.

[106] The geometric mean may be a flawed measure if either or both of those years were atypical; however, in this instance these values seem typical. An alternative method would be to use the time series of median wage data to estimate the linear trend in the values and continue this to project future median wages. This method may be preferred if either or both of the endpoint years are outliers, since the trend will be less influenced by them. However, the linear trend may be flawed if there are outliers in the interim years. The Department chose to use the geometric mean because individual year fluctuations are difficult to predict and applying the geometric growth rate to each year provides a better estimate of the long-term growth in wages.

[107] The OES growth measure compared median wages in the 2006 and the 2014 OES by industry-occupation combination. The difference between the OES and CPS growth measures averaged 0.00173 percentage points, but varied by up to 15.4 percentage points, depending on the occupation-industry category.

[108] To lessen small sample bias in the estimation of the median growth rate, this rate was only calculated using CPS MORG data when these data contained at least 10 observations in each time period.

employed). The Department believes that on average employment is more likely to grow at a constant percentage rate rather than by a constant level (a decreasing percentage rate). To account for employment growth, the Department applied the growth rates to the sample weights of the workers. This is because the Department cannot introduce new observations to the CPS MORG data to represent the newly employed.

In addition to the calculations described above, some assumptions had to be made 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 impacts 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).[109] 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.[110]

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 protected by the FLSA or are not

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

[110] 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 5.7 percent. To the extent these excluded workers are exempt, if they tend to work more overtime than other workers, then transfer payments, costs, and DWL may be underestimated. Conversely, if they work fewer overtime hours, then transfer payments, costs, and DWL may be overestimated.

subject to the Department's regulations for a variety of reasons—for instance, they may not be covered by, or considered to be employees under, the FLSA. These 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: members of the military on active duty, unpaid volunteers, and the self-employed. Religious workers were excluded from the analysis after being 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 are not subject to the Department's part 541 regulations because their entitlement to minimum wage and overtime pay is regulated by the Office of Personnel Management (OPM).[111] See 29 U.S.C. 204(f). Exceptions exist for U.S. Postal Service employees, Tennessee Valley Authority employees, and Library of Congress employees. See 29 U.S.C. 203(e)(2)(A). These covered federal workers were identified and included in the analysis using occupation and/or industry codes.[112] Employees of firms that have annual revenue of less than $500,000 and who are not engaged in interstate commerce are also not covered by the FLSA. The Department does not

[111] Federal workers are identified in the CPS MORG with the class of worker variable PEIO1COW.

[112] 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 D.C.

exclude them from the analysis because we have no reliable way of estimating 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.

Table 3 presents the Department's estimates of the total number of workers, and the number of workers covered by the FLSA and subject to the Department's part 541 regulations, in FY2005 and FY2017. The Department projected that in FY2017 there will be 159.9 million wage and salary workers in the United States. Of these, in the baseline scenario without changes in the salary levels, 132.8 million would be covered by the FLSA and subject to the Department's regulations (83.0 percent). The remaining 27.2 million workers would be excluded from FLSA coverage for the reasons described above and delineated in Table 4.

Table 3: Estimated Number of Workers Covered by the FLSA and Subject to the Department's Part 541 Regulations, FY2005 and FY2017

Year	Civilian Employment (1,000s)	Subject to the Department's Regulations	
		Number (1,000s)	Percent
FY2005[a]	141,519	122,043	86.2%
FY2017	159,914	132,754 [b]	83.0%

[a] The PRIA provided figures from calendar year 2005, which differ slightly from the fiscal year 2005 figures provided in this analysis.
[b] Estimate uses pooled data for FY2013-FY2015 projected to reflect FY2017.

Table 4: Reason Not Subject to the Department's Part 541 Regulations, FY2017

Reason	Number (1,000s)
Total	27,160
Self-employed and unpaid workers [a]	23,607
Religious workers	550
Federal employees [b]	3,005

Note: Estimates use pooled data for FY2013-FY2015 projected to reflect FY2017.
[a] Self-employed workers (both incorporated and unincorporated) and workers "without pay" are excluded from the MORG supplement. We assume workers "without pay" are "unpaid volunteers." These workers are identified as the difference between the population of workers in the CPS basic data and the CPS MORG data.
[b] Most employees of the federal government are covered by the FLSA but are not covered by part 541. Exceptions are for U.S. Postal Service employees, Tennessee Valley Authority employees, and Library of Congress employees.

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 are identified and excluded from further analysis since they are unlikely to be affected by this Final Rule. These include:

- blue collar workers,
- workers paid hourly, and
- workers who are exempt under certain other (non-EAP) exemptions.

The Department excludes a total of 87.9 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). In FY2017, we project there will be 48.1 million blue collar workers (Table 5). 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[113] and the Department's 2004 regulatory impact analysis. See 69 FR 22240-44 (Table A-1). Supervisors in traditionally blue collar industries are classified as white collar workers because their duties are generally managerial or administrative, and therefore they were not excluded as blue collar workers. The Department used the CPS MORG variable PEERNHRY to determine hourly status, and determined that 78.3 million workers will be paid on an hourly basis in FY 2017.

[113] GAO/HEHS. (1999). Fair Labor Standards Act: White Collar Exemptions in the Modern Work Place. GAO/HEHS-99-164, 40-41.

Also excluded from further analysis were workers who are exempt under certain other (non-EAP) exemptions. Although some of these workers may also be exempt under the EAP exemptions, even if these workers lost their EAP exempt status they would remain exempt from the minimum wage and/or overtime pay provisions based on the non-EAP exemption, and thus were excluded from the analysis. We excluded an estimated 4.5 million workers, including some agricultural and transportation workers, from further analysis because they will be subject to another (non-EAP) overtime exemption. See Appendix A: Methodology for Estimating Exemption Status, for details on how this population was identified.

Table 5: Estimated Number of Workers Covered by the FLSA and Subject to the Department's part 541 Regulations, FY2005 and FY2017 (1,000s)

Year	Subject to DOL's Part 541 Reg.	Workers in the Analysis [a]	Excluded from Analysis	Reason Excluded [b]				
				Blue Collar Workers	Hourly Workers	Another Exemption [c]		
						Agri-culture	Trans-portation	Other
FY2005	122,043	39,447	82,595	45,889	73,813	778	1,911	967
FY2017	132,754	44,845	87,909	48,119	78,310	902	1,912	1,691

Note: FY2017 estimates use pooled data for FY2013-FY2015 projected to reflect FY2017.
[a] Wage and salary workers who are white collar, salaried, and not eligible for another (non-EAP) overtime exemption.
[b] Numbers do not add to total due to overlap.
[c] Eligible for another (non-EAP) overtime pay exemption.

In the 2004 Final Rule the Department excluded some of these workers from the population of potentially affected EAP workers, but not all of them. Agricultural and transportation workers are two of the largest groups of workers excluded from this analysis, and they were similarly excluded in 2004. Agricultural workers were identified by occupational-industry combination.[114]

[114] In the 2004 Final Rule all workers in agricultural industries were excluded. 69 FR 22197. Here only workers also in select occupations were excluded since not all workers in agricultural industries qualify for the agricultural overtime pay exemptions. See Appendix A. This method

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). This methodology is the same as in the 2004 Final Rule and is explained in Appendix A. The Department excluded 902,000 agricultural workers and 1.9 million transportation workers from the analysis. In addition, the Department excluded another 1.7 million workers who fall within one or more of multiple FLSA minimum wage and overtime exemptions and are detailed in Appendix A. However, of these 1.7 million workers, all but 25,600 are either blue collar or hourly and thus the impact 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 would be 44.8 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);[115,116]

---

better approximates the true number of exempt agricultural workers and provides a more conservative—i.e., greater—estimate of the number of affected workers.

[115] 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.

[116] Additionally, administrative and professional employees may be paid on a fee basis, as opposed to a salary basis, at a rate of at least the amount specified by the Department in the regulations. Payment on a "fee basis" occurs where an employee is paid an agreed sum for a

- earn at least a designated salary amount; the salary level has been set at $455 per week since 2004 (the salary level test); and
- perform work activities that primarily involve executive, administrative, or professional duties as defined by the regulations (the duties test).

The 2004 Final Rule's HCE test requires the employee to pass the same standard salary basis and salary level tests. However, the HCE duties test is much less restrictive than the standard duties test, and the employee must earn at least $100,000 in total annual compensation, including at least $455 per week paid on a salary or fee basis, while the balance may be paid as nondiscretionary bonuses and commissions.

Salary Basis

As discussed above, the Department included only nonhourly workers in the analysis using the CPS variable PEERNHRY, which identifies workers as either hourly or nonhourly. 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. The Department notes that we made the same assumption regarding nonhourly workers in the 2004 Final Rule. See 69 FR 22197. Several commenters asserted that the Department's use of the CPS variable PEERNHRY to indicate whether a worker is salaried is inappropriate. For example, the NRF included an analysis it commissioned from Oxford Economics, which stated that this variable is inappropriate because all workers who earn under $455 a week (and are

---

single job regardless of the time required for its completion. § 541.605(a). Salary level test compliance for fee basis employees is assessed by determining whether the hourly rate for work performed (i.e., the fee payment divided by the number of hours worked) would total at least $455 per week if the employee worked 40 hours. § 541.605(b). However, the CPS MORG does not identify workers paid on a fee basis (only hourly or nonhourly). Thus in the analysis, workers paid on a fee basis are considered with nonhourly workers and consequently classified as "salaried" (as was done in the 2004 Final Rule).

therefore nonexempt) will report that they are "paid at an hourly rate." The Department believes this is an entirely unwarranted assumption: exempt status is not a prerequisite for being salaried; salaried status is a prerequisite for being exempt (the salary basis test). Millions of workers—white and blue collar alike—are salaried despite being nonexempt, including 3.2 million white-collar workers who reported earning less than $455 per week in the CPS. See 80 FR 38522 (noting the "widespread misconception[]" that "payment of a salary automatically disqualifies an employee from entitlement to overtime compensation.")

Some commenters, such as the Chamber and the National Association of Convenience Stores (NACS), expressed concern that the Department is using "nonhourly" workers to approximate "salaried" workers, even though this may include workers who are paid on a piece-rate, a day-rate, or largely on bonuses or commissions. 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 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 our regulations, and the commenters did not identify any such source.

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.[117] The Fisher & Phillips law

[117] The CPS MORG variable PRERNWA, which measures weekly earnings, is used to identify weekly salary. The CPS variable includes all nondiscretionary bonuses and commissions, which do not count toward the standard salary level under the current regulations but may be used to

firm, Jackson Lewis law firm, NACS, and the Clearing House Association (Clearing House) commented that CPS earnings data may be inappropriate because the data includes overtime pay, commissions, or 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. Lastly, the Department believes that commissions make up a relatively small share of earnings among nonhourly employees.[118] In any event, as discussed earlier in section IV.C., the Department has adopted a change to the salary basis test in this Final Rule that will newly allow employers to satisfy as much as 10 percent of the standard salary level requirement for employees who meet the standard duties test through the payment of nondiscretionary bonuses, incentive payments, and commissions.

NACS also asserted that the CPS MORG earnings data are unreliable because they "are self-reported and are therefore not subject to verification." The Department acknowledges that the CPS, like all surveys, involves some measurement error. However, based on the literature

---

satisfy up to 10 percent of the new standard salary level when this Final Rule takes effect. This discrepancy between the earnings variable used and the FLSA definition of salary may cause a slight overestimate of the number of workers estimated to meet the standard test. Additionally, because the variable includes earnings across all jobs, this could bias upward workers' earnings on a given job. However, the Department believes this bias is small because only 4.2 percent of salaried, white collar workers hold multiple jobs.

[118] In the PSID, relatively few nonhourly workers were paid by commission. Additionally, according to the BLS Employment Cost Index (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: http://www.bls.gov/opub/mlr/cwc/the-effect-of-incentive-pay-on-rates-of-change-in-wages-and-salaries.pdf.

measuring error in CPS earnings data, the Department believes that measurement error should not significantly bias its results.[119]

Duties

The CPS MORG data do not capture information about job duties, and at the time of writing the NPRM, there were no data available on the prevalence of EAP exempt workers. Due to this data limitation, 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 was the best available data and methodology. 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's representatives were uniquely qualified to provide the analysis. The analysis was used in both the GAO's 1999 white collar exemptions report[120] and the Department's 2004 regulatory impact analysis. See 69 FR 22198.

WHD's representatives 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's representatives determined that 251 occupational codes likely included EAP exempt workers and assigned one of four probability codes reflecting the estimated likelihood, expressed as ranges,

---

[119] For example, researchers have found that worker and employer reported earnings correlate 0.90 percent or higher. Bound, J., Brown, C., Mathiowetz, N. Measurement error in survey data. In Handbook of Econometrics; Heckman, J.J., Leamer, E.E., Eds.; North-Holland: Amsterdam, The Netherlands, V, 3705-3843.

[120] GAO/HEHS. (1999). Fair Labor Standards Act: White Collar Exemptions in the Modern Work Place. GAO/HEHS-99-164, 40-41.

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 our analysis of the provisions of the highly compensated test relative to the standard duties test (Table 6). To illustrate, WHD representatives 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 and 10 percent likelihood of meeting the standard EAP duties test. However, if that worker earns at least $100,000 annually, he or she has a 15 percent probability of passing the shorter HCE duties test.

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). Therefore, for this Final Rule, the Department used an occupational crosswalk to map the previous occupational codes to the 2002 Census occupational codes which are used in the CPS MORG 2002 through 2010 data, and to the 2010 Census occupational codes which are used in the CPS MORG FY2013 through FY2015 data.[121] 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 6: 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%

[121] References to occupational codes in this analysis refer to the 2002 Census occupational codes. Crosswalks and methodology available at: http://www.census.gov/people/io/methodology/.

2	50%	90%	94%	96%
3	10%	50%	58.4%	60%
4	0%	10%	15%	15%

These codes provide information on the likelihood 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 adhered to by both the Department in the 2004 Final Rule and the GAO in its 1999 Report.[122] 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.[123] 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.

[122] 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.

[123] 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).

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.[124] However, which particular workers are designated as exempt may vary with each set of ten random draws. For details see Appendix A.

The Chamber attached to its comment an Oxford Economic analysis commissioned by the NRF, which also submitted the analysis, asserting that that CPS data may not be appropriate to determine how many workers are EAP exempt, and specifically how many pass the duties test. The Oxford Economics analysis contends that occupational titles in the CPS are less accurate than the OES survey, a BLS-published data set based on employer surveys, because the occupational titles in the CPS are self-reported, while occupational titles in the OES survey are reported by firms, and are therefore better suited to obtain information on actual occupations. Oxford Economics asserts in their Appendix A that there is title-inflation in the CPS data, which would imply that the Department's number of affected workers was overestimated. Similarly, the Chamber described the CPS job title information as based on "brief, limited individual verbal responses."

The Department acknowledges that an establishment survey (like the OES) may more accurately reflect the occupational titles applied to workers by individual employers; however, we note that businesses, like workers, may also have an incentive to inflate or deflate occupational titles. In addition, Oxford Economics and the Chamber overstate the presumed weaknesses of the CPS occupation classification. When the CPS reports occupation codes,

[124] 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.

occupation is generally determined from the initial, in-person, in-depth interview with the respondent, and the interviewer is directed to determine the respondent's duties and responsibilities, not merely accept the occupational title at face value; Census coders then assign the occupation code based on the interview.

Moreover, there are important shortcomings of the OES, which made it an inappropriate data source for the Department's purposes. First, the OES data do not include individual level data. For example, earnings are not disaggregated by respondent; only select decile estimates are presented. This does not allow estimation of the number of workers earning at least $455.[125] Second, the OES does not provide information on hours worked. In order to estimate costs and transfers using OES data, Oxford Economics had to apply estimates of hours worked from the CPS data to the OES data. This requires mapping CPS occupational titles to OES occupational titles, and therefore does not avoid use of the titles Oxford Economics finds inadequate. The Department believes the direct information on earnings and hours worked from CPS is more germane to the analysis than some potential inaccuracy in occupational titles, and will result in a more accurate analysis than trying to map worker characteristics such as data on hours worked by earnings from CPS to the OES. Finally, even if there are slight discrepancies in occupational titles, a review of the occupational titles in Appendix A of this RIA will show that closely related occupational titles are generally assigned the same probability of exemption (for example, different types of engineers are all classified as probability code 1; and cashiers and counter and rental clerks are both classified as probability code 4).

[125] Oxford Economics made assumptions to estimate the number of workers earning at least $455 per week. The firm chose to include or exclude all workers in an occupation based on whether "the threshold wage was below the 10th percentile or above the 90th percentile respectively." See Appendix A: Detailed Methodology Description, at 32, available at https://nrf.com/sites/default/files/Documents/retail%20library/Rethinking-Overtime-Appendices.pdf.

The Chamber expressed concern that the probability codes used to determine the share of workers in an occupation who are EAP exempt are 17 years old and therefore out of date. Similarly, the Economic Policy Institute (EPI) commented that we underestimated the number of exempt workers for this reason. The Department acknowledges these codes were developed in 1998 for use by the GAO in its study of the part 541 exemptions, but we believe the probability codes continue to accurately estimate exemption status given the fact that the standard duties test is not substantively different from the former short duties tests reflected in the codes.[126] The Department looked at O*NET[127] to determine the extent to which the 1998 probability codes reflected occupational duties today. The Department's review of O*NET verified the continued appropriateness of the 1998 probability codes.

The Partnership to Protect Workplace Opportunity (PPWO) cited an Edgeworth Economics article asserting that the probability codes are inappropriate because there is evidence that the relationship between salaries and job duties assumed by the Department is not valid. The article provides the following example: "the median pay of 'Occupational Therapists' is more than twice as high as the median pay of 'First Line Supervisors/Managers of Retail Sales Workers,' yet the DOL places 'Occupational Therapists' in the 10 to 50 percent category for managerial and professional duties, while 50 to 90 percent of the positions in 'First Line Supervisors/Managers of Retail Sales Workers' were determined to include managerial and professional duties." However, this criticism is not valid since the positive relationship between

[126] The Chamber additionally expressed concern about the use of proxy respondents in the CPS. To check whether proxy respondents may cause biased results, the Department excluded proxy responses from the data and found that the share of potentially affected workers who are affected by the rulemaking remains very similar (it drops from 18.8 percent (see section VI.D.ii.) to 18.1 percent).

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

salary levels and passing the duties test was assumed within probability code categories, not between probability code categories. The probability codes only reflect the likelihood within an occupation of passing the duties test, not the probability of being exempt.

Potentially Affected Exempt EAP Workers

The Department estimated that of the 44.8 million salaried white collar workers considered in the analysis, 29.9 million qualified for the EAP exemptions under the current regulations (Table 7). However, some of these workers were excluded from further analysis because they would not be affected by the Final Rule. 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 is not dependent 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).[128] Out of the 29.9 million workers who are EAP exempt, 7.4 million, or 24.8 percent, are expected to be in named occupations in FY2017. Thus these workers will be unaffected by changes in the standard salary level and HCE compensation tests. The 22.5 million EAP exempt workers remaining in the analysis are referred to in this Final Rule as "potentially affected." In addition to the 22.5 million potentially affected EAP exempt workers, the Department estimates that an additional 5.7 million salaried white collar workers who do not satisfy the duties test and who currently earn at least $455 per week but less than the

[128] Some commenters asserted it is inappropriate to exclude these named occupations from the impact analysis, but not from the data set used to derive the salary level. These workers were included in the earnings distribution used to set the salary level because it achieves a sample that is more representative of EAP salary levels throughout the economy (see section IV.A.iv.).

updated salary level, will have their overtime protection strengthened because their exemption status will be clear based on the salary test alone without the need to examine their duties.

Table 7: Estimated Percentages of EAP Exempt Workers in Named Occupations, Prior to Rulemaking, FY2005 and FY2017

Year	Workers in the Analysis (Millions) [a]	EAP Exempt (Millions)	EAP Exempt in Named Occupations (Millions) [b]	% of EAP Exempt in Named Occupations
FY2005	39.4	24.9	6.4	25.9%
FY2017	44.8	29.9	7.4	24.8%

Note: FY2017 estimates use pooled data for FY2013-FY2015 projected to reflect FY2017.
[a] Wage and salary workers who are white collar, salaried, and not eligible for another (non-EAP) overtime exemption.
[b] Workers not subject to a salary level test include teachers, academic administrative personnel, physicians, lawyers, judges, and outside sales workers.

In response to the NPRM, the FL DEO conducted their own analysis of the number of Florida workers potentially affected by the proposed rule and asserted that the Department's analysis in the NPRM overestimates "by 195,000 the number of Florida workers who will qualify for overtime." The Department's NPRM estimated that 370,000 workers would be affected in Florida whereas the FL DEO estimated 175,100.[129] However, FL DEO did not provide details explaining how they arrived at their lower number so the Department has no way to judge the validity of their analysis or to update our own analysis to incorporate any methodological improvements that may exist in the FL DEO study.

There are three groups of workers who qualify for the EAP exemptions: (1) those passing only the standard EAP test (i.e., passing the standard duties test, the salary basis test, and the standard salary level test but not passing the HCE total annual compensation requirement); (2) those

[129] State level data was not included in the NPRM analysis, but was posted at the time of the NPRM publication and is available at: https://www.whitehouse.gov/sites/default/files/docs/ot_state_by_state_fact_sheet.pdf.

passing only the HCE test (i.e., passing the HCE duties test, the salary basis test, and the HCE total annual compensation requirement but not passing the standard duties test); and (3) those passing all requirements of both the standard and HCE tests. Based on analysis of the occupational codes and CPS earnings data, the Department has concluded that in FY2017, in the baseline scenario where the rule does not change, of the 22.5 million potentially affected EAP workers, approximately 15.4 million will pass only the standard EAP test, 7.0 million will pass both the standard and the HCE tests, and approximately 100,000 will pass only the HCE test (Table 8). When impacts are discussed in section VI.D., workers who pass both tests will be considered with those who pass only the standard EAP test because the standard salary level test is lower (i.e., the worker may continue to pass the standard salary level test even if he or she no longer passes the HCE total annual compensation requirement).

Table 8: Estimated Number of Workers Exempt under the EAP Exemptions by Test Type, Prior to Rulemaking, FY2005 and FY2017

Year	Potentially Affected EAP Workers (Millions)			
	Total	Pass Standard Test Only	Pass Both Tests	Pass HCE Test Only
FY2005	18.4	15.8	2.6	0.04
FY2017	22.5	15.4	7.0	0.10

Note: FY2017 estimates use pooled data for FY2013-FY2015 projected to reflect FY2017.

C. Determining the Revised Salary and Compensation Levels

The Final Rule sets the EAP standard salary level at the 40th percentile of the weekly earnings distribution of full-time salaried workers in the lowest-wage Census Region (currently the South) and sets the HCE total annual compensation requirement equal to the annual earnings equivalent of the 90th percentile of the weekly earnings distribution of full-time salaried workers

nationally.[130] These methods were chosen in part because they generate salary levels that (1) appropriately distinguish between workers who are eligible for overtime and those who may be EAP exempt; (2) are easy to calculate and thus easy to replicate, creating transparency through simplicity; and (3) are predictable. The Department believes that the standard salary level set using the methodology established in this rulemaking allows for reliance on the current standard duties test without necessitating a return to the more detailed long duties test. Additionally, the Department believes this salary level will not result in an unacceptably high risk that employees performing bona fide EAP duties will become entitled to overtime protection by virtue of the salary test.

In the NPRM, the Department proposed setting the EAP standard salary level at the 40th percentile of the weekly earnings distribution of full-time salaried workers nationally. In response to commenters' concerns that the proposed salary level would disqualify too many bona fide EAP employees in low-wage areas and industries, the Department limited the distribution to workers in the lowest-wage Census Region.

i. Methodology for the Standard Salary Level and Comparison to Past Methodologies

The Department in this rulemaking is setting the standard salary level at the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (currently the South). This methodology differs somewhat from previous revisions to the salary levels but the general concept holds: define a relevant population of workers, estimate an earnings distribution for that population, then set a salary level that corresponds to a designated percentile of that distribution in order for the salary to serve as a meaningful line of demarcation between those

[130] On a quarterly basis, BLS publishes a table of deciles of the weekly wages of full-time nonhourly workers, calculated using CPS data, which employers can use to help anticipate the likely amount of automatically updated salary levels. See http://www.bls.gov/cps/research_series_earnings_nonhourly_workers.htm.

Congress intended to protect and those who may qualify for exemption. The salary setting methodology adopted in this Final Rule continues the evolution of the Department's approach. Where the methodology differs from past methodologies, the Department believes the changes are an improvement. A comparison of this new method with methods from past rulemakings, and the reasons for selecting the new method are detailed in the rest of this section.

As discussed in section IV.A., the historical methodologies used to revise the EAP salary levels have varied somewhat across the seven updates to the salary level test since it was implemented in 1938. To guide the determination of the salary level, the Department considered methodologies used previously to revise the EAP salary levels. In particular, the Department focused on the 1958 revisions and the most recent revisions in 2004. The 1958 methodology is particularly instructive in that it synthesized previous approaches to setting the long-test salary level, and the basic structures it adopted have been a touchstone to setting the long test salary level in subsequent rulemakings (with the exception of 1975).

In 1958, the Department updated the salary levels based on a 1958 Report and Recommendations on Proposed Revision of Regulations, Part 541, by Harry S. Kantor (Kantor Report). To determine the revised salary levels the Department looked at data collected during WHD investigations on actual salaries paid to exempt EAP employees, grouped by geographic region, industry groups, number of employees, and size of city. The Department then set the long test salary levels so that no more than about 10 percent of exempt EAP employees in the lowest-wage region, lowest-wage industry, smallest establishment group, or smallest city group would fail to meet the test. Kantor Report at 6-7.[131,132] The Department then set the short test

[131] The Kantor long test method was based on an analysis of a survey of exempt workers as determined by investigations conducted by WHD. Subsequent analyses, including both the 2004 rulemaking and this Final Rule, have estimated exempt status using multiple data sources.

salary level in relation to, and significantly higher than, the long test salary levels. This methodology is referred to as the Kantor method, and the Department followed a similar methodology in setting the salary levels in 1963 and 1970.

A significant change in 2004 from the long test Kantor method was that the Department used the salaries of both exempt and nonexempt full-time salaried workers in the South and the retail industry to determine the required salary level (hereafter referred to as the 2004 method), rather than the salaries of exempt workers only. However, because the salaries of exempt workers on average are higher than the salaries of all full-time salaried workers, the Department selected a higher earnings percentile when setting the required salary. Based on the Department's 2004 analysis, the 20th percentile of earnings for exempt and nonexempt full-time salaried workers in the South and retail achieved a result very similar to the 10th percentile for workers in the lowest-wage regions and industries who were estimated to be exempt. See 69 FR 22169.

In the current rulemaking, the Department replicated the Kantor long test method and the 2004 method to evaluate and compare them to the chosen salary level.[133] Although the Department was able to replicate the 1958 and 2004 methods reasonably well, we could not completely replicate those methods due to changes in data availability, occupation classification systems, and incomplete documentation. In general, there are four steps in the process:

1. Identify workers likely to be members of the population of interest.

---

[132] Because the salary level test is likely to have the largest impact on the low-wage segments of the economy (e.g., low-wage regions and industries), salaries in those segments were selected as the basis for the required salary level under the Kantor long test method.

[133] The Department followed the same methodology used in the 2004 Final Rule for estimating the Kantor long test method with minor adjustments. In an attempt to more accurately estimate the Kantor long test method, for example, this analysis included non-MSAs as a low-wage sector as Kantor did but the 2004 revisions did not.

2. Further narrow the population of interest by distinguishing the sub-population employed in low-wage categories.
3. Estimate the distribution of earnings for these workers.
4. Identify the salary level that is equal to a pre-determined percentile of the distribution.

The population of workers considered for purposes of setting the salary level depends on whether the 2004 method or the Kantor long test method is used. In replicating both methods, the Department limited the population to workers subject to the FLSA and covered by the Department's part 541 provisions, and excluded exempt EAP workers in named occupations, and those exempt under another (non-EAP) exemption. For the 2004 method, the Department further limited the population to full-time salaried workers, and for the Kantor long test method further limited the population of interest by only including those workers determined as likely to be EAP exempt (see more detailed methodology in section VI.C. and Appendix A).

In the 2004 Final Rule, the Department identified two low-wage categories: the South (low-wage geographic region), and the retail industry (low-wage industry). In the current rulemaking, the Department identified low-wage categories by comparing average weekly earnings across categories for the populations of workers used in the Kantor long test method and the 2004 method. The South was determined to be the lowest-wage Census Region and was used for the 2004 method; however, the Department chose to use a more detailed geographical break-down for the Kantor long test method to reflect the geographic categories Kantor used. Therefore, for the Kantor long test method the East South Central Census Division is considered the lowest-wage geographical area.[134] The Department used three low-wage industries: leisure and

[134] The East South Central Division is a subset of the South and includes Alabama, Kentucky, Mississippi, and Tennessee. If the South is used instead, the resulting salary levels would increase slightly.

hospitality, other services, and public administration.[135] The Department also considered non-MSAs as a low-wage sector in the Kantor long test method. The 2004 revision did not consider population density but the Kantor long test method examined earnings across population size groups. In conclusion, for this analysis the 2004 method looks at workers in the South and the three low-wage industries, whereas the Kantor long test method looks at workers in the East South Central Division, non-MSAs, and the three low-wage industries.

Next, the Department estimated the distributions of weekly earnings of two populations: (1) workers who are in at least one of the low-wage categories and in the Kantor population (likely exempt workers), and (2) workers who are in at least one of the low-wage categories and in the 2004 population (full-time salaried workers). From these distributions, alternate salary levels were identified based on pre-determined percentiles. For the Kantor long test method, the salary level for the long duties test is identified based on the 10th percentile of weekly earnings for likely EAP exempt workers, while the 2004 method salary level is identified based on the 20th percentile of weekly earnings for both exempt and nonexempt salaried workers. Using 2015 quarter 3 CPS MORG data, the Kantor long test method resulted in a salary level of $684 per week, and the 2004 method resulted in a salary level of $596 per week.[136] Table 9 presents the distributions of weekly earnings used to estimate the salary levels under the method used in this Final Rule, the NPRM method, the 2004 method, and the Kantor long test method.

---

[135] In the NPRM, the Department found that the industry with the lowest mean weekly earnings depends on whether the Kantor long test method or the 2004 method's population was used. Therefore, three industries were considered low-wage. For the Final Rule, the "other services" industry was consistently the lowest-wage industry. However, the Department continues to use all three low-wage industries for consistency and because these three continue to be the three lowest-wage industries.

[136] Quarter 3 was used instead of quarter 4, which was used for the distribution of all full-time salaried workers, because at the time the analysis was conducted this was the most recently available data.

Table 9: Weekly Earnings Distributions

Percen-tile	Weekly Earnings				Annual Earnings [a]			
	Full-Time Salaried 2015Q4 [b]		2004 Method 2015Q3 [c]	Kantor Long Test Method 2015Q3 [d]	Full-Time Salaried 2015Q4 [b]		2004 Method 2015Q3 [c]	Kantor Long Test Method 2015Q3 [d]
	South	Nationally			South	Nationally		
10	$479	$509	$429	$684	$24,908	$26,468	$22,319	$35,560
20	$633	$692	$596	$817	$32,916	$35,984	$31,015	$42,491
30	$768	$838	$726	$949	$39,936	$43,576	$37,749	$49,332
40	$913	$972	$844	$1,110	$47,476	$50,544	$43,878	$57,739
50	$1,054	$1,146	$988	$1,259	$54,808	$59,592	$51,381	$65,451

[a] Weekly earnings multiplied by 52.
[b] BLS. Available at: http://www.bls.gov/cps/research_series_earnings_nonhourly_workers.htm.
[c] Full-time salaried workers in the South or employed in a low-wage industry (excludes workers not subject to the FLSA, not subject to the salary level test, and in agriculture or transportation). Quarter 3 was used instead of Q4 because at the time of the analysis this was the most recently available data.
[d] Salaried, white collar workers who earn at least $455 per week, pass the EAP duties test, and either live in the East South Central Division or a non-MSA or are employed in a low-wage industry (excludes workers not subject to FLSA, not subject to the salary level test, and in agriculture or transportation). Quarter 3 was used instead of Q4 because at the time of the analysis this was the most recently available data.

In response to the NPRM, the Iowa Association of Business and Industry (IABI) commented that the Department incorrectly replicated the Kantor long test methodology. Kantor determined the salary levels by looking separately at low-wage regions, less populated geographic regions, and low-wage industries and then identifying a single salary level that fits within these salary numbers. IABI asserted that we misapplied the methodology by aggregating these low-wage sectors into a single group. The Department disagrees with IABI that we misapplied the Kantor long-test methodology. As discussed at length in the NPRM, the Department replicated the Kantor methodology as closely as possible given changes in data availability. See 80 FR 38557.

ii. Rationale for the Methodology Chosen

The chosen methodology—the 40th percentile of full-time salaried workers in the lowest-wage Census Region—was selected because it (1) corrects for the elimination of the long duties test and allows for reliance on the current standard duties test; (2) appropriately distinguishes between workers who are eligible for overtime and those who may be EAP exempt in all regions and industries; (3) is easy to calculate and thus easy to replicate, creating transparency through simplicity; and (4) produces predictable salary levels.

The salary level test has historically been intended to serve as an initial bright-line test for overtime eligibility for white collar employees. As discussed previously, however, there will always be white collar overtime-eligible employees who are paid above the salary threshold. A low salary level increases the number of these employees. The necessity of applying the duties test to these overtime-protected employees consumes employer resources, may result in misclassification (which imposes additional costs to employers and society in the form of litigation), and is an indicator of the effectiveness of the salary level. Similarly, there will always be employees performing bona fide EAP duties who are paid below the salary threshold; the inability of employers to claim the EAP exemption for these employees is also an indicator of the effectiveness of the salary level. Selecting the standard salary level will inevitably affect the number of workers falling into each of these two categories.

1. Correcting for the Elimination of the Long Duties Test

The Kantor long test method sought to minimize the number of white collar employees who pass the long duties test but were excluded from the exemption by the salary threshold and therefore set the salary level at the bottom 10 percent of earnings of exempt EAP employees in low-wage regions and industries so as to prevent "disqualifying any substantial number of such

employees." Kantor Report at 5. This method was based on the long/short test structure, in which employees paid at lower salary levels were protected by significantly more rigorous duties requirements than are part of the current standard duties test. This approach, however, does not sufficiently take into account the inefficiencies of applying the duties test to large numbers of overtime-eligible white collar employees and the possibility of misclassification of those employees as exempt.

As discussed in section IV.A., for many decades the long duties test—which limited the amount of time an exempt employee could spend on nonexempt duties and was paired with a lower salary level—existed in tandem with a short duties test—which did not contain a specific limit on the amount of nonexempt work and was paired with a significantly higher salary level. In 2004, the Department eliminated the long and short duties tests and created the new standard duties test, based on the short duties test. The creation of a single standard test that did not limit nonexempt work caused new uncertainty as to what salary level is sufficient to ensure that employees intended to be overtime-protected are not subject to inappropriate classification as exempt, while minimizing the number of employees disqualified from the exemption even though their primary duty is EAP exempt work.

In the Final Rule, the Department corrects for the elimination of the long duties test and sets a salary level that works in tandem with the standard duties test to appropriately classify white collar workers as entitled to minimum wage and overtime protection or potentially exempt. Thus, while the standard salary level set by the Department is higher than the level the Kantor long test or 2004 methods would generate, it is set at the low end of the range of the historical short test levels, based on the ratios between the short test and long test levels, and much lower than the historical average for the short test. Between 1949 and 2003, the ratio of the short to

long salary tests ranged from approximately 130 percent to 180 percent. The low end of this range would result in a salary level of $889; the high end would result in a salary of $1,231 (measured in FY2015 dollars). The short salary level updates between 1949 and 2003 averaged $1,100 per week (measured in FY2015 dollars).[137] At the 40th percentile of weekly earnings of full-time workers in the South, 9.9 million white collar employees would no longer be subject to the standard duties test (4.2 million currently EAP exempt employees who would be newly entitled to overtime protection due to the increase in the salary threshold and 5.7 million overtime eligible white collar employees who are paid between $455 and $913 per week whose exemption status would no longer depend on the application of the duties test). As discussed in section IV.A.iv., the Department believes that many of the workers who will no longer be exempt are currently inappropriately classified because of the mismatch between the standard duties test and the standard salary level. The final salary threshold will therefore more efficiently distinguish between employees who may meet the duties requirement of the EAP exemption and those who do not, without necessitating a return to the more detailed long duties test.

2. Appropriately Distinguishing Overtime-Eligible White Collar Workers and Those Who May Be EAP Exempt

The revised salary level also 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. In the NPRM, the Department estimated that 13.5 percent of overtime-eligible white collar workers earning between the current salary level and the proposed salary level were misclassified. 80 FR 38559.

The Department updated our estimate of potential misclassification based on the salary level set in this Final Rule. The Department's analysis of misclassification draws on CPS data and

[137] This is the average of the values of the short test salary level inflated to 2015 dollars.

looked at workers who are white collar, salaried, subject to the FLSA and covered by part 541 regulations, earn at least $455 but less than $913 per week, 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.[138] Workers were considered misclassified if they did not receive overtime pay.[139] The Department estimates that 12.8 percent of workers in this analysis who usually work overtime do 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 $913, the Department estimates that there are approximately 732,000 white collar salaried workers earning at least $455 but less than $913 who are overtime-eligible but whose employers do not recognize them as such.[140] These employees' entitlement to overtime pay will now be abundantly evident.

Table 10 provides estimates of the extent of misclassification of workers as exempt among first-line supervisors/managers in a variety of industries using the same method of looking at white collar salaried employees who fail the duties test and who report working more than 40 hours a week but do not report receiving overtime compensation.[141] The Department's analysis found that 41 percent of first-line supervisors/managers of food preparation and serving workers, and 35 percent of first-line supervisors/managers of retail sales workers are misclassified.

---

[138] We have excluded workers who are in named occupations or are exempt under another non-EAP exemption.

[139] 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).

[140] 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.

[141] The occupational category of first-line supervisors and managers illustrates the concept across a range of industries. This category of workers may be susceptible to potential misclassification because they are the first level of management above overtime-protected line workers.

The Department also found that the industries with the largest number of workers who fail the duties test and report working more than 40 hours a week but do not receive overtime compensation are retail trade (125,000 workers) and food services and drinking places (97,000 workers). In these industries, the Department estimates the rate of misclassification to be 41percent of food services and drinking workers and 18 percent of retail workers.

Table 10: Estimates of Misclassification among First-Line Supervisors and Managers Covered by the Final Rule Who Earn at Least $455 and Less than $913

First-Line Supervisors/Manager Occupations	Overtime Eligible Salaried Workers who Earn between $455 and $913 per Week (1,000s)	Percent who Usually Work >40 Hours [a]	Percent Misclassified [b]
Total	5,697	15.0%	12.8%
First-line supervisors/managers of…			
Retail sales workers	208.5	39.9%	34.6%
Non-retail sales workers	66.0	32.6%	27.5%
Production and operating workers	62.4	26.3%	24.0%
Construction trades and extraction workers	58.5	19.9%	19.0%
Food preparation and serving workers	55.5	44.9%	41.0%
Housekeeping and janitorial workers	35.0	22.0%	17.2%
Mechanics, installers, and repairers	28.9	29.2%	27.6%
Office and administrative support workers	26.9	14.0%	13.1%
Personal service workers	21.0	31.5%	24.3%
Landscaping, lawn service, and grounds keeping workers	17.4	29.3%	26.0%

Source: CPS extract. Workers who are white collar, salaried, subject to the FLSA and covered by the part 541 regulations, earn at least $455 but less than $913 per week, and fail the duties test.

[a] Percent of overtime eligible salaried workers who usually work more than 40 hours per week. This differs from the 40 percent of all workers who work more than 40 hours in a week at least once per year because it only includes overtime eligible workers and excludes occasional overtime workers.

[b] Share of respondents who report usually working more than 40 hours per week and do not report that they "usually receive overtime pay, tips, or commissions."

Since the NPRM was published, 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) 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[142] found "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), at the new salary level, the Department estimates that approximately 1.8 million salaried workers earning between $455 and $913 per week who fail the standard duties test are currently misclassified as exempt.[143]

The Department also assessed the impact of the standard salary level as a bright-line test for EAP exemption by examining: (1) the number of salaried white collar workers who pass the standard salary level test but not the duties test and (2) the number of salaried white collar workers who pass the standard duties test but not the salary level test.[144] This first group is equivalent to the number of salaried white collar workers who are eligible for overtime pay because they do not pass the standard EAP duties test, but earn above a specific salary level. The

[142] 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.

[143] 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.

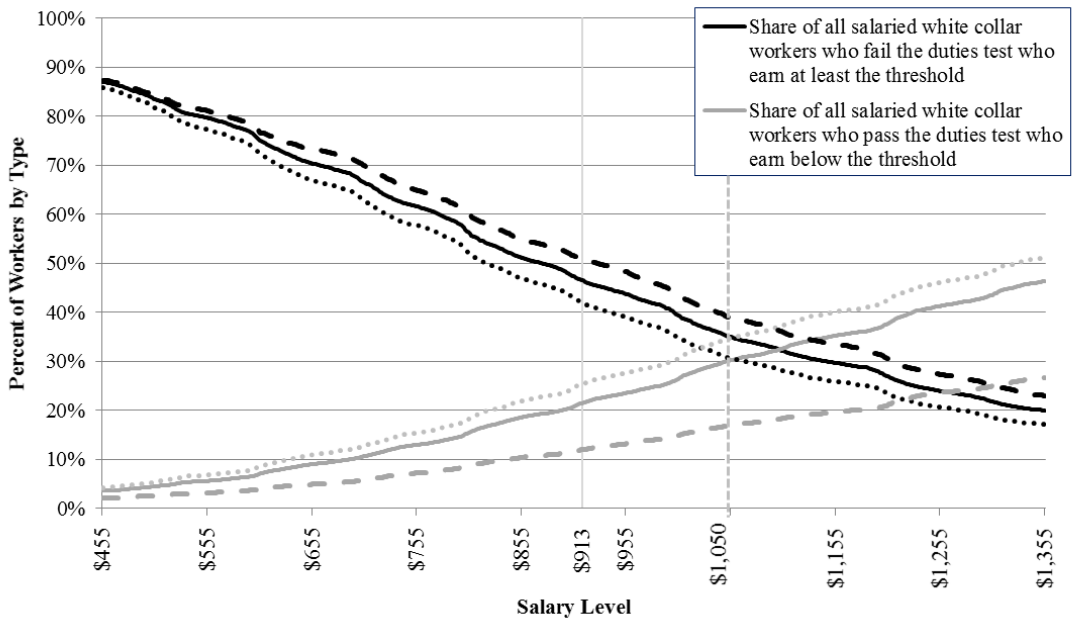
[144] These populations are limited to salaried, white collar workers subject to the FLSA and the Department's part 541 regulations, and not eligible for another (non-EAP) exemption, not in a named occupation, and not HCE only.

second group is the number of salaried white collar workers who satisfy the standard duties test but earn less than a specific standard salary level. The Department makes this assessment at the current salary level ($455) and the final salary level ($913), while holding all other factors determining exempt status constant (e.g., not considering whether the duties test is correctly applied or potential employer response to the change in the salary level test). Examining the impact of the salary threshold in isolation from the application of the duties test or employer adjustments to pay or hours does not provide a complete picture of the impact of a new salary threshold. It does, however, allow the Department to evaluate the effectiveness of the salary level in protecting overtime-eligible white collar employees without unduly excluding from the exemption employees performing EAP duties.

As a benchmark, the Department estimates that at the current standard salary threshold, there are 12.2 million salaried white collar workers who fail the standard duties test and are therefore overtime eligible, but earn at least the $455 threshold, while there are only 838,000 salaried white collar workers who pass the standard duties test but earn less than the $455 level. Thus the number of salaried white collar workers who pass the current salary threshold test but not the duties test is nearly 15 times the number of salaried white collar workers who pass the duties test but are paid below the salary threshold. This underscores the large number of overtime-eligible workers for whom employers must perform a duties analysis, and who may be at risk of misclassification as EAP exempt. At a salary threshold equal to the 40th percentile of full-time salaried workers in the South ($913), the number of overtime-eligible salaried white collar workers who would earn at least the threshold but do not pass the duties test would be reduced almost in half to 6.5 million (approximately 47 percent of all white collar salaried employees who fail the duties test). At a salary level of $913, the number of salaried white collar workers

who would pass the standard duties test but earn less than the salary level would increase to 5.0 million (approximately 22 percent of all white collar salaried employees who pass the standard duties test). While this number is higher than the number of such employees under the Kantor long test method (approximately 10 percent), it includes employees who would have been overtime-eligible because they would not have passed the more rigorous long duties test, which had a cap on the percentage of time an employee could spend on nonexempt duties, and therefore were not included under that approach. Further, the number of salaried white collar workers who pass the new salary threshold test but not the duties test (6.5 million) is 31 percent higher than the number of salaried white collar workers who pass the duties test but are paid below the salary threshold (5.0 million).

Figure 3: Percentage of White Collar Salaried Workers by Earnings and Duties Test Status for National, Highest-Wage, and Lowest –Wage Regions



Note: Solid lines are for the national level. Striped lines are for the highest-wage Region (West) and dotted lines are for the lowest-wage Region (South). Vertical lines indicate the salary levels using the South and the West ($1,050).

As illustrated in Figure 3, as the salary threshold increases there is a decrease in the share of overtime-eligible white collar workers for whom employers would be required to make an assessment under the duties test and who would be subject to possible misclassification (descending lines). At the same time, as the salary level increases there is an increase in the share of salaried white collar workers who pass the standard duties test but are screened from exemption by the salary threshold (ascending lines).[145] As previously discussed, the increase in the share from the traditional 10 percent of exempt employees excluded by the Kantor long test

[145] Of employees who are paid on a salary basis of at least $455 per week and meet the standard duties test, approximately 81 percent earn at least the new level of $913 per week. Conversely, among overtime-eligible salaried white collar employees earning at least $455 per week, approximately 47 percent earn less than the new salary level.

method reflects the shift to a salary level appropriate to the standard duties test. Because the long duties test included a limit on the amount of nonexempt work that could be performed, it could be paired with a low salary that excluded few employees performing EAP duties. In the absences of such a limitation in the duties test, it is necessary to set the salary level higher (resulting in the exclusion of more employees performing EAP duties) because the salary level must perform more of the screening function previously performed by the long duties test.

At the current salary level (far left of Figure 3), there is a very large gap between salaried white collar workers who are overtime eligible but earn at least the threshold (about 87 percent of all salaried white collar workers who fail the duties test are paid at least $455 per week) and salaried white collar workers who pass the standard duties test but do not meet the current salary level (about 4 percent of all salaried white collar workers who pass the duties test are paid less than $455 per week). At the salary level of the 40th percentile of weekly earnings of full-time salaried workers in the South ($913 per week), the percentage of overtime-eligible salaried white collar workers who earn above the threshold (and thus would be at risk of misclassification) still remains higher than the percentage of salaried white collar workers who pass the duties test but earn less than the salary threshold (and would become overtime protected).[146] The salary threshold would have to be considerably higher (at a weekly salary level of approximately $1,100) before the percentage of salaried white collar workers who earn less than the threshold but pass the duties test would equal the percentage who are overtime eligible but earn at least the salary threshold. While some commenters favored setting the salary level at this intersection

[146] Approximately 47 percent of white collar salaried workers who do not pass the duties test earn at least the new salary level ($913 per week). Conversely, approximately 22 percent of employees who pass the standard duties test earn less than the new salary level.

point, the Department concludes that the resulting salary level would unduly impact low-wage regions and industries.

The Department has also looked at the impact of the new salary level on these two groups of workers in low-wage (East South Central) and high-wage (Pacific) Census divisions in addition to nationally.[147] For the East South Central Census division, the salary level at which the percentages of the two groups are about equal is approximately $995 per week, while in the Pacific Census division, the salary at which the percentages of the two groups are equal is approximately $1,217 per week. The Department's new salary level of the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region ($913 per week) falls below the estimate for the East South Central division. This further supports that the Department's change in the Final Rule to the lowest-wage Census Region establishes a salary level that is appropriate for classifying workers as entitled to minimum wage and overtime pay or potentially exempt in even the lowest wage areas.

3. Simplicity and Transparency

The method of basing the standard salary threshold on a particular percentile of weekly earnings of full-time salaried employees in the lowest-wage Census Region involves less estimation than previous updates, making it easier to implement, less prone to error, and more transparent than before. The method reduces computation by simplifying the classification of workers to just two criteria: wage or salaried, and full-time or part-time. Application of the Kantor long test method, in particular, would involve significant work to replicate since one would need to identify likely EAP exempt workers, a process which requires applying the

[147] Of the nine Census divisions, the East South Central and Pacific divisions correspond to the divisions with the lowest and highest earnings using the Kantor long test method. The East South Central includes Alabama, Kentucky, Mississippi, and Tennessee. The Pacific includes Alaska, California, Hawaii, Oregon, and Washington.

standard duties test to determine the population of workers used in the earnings distribution. In addition, both the Kantor long test and 2004 methods exclude workers not subject to the FLSA, not subject to the salary level test, or in agriculture or transportation. The method adopted in this Final Rule is easier for stakeholders to replicate and understand because the standard duties test does not need to be applied to determine the population of workers used in the earnings distribution.

International Foodservice Distributors Association, IABI, and others criticized the Department for not restricting the CPS sample to workers subject to the part 541 regulations or subject to the salary level test. As explained in section IV.A.iv., the Department believes these white collar professionals are part of the universe of executive, administrative, and professional employees who Congress intended to exempt from the FLSA's minimum wage and overtime requirements and including them in the data set achieves a sample that is more representative of EAP salary levels throughout the economy.

4. Consistency and Predictability

A method that produces very different salary levels in consecutive years may reduce confidence that the salary levels in any given year are optimal. The growth rate using the Kantor long test method varies across years. The primary reason for this is because the Kantor long test method—or any other method that limits the data set to currently exempt workers—uses the value of the current salary level test to identify the population of workers from which the earnings distribution is determined. Therefore, the Kantor long test method limits the pool of workers in the sample used to set the salary level to those who meet the currently required salary level, while the 2004 method and the new method implemented in this Final Rule do not exclude workers with salaries below the current salary level. Since FY2004, the salary levels that would

have been generated by the Kantor method increased by 3.6 percent on average annually.[148] Conversely, since FY2004, the 40th percentile of earnings of full-time salaried workers in the South has increased by an average of 2.4 percent annually. Similarly, the salary levels that would have been generated by the 2004 method (keeping low-wage sectors constant) increased 2.5 percent annually on average. This explains why the salary levels generated by the Kantor long test method and the 2004 method have diverged significantly since 2004 (in the third quarter of 2015, Kantor = $684; 2004 = $596).

For example, in 2003 the Kantor long test method's population of interest was limited to workers earning at least $155 per week (the 1975 long test salary level); in this Final Rule the Kantor long test method's population was restricted to workers earning at least $455 per week. Therefore the population considered in the Kantor long test method changes each time the salary level is changed. The Department's Final Rule, like the 2004 method, considers all full-time salaried workers and does not limit the pool to only those workers who meet the current salary level test, thus avoiding this potential shortcoming of the Kantor long test method.

iii. Standard Salary Levels with Alternative Methodologies

When assessing the standard salary level, the Department evaluated several alternatives in addition to the level chosen. This section presents the alternative salary levels considered and the bases for identifying those alternative levels. While commenters proposed other methods for calculating the salary level, the Department determined that these alternatives remained the best comparators for evaluating the chosen salary level methodology. As shown in Table 11, the alternative salary levels evaluated are:

[148] Values calculated using geometric growth rates and starting in FY2004, the last time the salary level was increased.

- Alternative 1: Inflate the 2004 weekly salary level to FY2015 dollars, which results in a salary level of $570 per week.
- Alternative 2: Use the 2004 method to set the salary level at $596 per week.
- Alternative 3: Use the Kantor long test level of $684 per week.
- Alternative 4: Use the 40th earnings percentile of full-time salaried workers nationally. This was the methodology proposed in the NPRM. This results in a salary level of $972 per week.
- Alternative 5: Adjust the salary level from the Kantor long test method to reflect the average historical ratio between the long and short test salary levels. This results in a salary level of $1,019 per week.
- Alternative 6: Inflate the 1975 short duties test salary level, which is $1,100 in FY2015 dollars.

Table 11: Standard Salary Level and Alternatives, FY2017

Alternative	Salary Level (Weekly/Annually)	Total Increase [a]	
		$	%
Alt. #1: Inflate 2004 level [b]	$570 / $29,640	$115	25.3%
Alt. #2: 2004 method [c]	$596 / $31,015	$141	31.1%
Alt. #3: Kantor long test [c]	$684 / $35,568	$229	50.3%
Final Rule method (40th percentile of full-time salaried workers in lowest-wage Census Region)	$913 / $47,476	$458	100.7%
Alt. #4: 40th percentile of full-time salaried workers nationally	$972 / $50,544	$517	113.6%
Alt. #5: Kantor short test [c]	$1,019 / $52,984	$564	123.9%
Alt. #6: Inflate 1975 short test level [b]	$1,100 / $57,205	$645	141.8%

[a] Change between salary level or alternative and the salary level set in 2004 ($455 per week).
[b] Value in FY2015$. Inflated using CPI-U to FY2015$ (most recent data available).
[c] Data for 2015, quarter 3.

Alternative 1 inflates the 2004 standard salary level ($455) to FY2015 dollars using the CPI-U. This produces a salary level of $570 per week. As noted above, the 2004 method sets the standard salary level at approximately the 20th percentile of full-time salaried workers in the South and retail industry. Alternative 2 applies this methodology to more recent data (quarter 3 of 2015), resulting in a salary level of $596 per week. Alternative 3 produces the salary level using the Kantor method for the long duties test, resulting in a level of $684 per week.
As we explain earlier in the preamble, the Department rejected the use of these alternatives because they pair a salary level appropriate for use with the long duties test with a duties test appropriate for use with the short test salary.

Alternative 4 sets the standard salary equal to the 40th percentile of weekly earnings of all full-time salaried workers nationally. This is the approach that the Department proposed in the NPRM. This alternative uses the same methodology as this Final Rule—setting the salary level at the 40th percentile of earnings—but uses a data set including full-time salaried workers nationwide instead of limiting the population to the lowest-wage Census Region. The 40th percentile of earnings of all full-time salaried workers nationally, in the fourth quarter of 2015, is $972. As discussed in more detail in section IV.A.iv., the Department declined to adopt this method in response to commenters' concerns that the proposed salary level could disproportionately impact workers in low-wage regions and industries by inappropriately excluding from exemption too many workers who meet the duties test.

Alternative 5 (Kantor short test) is also based on the Kantor method but, whereas alternative 3 generates the salary level associated with the long duties test, alternative 5 generates a level more closely resembling the salary associated with the short duties test, which the Department set as a function of the Kantor long test. In the 2004 Final Rule, the Department replaced the structure of

separate short and long duties tests with a single standard duties test based on the less restrictive short duties test, which had historically been paired with a higher salary level test. However, the Department set the standard salary level in 2004 at a level that was equivalent to the Kantor long test salary level, which was associated with the long duties test and limited the amount of nonexempt work that the employee could perform. In alternative 5, the Department therefore considered revising the standard salary level to approximate the short test salary that better matches the standard duties test. On average, the salary levels set in 1949 through 1975 were 149 percent higher for the short test than the long test. Therefore, the Department inflated the Kantor estimate of $684 by 149 percent, which generated a short salary level equivalent of $1,019 per week.[149] While the Department used the average difference between the Kantor short and long tests for this alternative, the ratio of the short to long salary tests ranged from approximately 130 percent to 180 percent between 1949 and 2004. The low end of this range would result in a weekly salary of $889; the high end would result in a salary of $1,231. The Department rejected the use of the Kantor short test, as explained in this preamble, because we concluded that a standard salary level of $1,019 per week might exclude from exemption too many bona fide EAP workers in certain regions or industries.

Alternative 6 inflates the 1975 short duties test salary level to $1,100 per week in FY2015 dollars. Similar to alternative 5, the Department rejected the use of a short test salary level due to the concern that it might exclude from exemption too many bona fide EAP workers in certain regions or industries.

[149] The Department estimated the average historic ratio of 149 percent as the simple average of the fifteen historical ratios of the short duties salary level to the long duties salary level (salary levels were set in 5 years and in each year the salary level varied between the three exemptions: executive, administrative, and professional). If the Department had weighted the average ratio based on the length of time the historic salary levels were in effect, this would have yielded an average historic ratio of 152 percent and a salary level of $1,039.

Section VI.D. details the transfers, costs, and benefits of the new salary level and the above alternatives. A comparison of the costs and benefits supports the Department's decision to set the standard salary level of the 40th percentile of weekly earnings of all full-time salaried workers in the South ($913 per week).

iv. Methodology for the HCE Total Annual Compensation Level and Alternative Methods

The Department sets the HCE compensation level equal to the annual equivalent of the 90th percentile of the distribution of earnings of all full-time salaried workers nationally. BLS calculated the salary level from the CPS MORG data by limiting the population to nonhourly workers who work full-time (i.e., at least 35 hours per week) and determining the 90th percentile of the resulting weighted weekly earnings distribution. The 90th percentile of weekly earnings in the fourth quarter of 2015 was $2,577. This was then multiplied by 52 to determine the annual earnings equivalent ($134,004). This method uses a percentile towards the top of the nationwide earnings distribution to reflect the minimal duties criteria associated with the highly compensated employee exemption.

The Department also evaluated the following alternative HCE compensation levels:

- HCE alternative 1: Leave the HCE compensation level unchanged at $100,000 per year.
- HCE alternative 2: Inflate the 2004 level using CPI-U to $125,320 per year in FY2015 dollars.
- HCE alternative 3: Set the HCE compensation level at $149,894 per year, which is approximately the annualized level of weekly earnings exceeded by 6.3 percent of full-time salaried workers. This is the same percent of such workers that exceeded the HCE compensation level in 2004. See 69 FR 22169.

The Department continues to believe that HCE alternative 1 is inappropriate because leaving the HCE compensation level unchanged at $100,000 per year would ignore more than 10 years of wage growth. In FY2017, approximately 20 percent of full-time salaried workers are projected to earn at least $100,000 annually, more than three times the share who earned that amount in the 2004 Final Rule analysis. HCE alternative 2 uses the CPI-U to inflate the value set in 2004 instead of using the higher wage growth over that time period, and therefore the Department does not believe this alternative accurately reflects wage growth since 2004. Finally, HCE alternative 3 would set the annual compensation level at $149,894. The Department believes this compensation level would be too high to provide a meaningful alternative test for exemption. Thus, the Department concludes that adjusting the HCE total annual compensation to reflect the 90th percentile of earnings of full-time salaried workers nationwide ($134,004) strikes the appropriate balance.

D. Impacts of Revised Salary and Compensation Level Test Values

i. Overview and Summary of Quantified Impacts

The impacts 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. For workers who usually work 40 hours a week or less, the Department assumes that employers will reclassify these affected EAP workers as overtime-eligible and will pay them the same weekly earnings for the same number of hours worked. While these employees will become overtime eligible, employers can continue to pay their current salaries and will not need to make any adjustments as long as the employees' hours do not exceed 40 hours in a workweek. For affected EAP employees who work overtime, employers may: (1) pay the required overtime premium for the current number of overtime hours based upon the current implicit regular rate of

pay; (2) reduce or eliminate overtime hours; (3) reduce the regular rate of pay so total weekly earnings and hours do not change after overtime is paid; (4) increase employees' salaries to the new salary level; or (5) use some combination of these responses. Transfers from employers to employees and between employees, direct employer costs, and DWL depend on how employers respond to the Final Rule.

In order to increase the sample size and the reliability and granularity of results in this analysis, the Department used three years (FY2013-FY2015) of CPS MORG data to represent the FY2015 labor market. Monetary values in FY2013 and FY2014 were inflated to FY2015 dollars and the sample was reweighted to reflect the population of potentially affected workers in FY2015. Afterwards, this pooled sample was adjusted to reflect the FY2017 economy by further inflating wages and sampling weights to match projections for FY2017. See section VI.B.ii.

Table 12 presents the projected impact on affected workers, costs, transfers, and DWL associated with increasing the standard EAP salary level from $455 per week to the 40th earnings percentile of full-time salaried workers in the South, $913 per week; increasing the HCE compensation level from $100,000 to the 90th earnings percentile of full-time salaried workers nationally, $134,004 annually; and updating both of these levels triennially. The Department estimated that the direct employer costs of this Final Rule will total $677.9 million in the first year, with average annualized direct costs of $295.1 million per year over 10 years. In addition to these direct costs, this Final Rule will also transfer income from employers to employees. Year 1 transfers will equal $1,285.2 million, with average annualized transfers estimated at $1,189.1 million per year over 10 years. Finally, the 10-year average annualized DWL was estimated to be $9.2 million. Potential employer costs due to reduced profits and

additional hiring were not quantified but are discussed in section VI.D.iii. Benefits were also not quantified but are discussed in section VI.D.vii.

Table 12: Summary of Affected Workers and Regulatory Costs and Transfers, Standard and HCE Salary Levels

Impact [a]	Year 1	Future Years [b]		Average Annualized Value	
		Year 2	Year 10	3% Real Rate	7% Real Rate
Affected Workers (1000s)					
Standard	4,163	3,893	5,045	--	--
HCE	65	73	217	--	--
Total	4,228	3,965	5,261	--	--
Direct Employer Costs (Millions FY2017$)					
Regulatory familiarization [c]	$272.5	$0.0	$23.1	$37.6	$42.4
Adjustment [d]	$191.4	$1.5	$5.9	$25.4	$29.0
Managerial	$214.0	$206.6	$255.1	$225.0	$223.6
Total direct costs [e]	$677.9	$208.0	$284.2	$288.0	$295.1
Transfers from Employers to Workers (Millions FY2017$) [f]					
Due to minimum wage	$34.3	$28.5	$17.8	$23.2	$23.8
Due to overtime pay	$1,250.8	$907.9	$1,589.4	$1,178.5	$1,165.3
Total transfers [e]	$1,285.2	$936.5	$1,607.2	$1,201.6	$1,189.1
DWL (Millions FY2017$) [g]					
DWL	$6.4	$8.7	$11.1	$9.3	$9.2

[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] Regulatory familiarization costs occur only in years when the salary levels are updated (Years 1, 4, 7, and 10).
[d] Adjustment costs occur in all years when there are newly affected workers, including years when the salary level is not updated. Adjustment costs may occur in years without updated salary levels because some workers' projected earnings are estimated using negative earnings growth.
[e] Components may not add to total due to rounding.
[f] This is the net transfer that we primarily describe as being from employers to workers. There may also be transfers between workers. Moreover, some of these transfers may be intrapersonal (for instance, higher earnings may be offset by increased hours worked for employees who remain overtime-exempt or may be supplemented by reduced hours for some newly overtime-protected employees).
[g] DWL was estimated based on the aggregate impact of both the minimum wage and overtime pay provisions. Since the transfer associated with the minimum wage is negligible compared to

the transfer associated with overtime pay, the vast majority of this cost is attributed to the overtime pay provision.

ii. Affected EAP Workers

1. Overview

Costs, transfer payments, DWL, and benefits of this Final Rule depend on the number of affected EAP workers and labor market adjustments made by employers. The Department estimated there were 22.5 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, passed the standard salary level test, the HCE total compensation level test, and the HCE duties test. This number excludes workers in named occupations who are not subject to the salary tests or who qualify for another (non-EAP) exemption.

The Department estimated that increasing the standard salary level from $455 per week to the 40th earnings percentile of all full-time salaried workers in the lowest-wage Census Region (South, $913 per week) would affect 4.2 million workers (i.e., the number of potentially affected workers who earn at least $455 per week but less than $913 per week). These affected workers compose 18.5 percent of potentially affected EAP workers. The Department also estimated that 65,000 workers would be affected by an increase in the HCE compensation level from $100,000 to the annual earnings equivalent of the 90th percentile of full-time workers nationally (the number of potentially affected workers who earn at least $100,000 but less than $134,004 annually and pass the minimal duties test but not the standard duties test, about 0.3 percent of the pool of potentially affected EAP workers). By Year 10 the total number of affected workers is predicted to increase to 5.3 million.

Figure 4: Number of Affected Workers

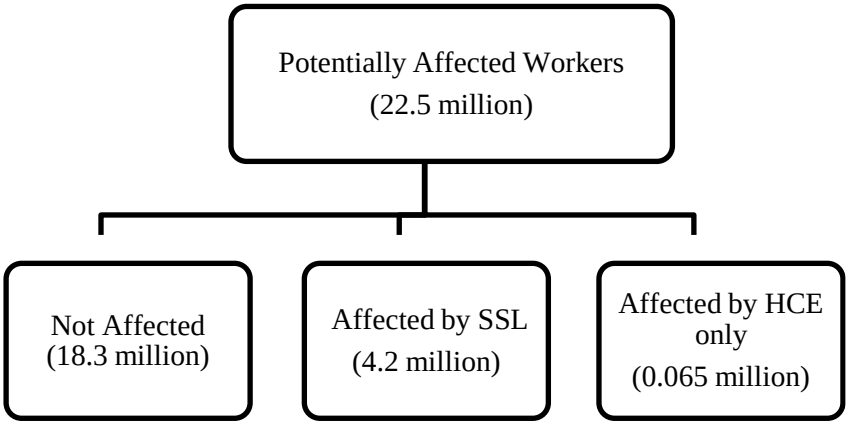


Table 13 presents the number of affected EAP workers, the mean number of overtime hours they work per week, and their average weekly earnings. The 4.2 million workers affected by the increase in the standard salary level average 1.4 hours of overtime per week and earn an average of $734 per week. The average number of overtime hours is low because most of these workers (3.3 million) do not usually work overtime.[150] However, the estimated 825,000 affected workers who regularly work overtime average 11.1 hours of overtime per week. The 65,000 EAP workers affected by the change in the HCE annual compensation level average 5.5 hours of overtime per week and earn an average of $2,181 per week ($113,389 per year).

Although most affected EAP workers who typically do not work overtime might experience little or no change in their daily work routine, those who regularly work overtime may experience significant changes. The Department expects that workers who routinely work some overtime or who earn less than the minimum wage are most likely to be tangibly impacted by the

[150] That is, workers who report they usually work 40 hours or less per week (identified with variable PEHRUSL1 in CPS MORG).

revised standard salary level.[151] Employers might respond by: reclassifying such employees to nonexempt status (either paying at least the hourly minimum wage and a premium for any overtime hours, or its salary equivalent with half-time paid for any overtime hours); reducing workers' regular wage rates (provided that the reduced rates still exceed the minimum wage); increasing the employees' salary to the salary level; reducing or eliminating overtime hours; or using some combination of these responses.

Table 13: Number of Affected EAP Workers, Mean Overtime Hours, and Mean Weekly Earnings, FY2017

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	4,163	100%	1.4	$734
Earn less than the minimum wage [b]	11	0.3%	29.3	$551
Regularly work overtime	825	19.8%	11.1	$744
CPS occasionally work overtime [c]	150	3.6%	8.5	$727
HCE Compensation Level				
All affected EAP workers	65	100%	5.5	$2,181
Earn less than the minimum wage [b]	--	--	--	--
Regularly work overtime	30	45.8%	12.3	$2,153
CPS occasionally work overtime [c]	3	4.2%	8.5	$2,309

Note: Pooled data for FY2013-FY2015 projected to reflect FY2017.
[a] Estimated number of workers exempt under the EAP exemptions who would 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 impacted 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 when we define Type 2 workers.

[151] A small proportion (0.3 percent) of affected EAP workers earns 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 current $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).

The Department considered two types of overtime workers in this analysis: regular overtime workers and occasional overtime workers.[152] 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 considers 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, an estimated 152,000 occasional overtime workers will be affected by either the standard salary level or the HCE total annual compensation level increase (3.6 percent of all affected EAP workers; this number does not match Table 13 due to rounding). They averaged 8.5 hours of overtime in weeks when they work at least some overtime. This group represents the number of workers with occasional overtime hours in the week the CPS MORG survey was conducted. In other weeks, these specific individuals may not work overtime but other workers, who did not work overtime in the survey week, may work overtime. 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).[153]

---

[152] Regular overtime workers were identified in the CPS MORG with variable PEHRUSL1. Occasional overtime workers were identified with variables PEHRUSL1 and PEHRACT1. As described in section VI.D.iv., some workers who are not observed working overtime in the reference week are assumed to be occasional overtime workers. This analysis therefore accounts for workers who work overtime at some point in the year, although they did not work overtime in the reference week.

[153] The Department cannot identify which of the workers in the CPS sample work occasional overtime in a week other than the reference week.

2. Characteristics of Affected EAP Workers

In this section the Department examines the characteristics of affected EAP workers. Table 14 presents the distribution of affected workers across industries and occupations. The industry with the most affected EAP workers was education and health services (956,000 affected workers). Other industries where a large number of workers are expected to be affected are professional and business services (704,000), financial activities (571,000), and wholesale and retail trade (562,000). The industries with the largest share of potentially affected workers who are affected are "other services" (30 percent) and leisure and hospitality (30 percent). Impacts by industry are considered in section VI.D.v.

The management, business, and financial occupation category accounted for the most affected EAP workers by occupation (1.8 million). A large number of workers are expected to be affected in the professional and related occupations category (1.4 million). The occupations with the largest share of potentially affected workers who are expected to be affected are farming, fishing, and forestry (63 percent)[154], office and administrative support (39 percent), and services (37 percent).

Some commenters expressed concern about the impacts of the rule on non-profits organizations. The Department found that workers in non-profits are somewhat more likely to be affected by the rulemaking; 25 percent of potentially affected workers in private non-profits are affected compared to 18 percent in private for-profit firms.

[154] There are only 33,000 potentially affected workers in the farming, fishing, and forestry industry. Although a large share of potentially affected workers may be affected in this industry, many of these workers are exempt under another non-EAP exemption, and therefore their entitlement to overtime will not change.

Table 14: Estimated Number of Exempt Workers with the Current and Updated Salary Levels, by Industry and Occupation, FY2017

Industry / Occupation / Non-profit	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	132.75	22.51	18.29	4.23	19%
By Industry					
Agriculture, forestry, fishing, & hunting	1.12	0.03	0.03	0.01	16%
Mining	1.04	0.23	0.21	0.02	10%
Construction	7.41	0.80	0.67	0.13	16%
Manufacturing	14.82	3.26	2.89	0.36	11%
Wholesale & retail trade	19.03	2.46	1.90	0.56	23%
Transportation & utilities	6.95	0.79	0.65	0.13	17%
Information	2.86	0.95	0.78	0.17	18%
Financial activities	9.21	3.43	2.86	0.57	17%
Professional & business services	14.22	4.64	3.94	0.70	15%
Education & health services	32.95	3.73	2.77	0.96	26%
Leisure & hospitality	12.58	0.78	0.54	0.23	30%
Other services	5.36	0.58	0.40	0.18	30%
Public administration	5.19	0.85	0.65	0.20	24%
By Occupation					
Management, business, & financial	19.18	11.36	9.52	1.84	16%
Professional & related	30.30	7.66	6.31	1.35	18%
Services	23.61	0.20	0.13	0.08	37%
Sales and related	13.72	2.16	1.60	0.56	26%
Office & administrative support	17.82	0.94	0.57	0.37	39%
Farming, fishing, & forestry	0.84	0.00	0.00	0.00	63%
Construction & extraction	6.16	0.03	0.02	0.01	21%
Installation, maintenance, & repair	4.63	0.04	0.03	0.01	15%
Production	8.31	0.08	0.07	0.01	17%
Transportation & material moving	8.20	0.03	0.02	0.01	24%
By Non-profit and Government Status					
Non-profit, private[d]	9.12	1.81	1.35	0.46	25%
For profit, private	105.08	18.80	15.49	3.31	18%
Government (state, local, and federal)	18.55	1.91	1.45	0.46	24%

Note: Pooled data for FY2013-FY2015 projected to reflect FY2017.

[a] 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 would be entitled to overtime protection under the updated salary levels (if their weekly earnings do not increase to the new salary levels).
[d] 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 reliable way of estimating this population. The estimates also do not exclude workers at non-covered enterprises who are not individually covered (because the estimates assume all workers are employed by covered entities). Although not excluding workers who work for non-covered enterprises would only impact a small percentage of workers generally, it may have a larger impact (and result in a larger overestimate) for workers in non-profits because when determining enterprise coverage only revenue derived from business operations, not charitable activities, are included.

Table 15 presents the distribution of affected workers based on Census Regions and divisions, and MSA status. The region with the most affected workers is the South (1.7 million). However, as a share of potentially affected workers in the region, the South is not unduly affected relative to other regions (22 percent are affected compared with 16 to 19 percent in other regions). Impacts by region are considered in section VI.D.v. Although the vast majority of affected EAP workers resided in MSAs (3.8 of 4.2 million, or 89 percent), this largely reflects the fact that 86.7 percent of all workers reside in metropolitan areas.[155]

Employers in low-wage industries, regions, and non-metropolitan areas may perceive a greater impact due to the lower wages and salaries typically paid in those areas and industries. The Department believes the salary level adopted in this Final Rule (which we have adjusted downward from the amount proposed in the NPRM to account for these low-wage areas) is appropriate. In addition, the vast majority of potentially affected workers reside in metropolitan areas and do not work in low-wage industries, and workers in low-wage regions are not unduly affected relative to other regions.

[155] Identified with CPS MORG variable GTMETSTA.

Table 15: Estimated Number of Potentially Affected EAP Workers with the Current and Updated Salary Levels, by Region, Division, and MSA Status, FY2017

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	132.75	22.51	18.29	4.23	19%
By Region / Division					
Northeast	24.77	4.80	4.02	0.79	16%
New England	6.69	1.36	1.17	0.19	14%
Middle Atlantic	18.08	3.44	2.84	0.59	17%
Midwest	29.53	4.73	3.84	0.88	19%
East North Central	19.97	3.17	2.58	0.58	18%
West North Central	9.56	1.56	1.26	0.30	19%
South	48.21	7.84	6.10	1.74	22%
South Atlantic	25.02	4.47	3.51	0.95	21%
East South Central	7.23	0.94	0.69	0.25	27%
West South Central	15.96	2.44	1.90	0.53	22%
West	30.25	5.15	4.32	0.82	16%
Mountain	9.48	1.51	1.22	0.29	19%
Pacific	20.76	3.64	3.10	0.53	15%
By Metropolitan Status					
Metropolitan	114.56	20.82	17.07	3.75	18%
Non-metropolitan	17.24	1.59	1.14	0.45	28%
Not identified	0.96	0.10	0.08	0.03	25%

Note: Pooled data for FY2013-FY2015 projected to reflect FY2017.

[a] 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 would be entitled to overtime protection under the updated salary levels (if their weekly earnings do not increase to the new salary levels).

iii. Costs

1. Summary

Three direct costs to employers were quantified in this analysis: (1) regulatory familiarization costs; (2) adjustment costs; and (3) managerial costs. Regulatory familiarization costs are costs to learn about the change in the regulation, occurring primarily in Year 1 and to a lesser extent in future years when the salary and compensation levels are automatically updated (e.g., Years 4, 7, 10). Adjustment costs are costs incurred by firms to determine workers' exemption statuses, notify employees of policy changes, and update payroll systems. Managerial costs occur because employers may spend more time scheduling newly nonexempt employees and more closely monitor their hours to minimize or avoid paying the overtime premium.

The Department estimated costs for Year 1 assuming that the first year of the analysis will be FY2017. The Department estimated that Year 1 regulatory familiarization costs will equal $272.5 million, Year 1 adjustment costs will sum to $191.4 million, and Year 1 managerial costs will total $214.0 million (Table 16). Total direct employer costs in Year 1 are estimated to equal $677.9 million. Regulatory familiarization costs, adjustment costs and management costs are recurring and thus are projected for years 2 through 10 (section VI.D.x.).

Many commenters, including PPWO, NRF, and the National Grocers Association, stated that the NPRM underestimated the costs of complying with the rulemaking. The Assisted Living Federation of America, Associated Builders and Contractors, and the College and University Professional Association for Human Resources (CUPA-HR) stated that 80 to 90 percent of respondents to their member surveys indicated that the Department's costs estimates were understated. Throughout this analysis, the Department addresses comments relating to regulatory familiarization costs, adjustment costs, and managerial costs in turn. We also discuss costs that are not quantified and comments asserting that the regulation will result in additional

unquantified costs in section VI.D.iii. Regulatory familiarization costs, adjustment costs and managerial costs associated with automatically updating the standard salary level are discussed in section VI.D.x.

Table16: Summary of Year 1 Direct Employer Costs (Millions)

Direct Employer Costs	Standard Salary Level	HCE Compensation Level	Total
Regulatory familiarization [a]	--	--	$272.5
Adjustment	$188.5	$2.9	$191.4
Managerial	$208.6	$5.5	$214.0
Total direct costs	$397.0	$8.4	$677.9

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

2. Regulatory Familiarization Costs

Changing the standard salary and HCE total compensation thresholds will impose direct costs on businesses by requiring them to review the regulation. It is not clear whether regulatory familiarization costs are a function of the number of establishments or the number of firms. The Department believes that generally the headquarters of a firm will conduct the regulatory review for the entire company; however, some firms provide more autonomy to their establishments, and in such cases regulatory familiarization may occur at the establishment level. To be conservative, the Department uses the number of establishments in its cost estimate assuming that regulatory familiarization occurs at a decentralized level.

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 Final Rule includes any provisions that may impact their workers. 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 regulations will probably follow the initial decision that the firm is affected). However, the Department does not know the distribution of affected EAP workers across firms and so an average cost per establishment is used.

In the NPRM, the Department requested that commenters provide data if possible on the costs of regulatory familiarization, and a few commenters provided estimates based on personal judgments or responses by members. While the information provided may reflect the experiences of individual commenters, the information does not provide a basis for the Department to revise its estimate of time required for regulatory familiarization. The Department continues to believe that our estimate of one hour per establishment in the NPRM is a reasonable average that accounts for some businesses requiring more time while other businesses require less time.

To estimate the total regulatory familiarization costs, three pieces of information must be estimated: (1) a wage level for the employees reviewing the rule; (2) the number of hours employees spend reviewing the rule; and (3) the number of establishments employing workers. The Department's analysis assumes that mid-level human resource workers with a median wage of $24.86 per hour will review the Final Rule.[156] Assuming benefits are paid at a rate of 46 percent of the base wage and one hour of time is required for regulatory familiarization, the

[156] We calculated this wage as the projected median wage in the CPS for workers with the Census 2010 occupations "human resources workers" (0630); "compensation, benefits, and job analysis specialists" (0640); and "training and development specialists" (0650) in FY2013-FY2015, projected to FY2017. The Department determined these occupations include most of the workers who would conduct these tasks. Bureau of Labor Statistics, U.S. Department of Labor, Occupational Outlook Handbook, 2014-15 Edition. These are the same occupation classifications used in the NPRM but updated to reflect the Census 2010 occupational classification.

average cost per establishment is $36.22.[157] The number of establishments with paid employees was 7.52 million.[158] Regulatory familiarization costs in Year 1 were estimated to be $272.5 million ($36.22 per hour x 1 hour x 7.52 million establishments).[159] Regulatory familiarization costs in future years are discussed in section VI.D.x.

Wage Rate

The Department estimated in the NPRM that one hour of regulatory familiarization time costs $34.19 based on the wage for a mid-level human resources worker adjusted to include benefits. We follow the same approach in this RIA; however, due to growth in wages, the wage rate used in the Final Rule is $36.22. The Chamber asserted that time spent on regulatory familiarization

[157] The benefits-earnings ratio is derived from the BLS' Employer Costs for Employee Compensation data using variables CMU1020000000000D and CMU1030000000000D. This fringe benefit rate includes some fixed costs such as health insurance. The Department believes that the overhead costs associated with for 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, as a sensitivity analysis of results, we calculate the impact of more significant overhead costs by including an overhead rate of 17 percent. This rate has been used by the Environmental Protection Agency (EPA) in its final rules (see for example, EPA Electronic Reporting under the Toxic Substances Control Act Final Rule, Supporting & Related Material), and is based upon a Chemical Manufacturers Association study. An overhead rate from chemical manufacturing may not be appropriate for all industries, so there may be substantial uncertainty concerning the estimates based on this illustrative example. Using an overhead rate of 17 percent would increase total costs (including regulatory familiarization costs, adjustment costs, and managerial costs) by from $677.9 million in Year 1 to $757.0 million, or 11.7 percent. For the reasons stated above, the Department believes this estimate overestimates the additional costs arising from overhead costs while recognizing that there is not one uniform approach to estimating the marginal cost of labor.

[158] Data for 2012 were the most recent available at the time of writing. Survey of U.S. Businesses 2012. Available at: https://www.census.gov/econ/susb/. Also included in the number of establishments incurring regulatory familiarization costs are the 90,106 state and local governments reported in the 2012 Census of Governments: Employment Summary Report. Available at: http://www2.census.gov/govs/cog/g12_org.pdf.

[159] As previously noted, the Department chose to use the number of establishments rather than the number of firms to provide a more conservative estimate of the regulatory familiarization cost. Using the number of firms, 5.82 million, would result in a reduced regulatory familiarization cost estimate of $210.7 million in Year 1.

will generally be conducted by a manager with a base wage better approximated at $60 per hour, multiplied by a mark-up of 3.3 to cover indirect overhead and support.[160] The National Association of Landscape Professionals (NALP) commented that 92 percent of the members it surveyed believe the wage rate should be "be more like $51.00 to $68.00 per hour."[161] The Department believes that we have utilized an appropriate wage rate; we similarly used wage rates for human resources specialists in the 2004 Final Rule (using a low to high range of such rates, depending upon employer size, rather than a single mid-level wage rate as we do currently). 69 FR 22222-24. Although higher paid managers may be briefed on the rule, we expect in general that mid-level human resource specialists will be the individuals primarily responsible for becoming familiar with the new rule. Moreover, this wage estimate is an average across all firms, some of which will pay higher rates and others lower rates.

Time Requirement

In the NPRM, the Department estimated each establishment will, on average, spend one hour on regulatory familiarization. Firms with more affected EAP workers will likely spend more time reviewing the regulation than firms with fewer or no affected EAP workers. No data were identified from which to estimate in the NPRM the amount of time required to review the regulation, and the Department requested that commenters provide data if possible. The Department did not receive any reliable data from commenters, although some commenters suggested different amounts of time based on their personal judgment or surveys they conducted. The American Hotel and Lodging Association (AH&LA), the National Roofing Contractors

[160] The Chamber also incorrectly stated that the Department used the wage for a "human resources office administrative clerk;" the Department actually used wages for "human resources, training, and labor relations specialists."

[161] NALP believes both time and hourly cost are underestimated. It is not clear whether the amount cited is the hourly wage rate members believe is appropriate or the total cost across more than one hour of time.

Association, NRF and others commented that regulatory familiarization will take longer than one hour, with some stating that several individuals in each of their establishments will need to read and familiarize themselves with the new rule. AH&LA estimated it will take at least four hours per establishment to become familiar with the Final Rule. The Chamber commented that an average of 6 hours of time is appropriate because: "For the very smallest establishments a familiarization time of one to two hours may be possible, but for larger establishments the number of labor hours may amount to hundreds or more."

The Department believes these commenters significantly overestimate the time necessary for regulatory familiarization. The EAP exemptions have been in existence in one form or another since 1938, and were updated as recently as 2004. While the 2004 rulemaking promulgated a host of changes, including revisions to the duties test, the most significant change promulgated in this rulemaking is setting a new standard salary level for exempt workers, and updating that salary level every three years. The Department believes that, on average, one hour is sufficient to time to read about and understand, for example, the change in the standard salary level from $455 to $913 per week, and we note that the regulatory text changes comprise only a few pages.

Recurrence

The Chamber criticized the Department for failing to estimate regulatory familiarization costs occurring after the first year, commenting that regulatory familiarization costs would repeat with each automatic update to the salary level. Upon further consideration, the Department agrees there will be some regulatory familiarization costs in future years when the salary level is updated (e.g., 2020, 2023, 2026). However, because subsequent updates will use the same method adopted in this Final Rule, and this rule informs stakeholders that the salary and compensation levels will be updated every three years, there is little additional regulatory change

with which employers will have to familiarize themselves. Accordingly, the Department has added 5 minutes per establishment of regulatory familiarization time to access and read the published salary levels in future years when the salary and compensation levels are automatically updated (see projected costs in section VI.D.x.).

3. Adjustment Costs

Changes in the standard salary and HCE compensation levels will impose direct costs on firms by requiring them to re-determine the exemption status of employees, update and adapt overtime policies, notify employees of policy changes, and adjust their payroll systems. The Department believes the size of these 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 for human resources, training, and labor relations specialists is $36.22 per hour (as explained above). No applicable data were identified from which to estimate the amount of time required to make these adjustments.[162] However, in response to comments claiming that the Department underestimated the adjustment time, for this Final Rule, the Department increased the time from one hour to 75 minutes per affected worker. The estimated number of affected EAP workers in Year 1 is 4.2 million (as discussed in section VI.D.ii.). Therefore, total Year 1 adjustment costs were estimated to equal $191.4 million ($36.22 x 1.25 hours x 4.2 million workers).

[162] Costs stated in 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.

Adjustment costs may be partially offset by a reduction in the cost to employers of determining employees' exempt status. Currently, to determine whether an employee is exempt firms must apply the duties test to salaried workers who earn at least $455 per week. Following this rulemaking, firms will no longer be required to apply the potentially time-consuming duties test to employees earning less than the updated salary level. This will be a clear cost savings to employers for employees 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.

Wage Rate

The Chamber commented that a more appropriate wage rate would be $200 per hour, based on a manager's wage of around $60 per hour, multiplied by a mark-up (or loaded) rate of 3.3 to cover indirect overhead and support. The Department believes its use of the occupation of "human resources, training, and labor relations specialists" and corresponding wage rate appropriately reflects the occupational classification and wage rate on average for the individuals who will re-determine the exemption status of employees, update and adapt overtime policies, notify employees of policy changes, and adjust their payroll systems. The Department recognizes that in some businesses, more senior staff will conduct at least portions of this work, while in other businesses, more junior staff may perform at least a portion of this work. Therefore, the Department continues to rely on its use of the "human resources, training, and labor relations specialists" and corresponding wage rate to reflect the average costs to businesses impacted by this Final Rule. The Department also disagrees with the mark-up rate suggested by the Chamber, because an additional 75 minutes of time will have little-to-no effect on the cost of overhead and support services. No other commenters provided alternative wage rates.

Time Requirement

To estimate adjustment costs, the Department assumed in the NPRM that each establishment will, on average, spend one hour of time per affected worker to make adjustments required because of this rulemaking. 80 FR 38566. The Department requested that commenters provide any applicable data concerning this issue, but no applicable data were identified from which to estimate the amount of time required to make these adjustments. The Department believes that commenters that did address adjustment costs significantly overestimated the time necessary for making appropriate workplace adjustments. However, the Department agrees that some increase is warranted, and thus increased the estimated average adjustment time to 75 minutes per affected worker.

Based on feedback from their members, AH&LA and Island Hospitality Management estimated that employers will need approximately four to seven hours per affected employee. The National Council of Chain Restaurants (NCCR) stated that "[e]mployers have told NCCR that the approximate time needed to make such adjustments will be 3-4 hours per employee," and NRF reported that its members "estimate it would take at least three to four hours per affected employee to make applicable adjustments." The American Insurance Association and the Property Casualty Insurers Association of America (AIA-PCI) asserted that adjustments will require more time than the Department estimated because employers will not make adjustments in response to the rule "in a vacuum; legal, HR, and operations all will need to be involved to assess risk, determine value, and ultimately decide whether a position, or classification, or part of a classification should be reclassified to non-exempt as a result of the Department's salary level increase." New Castle Hotels & Resorts similarly stated that a "hotel's GM and HR as well as the Department Head and the effected manager would all need to be involved together with

payroll." AIA-PCI also asserted that in many cases, information technology systems "cannot be configured to accommodate exempt and non-exempt employees in the same job classification," and thus additional time will be required to reconfigure these systems.

A report by Oxford Economics, submitted by NRF and referenced by other commenters, estimated the "transitional costs" associated with this rule.[163] The tasks covered by Oxford Economics' transition cost measure include: "identifying which employees ought to have salaries adjusted and then making and communicating that adjustment"; "converting a salaried employee to an hourly rate and then adding that employee to the time tracking system (already in use for existing hourly employees)"; disruptions to normal business operations; time for "HR personnel [to] communicate and implement the change"; time for additional IT support for time-tracking system; costs associated with the added complexity of managing and scheduling people's time; and costs associated with "establishing an hourly rate (lower than existing base salary) that is calculated so that overall compensation (including new overtime payments) will leave current total compensation unchanged." These costs appear to be roughly comparable to the Department's adjustment cost category, although with some inclusion of costs the Department categorized as managerial costs. However, Oxford Economics also included costs associated with converting newly nonexempt workers from salaried to hourly status, which the Department recognizes is a choice some employers may make in responding to this rule, but is not a requirement of the regulation. Oxford Economics estimated Year 1 transactional costs of $648 million in the retail and restaurant industry if the salary level were set at $808 per week,

[163] Oxford Economics. (2015). Rethinking Overtime: How Increasing Overtime Exemption Thresholds Will Affect The Retail And Restaurant Industries. Two additional documents produced by Oxford Economics were also included by some commenters: letter dated July 17, 2015 that updates the estimates provided in the "Rethinking Overtime" paper in light of the Department's proposal; and a letter dated August 18, 2015 that examines states' prevailing wage levels and the Department's automatic updating proposal.

and $874 million if the salary level were set at $984 per week. These costs for the retail and restaurant industry alone are roughly 4 to 5.5 times larger than our NPRM estimate for all industries ($160.1 million based on a $921 salary level in Year 1). The Department has evaluated Oxford Economics' analysis and determined that this discrepancy is due in part to Oxford Economics' estimation of the time requirement for adjustment.[164]

Oxford Economics assumed that adjustment costs for Type 1 workers (those who do not work overtime) are zero, and that each worker who receives a pay increase to the new salary level in order to remain exempt (Oxford Economics' equivalent to Type 4 workers) requires 1/1000th of a human resource employee full time equivalent; this equates to approximately 2.1 hours of time per affected worker (i.e., 2,080 FTE hours/1,000).[165] These per worker cost estimates are comparable to the Department's cost estimates. However, for employees reclassified as nonexempt as a result of the rulemaking, Oxford Economics appears to estimate that transitioning these workers will require 34.7 hours per worker for "group 2" workers and 10.4 hours per worker for "group 3" workers.[166] These workers appear to be very roughly comparable

[164] Although Oxford Economics' Table A2 reports some values they used to calculate transactional costs, the report NRF submitted to the record does not explain why they chose these values, nor does it describe in detail the source for these values, other than noting that it obtained information from "interviews with industry experts." Therefore, the Department could not easily assess the reasonableness of these estimates. See https://nrf.com/sites/default/files/Documents/retail%20library/Rethinking-Overtime-Appendices.pdf.

[165] As detailed in section VI.D.iv., the Department concludes that employers will respond to the Final Rule differently for different categories of workers, depending upon whether they work overtime and the nature of the overtime. The Department has divided workers into four categories, based upon the nature of any overtime work. Type 1 workers do not work overtime; Type 2 workers work occasional overtime (some on a regular basis and some on an unpredictable basis): Type 3 workers regularly work overtime; and Type 4 workers regularly work overtime and will earn sufficient wages after the Final Rule is implemented that employers will increase their salaries to the new level.

[166] Oxford Economics also estimated costs related to changing computer systems. This discussion focuses on Human Resources costs.

to the Department's Type 2 and 3 workers, but with much more extreme assumptions concerning how employers will respond (e.g., all overtime hours will be eliminated instead of reduced as the Department expects). Oxford Economics defines "group 2" workers as those who "will have their hourly wage rate set in such a way that their total compensation remains unchanged," and "group 3" workers as those who will "see their hours cut to 38 per week, with their salary cut proportionally."

The Department believes Oxford Economics' estimates of the time requirement for adjusting Type 2 and 3 (Oxford Economics' "group 2" and "group 3") workers are too high. It is unreasonable to expect, for example, that it will take a human resource worker 34.7 hours (almost an entire workweek) to reclassify each Type 2 worker as nonexempt, and possibly adjust his or her implicit hourly wage rate so the total compensation remains unchanged. As we stated above, in this Final Rule, the Department estimates an average of 75 minutes of adjustment time per affected worker. However, employers will need to exert minimal effort to determine the change in status of perhaps 60 percent of affected workers (e.g., the majority of affected workers who work no overtime). Thus, we assume that the average of 75 minutes per worker is concentrated on the subset of employees requiring more analysis to make a decision. If, for example, we allocate 0.5 hours per Type 1 worker and 50 percent of Type 2 workers (i.e., workers whose hours and base wage rates do not change), then that still leaves 3.0 hours per worker for the remaining 50 percent of Type 2 workers, and all Type 3 and Type 4 workers. Finally, larger firms are likely to experience economies of scale in evaluating affected workers; a decision on how to treat a worker with specific characteristics (e.g., earnings, hours, duties) is likely to be applicable to multiple workers.

With respect to the concern raised by AIA-PCI about reconfiguring 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) so that additional costs associated with the rule should be relatively small in the short run.[167]

[167] The Department notes that no particular form or order of records is required and employers may choose how to record hours worked for overtime-eligible employees. For example where an employee works a fixed schedule that rarely varies, the employer may simply keep a record of the schedule and indicate the number of hours the worker actually worked only when the worker varies from the schedule. This is sometimes referred to as exceptions reporting. 29 CFR 516.2(c).

Recurrence

The Chamber also expressed concern the Department underestimated projected adjustment costs associated with automatic updating, stating that employers would incur significant adjustment costs in years the salary is automatically updated, even if subsequent salary level changes affect fewer workers than the initial increase (to $913). Similarly, PPWO stated that the Department's cost projections did not account for the fact that "compliance review activities that take place in Year 1 will be repeated on an annual basis, for different groups of employees that fall below the new salary minimum." See also North Dakota Bankers Association (the Department should recognize that future salary updates require time to determine whether an employee should be classified as exempt or nonexempt, not just time to reprogram the payroll). Contrary to these comments, the Department's estimated adjustment costs include costs in all years for newly affected workers. The Department limits adjustment costs in projected years to newly affected workers because there is no need to "adjust" for workers who are already overtime eligible (due to a prior adjustment of the EAP salary level) when the salary level is updated again.

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 associated with this Final Rule because the employer may schedule and more closely monitor an employee's hours to minimize or avoid working overtime-eligible employees more than 40 hours in a week. 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 and to a much lesser extent in years when the salary is automatically updated, managerial costs are incurred more uniformly every year.

Because there was little precedent or data to aid in evaluating these costs, the Department examined several sources to estimate costs. First, prior part 541 rulemakings were reviewed to determine whether managerial costs were estimated. No estimates were found. This cost was not quantified for the 2004 rulemaking. Second, a literature review was conducted in an effort to identify information to help guide the cost estimates; again, no estimates were found. The Department also requested data from the public applicable to this cost estimate; however, as discussed below, the Department received no time estimates that seemed more appropriate than the estimates used in the NPRM.

Based on commenters' concerns, discussed below, that managerial costs are applicable to more workers than were included in the NPRM, the Department expanded the number of workers for whom employers experience additional managerial costs (section VI.D.iv.) As in the NPRM, managerial costs are applied to workers who are reclassified as overtime-protected and who either regularly work overtime or occasionally work overtime but on a regular basis. For the Final Rule, however, the Department expanded its count of the number of workers who occasionally work regular overtime (defined later as half of Type 2 workers) by assuming that some Type 1 workers (who report that they do not work overtime) will actually work overtime during some week of the year. Therefore, the number of workers for whom we apply managerial costs increased from 808,000 using the NPRM methodology to 1.2 million using the Final Rule methodology.

To provide a sense of the potential magnitude of these costs, the Department estimated these costs assuming that management spends an additional five minutes per week scheduling and monitoring each affected worker expected to be reclassified as overtime eligible as a result of this rule, and whose hours are adjusted (1.2 million affected EAP workers as calculated in section VI.D.iv.). As will be 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. Similarly, employers are likely to find that it is less costly to give some workers a raise in order to maintain their exempt status. For both these groups of workers, management will have little or no need to increase their monitoring of hours worked. Under these assumptions, the additional managerial hours worked per week were estimated to be 97,300 hours ((5 minutes/60 minutes) x 1.2 million workers).

The median hourly wage in FY2017 for a manager is estimated to be $29.04 and benefits are estimated to be paid at a rate of 46 percent of the base wage, which totals $42.31 per hour.[168,169] Multiplying the additional 97,300 weekly managerial hours by the hourly wage of $42.31 and 52 weeks per year, the Year 1 managerial costs were estimated to total $208.6 million due to this rule. Although the exact magnitude would vary with the number of affected EAP workers each year, managerial costs would be incurred annually.

Additional Investment

Some commenters, such as the National Grocers Association and the National Association of Area Agencies on Aging asserted that managerial costs will be higher than the Department estimated because some employers may need to purchase new systems or hire additional

[168] Calculated as the projected median wage in the CPS for workers in management occupations (excluding chief executives) in FY2013-FY2015, projected to FY2017.
[169] The adjustment ratio is derived from the BLS' Employer Costs for Employee Compensation data using variables CMU1020000000000D and CMU1030000000000D.

personnel to monitor hours. However, the Department believes that most companies already manage a mix of exempt and nonexempt employees, and already have policies and recordkeeping systems in place for nonexempt employees. Thus, they are unlikely to need to purchase systems or hire additional monitoring personnel as a result of this rulemaking. Moreover, no particular form or order of records is required and employers may choose whatever form of recordkeeping works best for their business and their employees. For example, where an employee works a fixed schedule that rarely varies, the employer may simply keep a record of the schedule and indicate the number of hours the worker actually worked only when the worker varies from the schedule ("exceptions reporting"). 29 CFR 516.2(c). Because simple recordkeeping systems, such as exceptions reporting systems for workers on a fixed schedule, are permissible, costs may be minimal.

Time Requirement

Several commenters asserted that scheduling and monitoring newly overtime eligible workers will require more time than the Department assumes. One human resource manager commented that the time required will "be closer to 15 minutes than 5," and AH&LA stated that its members believe these costs "will be closer to 25 minutes to an hour a week." NCCR stated that it received feedback from employers in the restaurant industry who estimated that managerial costs will range from one to three hours per week. NRF similarly states that its members estimated that managerial costs would range from one to three hours per week.

The Department believes these commenters' estimates are excessive. For example, 75 percent of currently exempt employees who work overtime average less than 10 hours of overtime per week. Assuming a newly nonexempt employee averages 10 hours of overtime per week, then based on NCCR's estimate, a manager would spend from 6 minutes to 18 minutes monitoring for

each hour of overtime worked by that employee. The Department believes this estimate is unrealistically high. We also note that commenters did not submit any data supporting their 15 minute and 25 minute estimates. Furthermore, we recognize that employers routinely apply efficiencies in their operations, and see no reason why they will not do so with regard to scheduling as well.

Wage Rate

The Chamber recommended that the Department use the mean wage rather than the median to calculate hourly managerial costs, and also asserted that the wage should include all loaded overhead cost. However, the mean and median wages for managers are very similar in the CPS data ($32.71 versus $29.04, respectively), so using the mean wage will not result in substantially different estimated costs. Furthermore, if the distribution of wages is skewed (as demonstrated here by a mean wage larger than the median wage), the median value is more representative of the wage most firms will pay. The Department does not believe it is appropriate to use all overhead costs in estimating a marginal cost increase because the relevant cost is the marginal value of the cost of labor, which is much smaller than the loaded overhead cost. Most overhead costs are largely fixed and unaffected if an employee works an incremental hour. For example, accounting and administrative staff are unlikely to work more time; building rent, heat and electricity are unlikely to change if a supervisor or human resource staff person works an incremental hour. However, acknowledging that there might be some overhead costs, we include a sensitivity analysis providing an upper bound cost estimate.[170]

[170] As a sensitivity analysis of results, we calculate the impact of more significant overhead costs by including an overhead rate of 17 percent. This rate has been used by the EPA in its final rules (see for example, EPA Electronic Reporting under the Toxic Substances Control Act Final Rule, Supporting & Related Material), and is based upon a Chemical Manufacturers Association study. An overhead rate from chemical manufacturing may not be appropriate for all industries, so there

Number of Affected Workers

The Chamber also asserted that managerial costs should apply to all affected workers whose status changes, not just those who regularly work overtime, because "even those who usually work only 40 hours will require additional management schedule monitoring to ensure that their hours do not go higher." The Department believes that although some companies may closely monitor hours for workers who usually do not work overtime, many companies do not. Many companies simply prohibit overtime without express approval and/or assign workers to a set weekly schedule of hours; in such firms monitoring costs for these newly nonexempt workers who usually do not work overtime should be negligible. Furthermore, without additional information, it is impossible to determine the prevalence of the more strenuous form of managerial oversight described by the Chamber. However, we did increase the number of workers for whom managerial costs are estimated to include more occasional overtime workers, as discussed above.

5. Other Potential Costs

In addition to the costs discussed above, there may be additional costs that have not been quantified. In the NPRM we identified these potential costs to include reduced profits and hiring costs. See 80 FR 38578-80. Commenters addressed a variety of other potential costs.

---

may be substantial uncertainty concerning the estimates based on this illustrative example. Using an overhead rate of 17 percent would increase total costs (including regulatory familiarization costs, adjustment costs, and managerial costs) by from $677.9 million in Year 1 to $757.0 million, or 11.7 percent. For the reasons stated above, the Department believes this estimate overestimates the additional costs arising from overhead costs while recognizing that there is not one uniform approach to estimating the marginal cost of labor.

Reduced Scheduling Flexibility

Some commenters, such as the ASAE, Thombert, Inc., Applied Measurement Professionals; and Alaska USA Federal Credit Union, asserted that exempt workers enjoy more scheduling flexibility claiming that their hours generally are not monitored, and thus this rulemaking will impose costs on newly overtime-eligible workers by (for example) limiting their ability to adjust their schedule to meet personal and family obligations. Other commenters suggested that the rulemaking would impose costs on employers because they will lose flexibility to schedule employees. For example, TRANSITIONS for the Developmentally Disabled commented that "[h]aving managers that can work those urgencies and emergencies, then giving them time off later to make up for those extra hours, helps our managers manage the business without us paying expensive overtime or having someone without managerial skills deal with those situations" (emphasis in comment).

The Final Rule does not necessitate that employers 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 does not quantify potential costs regarding scheduling flexibility to either employees or employers. Moreover, the limited literature available suggests that if there is a reduction in flexibility for employees, it would not be as large as commenters suggested. A study by Lonnie Golden[171], referenced by the National Employment Law Project (NELP), found using data from the General Social Survey (GSS) that "[i]n general, salaried workers at the lower

[171] Golden, L. (2014). Flexibility and Overtime Among Hourly and Salaried Workers. Economic Policy Institute.

(less than $50,000) income levels don't have noticeably greater levels of work flexibility that they would 'lose' if they became more like their hourly counterparts."

Reclassification to Overtime Eligible Status

Some commenters asserted that the rulemaking will negatively affect the morale of employees reclassified as overtime eligible.[172] For example, WorldatWork stated that 79 percent of survey respondents said the proposed rule would have a negative effect on the reclassified employees' morale, as exemption classification is a perceived measure of status desired by employees, and Kimball Midwest similarly commented that "many of the young professionals that we employ would view being reclassified to nonexempt as a demotion and an insult to their professional and social status in the workplace." The Department believes that for most employees their feelings of importance and worth come not from their FLSA exemption status, but from the increased pay, flexibility, fringe benefits, and job responsibilities that traditionally have accompanied exempt status, and that these factors are not incompatible with overtime eligibility.

However, if the worker does prefer to be salaried rather than hourly, then this change may impact the worker. The likelihood of this impact occurring depends on the costs to employers and benefits to employees of being salaried. Research has shown that salaried workers (who are not synonymous with exempt workers, but whose status is correlated with exempt status) are more likely than hourly workers to receive benefits such as paid vacation time and health insurance,[173] are more satisfied with their benefits,[174] and that when employer demand for labor

[172] The Department notes that to the extent that such negative effects are attributable to the employer converting the employee to hourly pay status, employers can avoid this consequence by continuing to pay overtime-eligible employees a salary and pay overtime when the employee works more than 40 hours in the workweek.

[173] 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, D.C.: Urban Institute Press.

decreases, hourly workers tend to see their hours cut before salaried workers, making earnings for hourly workers less predictable.[175] 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.

Some evidence suggests that it is more costly for the employer to employ a salaried worker than an hourly worker. If true, employers may choose to accompany the change in exemption status with a change to the employee's method of pay, from salary to an hourly basis, since there is no longer as great an incentive to classify the worker as salaried.[176]

Jackson Lewis asserted that the Department did not adequately consider other costs associated with reclassifying employees from exempt to nonexempt: "This is not just a mere matter of accounting for potential changes in direct wage costs. Exempt and non-exempt employees function very differently in the workplace. Reclassifying employees imposes costs with respect to re-engineering roles, determining new performance metrics, and devising compensation programs that drive the desired behaviors consistent with an obligation to pay a wage premium after forty hours in a workweek." We believe these considerations are adequately accounted for in the Department's adjustment cost estimate, which we increased by 15 minutes from 60 to 75 minutes for each affected worker.

---

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

[175] 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, D.C.: Urban Institute Press.

[176] There is not requirement that overtime eligible employees be paid on an hourly basis. Paying such employees a salary is appropriate so long as the employee receives overtime pay for working more than 40 hours in the workweek. See §§ 778.113-.114.

Earnings Predictability

Some commenters asserted that employers will convert newly nonexempt employees to hourly pay and that these employees will lose the earnings predictability of a guaranteed salary. See, e.g., AH&LA; Island Hospitality Management; NCCR; NRF. These commenters asserted that receipt of a guaranteed minimum salary provides peace of mind to employees. These comments appear to reflect a common misperception among employers that overtime-eligible employees must be paid on an hourly basis. Overtime-eligible employees 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 premium on that base wage for any overtime hours each week. §§ 778.113-.114.

Reduced Opportunities for Training and Advancement

Some commenters stated that the rulemaking will reduce training and promotional opportunities. For example, ASAE commented that employers would not permit newly overtime eligible employees to attend conferences and annual meetings. In response to these comments, the Department notes that if an employer believes that training opportunities are sufficiently important, it can ensure employees attend the trainings during their 40-hour workweek, or pay the overtime premium where training attendance causes the employee to work over 40 hours in a workweek. Given this, and because there is no data and literature to quantify any potential costs to workers, we decline to do so in this analysis.

Reduced Productivity

Some commenters expressed concern that the automatic updating provisions of the rule may reduce productivity. For example, the Michael Best & Friedrich law firm commented that many

employees will "assume they could perform at the same level, or do the bare minimum, and still receive an automatic pay increase," and this "unmotivated workforce will lead to lesser productivity." This rulemaking does not require any employer to provide an automatic pay raise when the standard salary level increases. As always, employers have the ability to determine which employees deserve raises, and the size of that raise, and to decide how to handle employees whose work is unsatisfactory. Additionally, the Final Rule has been modified so that updating will occur every three years, not annually, which should lessen commenters' concerns on this issue. Furthermore, as discussed in section VI.D.vii., the Department believes that in some instances employers may in fact experience increased worker productivity due to factors including efficiency wages, improved worker health, and a reduction in turnover.

Quality of Services

Some commenters expressed concern that the rulemaking, by restricting work hours, will negatively impact the quality of public services provided by local governments, see, e.g., City of Galax; disability services providers, see, e.g., American Network of Community Options and Resources (ANCOR); health care providers, see, e.g., Lutheran Services in America; education providers, see, e.g., La Salle Catholic College Preparatory, and others. The Indian River Schools commented that the "only way a school system can adjust for this change is to reduce services to students, given that our industry operates with low-overhead."

The Department believes the impact 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. However, 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, as discussed in section VI.D.vii.,

may offset some reduction in services. Furthermore, the Department notes that school systems would largely be unaffected by the rulemaking: teachers and academic administrative personnel are "named occupations" and thus do not have to pass the salary level test to remain exempt. 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, as indicated in the comments of many employers.

Increased Prices

Some commenters expressed concern that increased labor costs will be passed along to consumers in the form of higher prices. See, e.g., National Association of Home Builders (NAHB) (stating that of the 33 percent of members surveyed who predicted some change, 44 percent indicated that the proposal "would result in higher home prices for consumers"); SnowSports Industries of America. NRF stated that many of its members noted that raising prices would result in a loss of sales.

The Department does anticipate that, in some cases, part of the additional labor costs may be offset by higher prices of goods and services. However, because costs and transfers are on average small relative to payroll and revenues, the Department does not expect this rulemaking to have a significant effect on prices. The Department projects that, on average, costs and transfers make up less than 0.03 percent of payroll and less than 0.01 percent of revenues, although for specific industries and firms this percentage may be larger. Therefore, the Department expects that any potential change in prices will be modest. Further, any significant price increases, would generally not represent a separate category of impacts relative to those

estimated in the RIA; rather, price increases (where they occur) are the channel through which consumers, rather than employers or employees, bear rule-induced costs (including transfers).[177]

Foreign Competition

Some commenters expressed concern that the rulemaking will hurt the United States' ability to compete in the international market. See, e.g, Jackson Lewis; NACCO Industries; National Association of Manufacturers; National Association of Wholesale Distributors; Precision Machined Products Association. The Department does not believe this is a serious concern due to the small ratio of employer costs and transfers to revenues.

Substitution of Capital

Some commenters, such as the National Parking Association and the National Beer Wholesalers Association, asserted that, by increasing the marginal cost of labor, the rule will lead companies to automate their business operations and substitute capital for labor. The Department believes that it is unlikely that employees performing jobs that can be easily automated will satisfy the duties test, and that any such effect would be negligible due to the small ratio of employer costs and transfer payments to operating revenue.

Wage Compression and Spillover Effects

Several commenters stated that employers may increase the wages of workers currently paid just above the new threshold to maintain a distribution of wages, and some asserted that the Department failed to account for this effort to avoid salary compression in our economic analysis. See, e.g., Cornerstone Credit Union League; First Premier Bank; HMR Acquisition

[177] The deadweight loss associated with price increases is appropriately categorized as a cost, but it is discussed in detail in in section VI.D.vi because the methodology whereby it is estimated is more clearly explained as a follow-up to the transfers methodology.

Company; International Franchise Association; PPWO; Seyfarth Shaw law firm; Tulsa Regional Chamber. The Department did not consider salary compression in the NPRM because data are not available to estimate this effect. For the same reason, we decline to consider this cost in the analysis accompanying this Final Rule.

Substitution of Part-Time Jobs in Place of Full-Time Jobs

Some commenters stated that firms will reduce the number of full-time positions and replace them with part-time positions to limit overtime payments. See, e.g., Associated General Contractors of America (AGC); National Newspaper Association; SnowSports Industries of America. These commenters assume that rather than cutting the hours of a worker who works 60 hours per week to 40 hours and hiring a part-time employee to work the remaining 20 hours (which would potentially reduce unemployment), employers will create part-time positions at the expense of full-time employment.

As an initial matter, an employer will have an incentive to make these adjustments only if the cost of paying overtime is greater than the costs associated with hiring another worker. Further, although the Department acknowledges the possibility that firms may reduce the number of full-time positions and replace them with part-time positions, on net the Department believes the benefits of additional jobs (i.e., external margins) will outweigh any detriment of reduction in hours for current employees (i.e., internal margins), although the Department cannot quantify this effect. Due to data limitations the Department has not estimated transfers between workers. We note, however, that most of the estimates submitted by commenters of large costs, transfers, and employment impacts rely implicitly on the assumption that employers make no adjustment to the rulemaking except to pay the overtime premium. This lack of employer response is

contradicted by quantitative analysis of employer behavior (see Barkume,[178] for example), and by the employer comments on this rulemaking. Employers will adjust to the rule by adjusting base pay for newly nonexempt employees, as well as in other ways. After accounting for employer adjustments, the costs and transfers resulting from the rule are small relative to payroll and revenues, as are the projected reductions in employee hours, and the likelihood of large scale impacts on employment appears to be small.

Conversely, other commenters, such as the International Food Service Distributors Association, expressed concern that employers would eliminate part-time positions "where the employees value the flexibility." See also CUPA-HR. The Department believes it is unlikely that an employer will eliminate part-time positions simply because the workers become eligible for overtime, as an employer will not have to pay workers employed for less than 40 hours per week the overtime premium even if they are newly entitled to overtime pay.

Finally, the Home Loan and Investment Company and other commenters also asserted that some workers who currently hold only one job will need to take a second job to supplement their now reduced hours. This would reduce workers' utility since juggling two jobs is more difficult than holding one job, even if the total hours are the same. To address this concern, the Department looked at the effect of the 2004 rulemaking on the probability of multiple job holding. The 2004 rulemaking increased the salary level required to be eligible for exemption from $250 per week (short test salary level) to $455 (standard test salary level).[179] To estimate

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

[179] The 2004 Final Rule increased the salary level from the previous long test level of $155 per week (executive and administrative exemptions) or $170 per week (professional exemption) to $455 per week. For purposes of this analysis, the Department compared the increase from the short test salary level ($250 per week) since the long test was no longer operative due to increases in the minimum wage.

the effect of this update on the share of full-time, white collar workers holding multiple jobs, the Department conducted a difference-in-differences (DD) analysis. This analysis allows the identification of any potential regulatory impact, while controlling for time trends and a broad range of other relevant factors (education, occupation, industry, geographic location, etc.). The Department compared January-March 2004 to January-March 2005[180] and compared workers earning between $250 and $455 and those earning at least $455 but less than $600. The Department found no statistically significant change in workers' probability of holding multiple jobs before and after the 2004 Final Rule took effect.[181] However, a caveat should be noted about

---

[180] The 2004 Final Rule was published April 23, 2004 and went into effect August 23, 2004.

[181] The difference-in-differences model used to examine whether the share of workers holding multiple jobs increased as a result of the 2004 rule can be written as

$$M_i = \beta_0 + \beta_1 T_i + \beta_2 P_i + \beta_3 T_i * P_i + \sum_n \beta_n C_{in} + u_i,$$

where M_i is equal to 1 if worker i is has more than one job and 0 otherwise, T_i is equal to 1 if worker i earns at least $250 but less than $455 and 0 if he earns between $455 and $600, P_i is equal to 1 for the post-change period (Jan.-Mar. 2005) and 0 for the pre-change period (Jan.-Mar. 2004), and C_i is a set of worker-specific controls (age, education, gender, race, ethnicity, occupation, industry, state of residence, working overtime, whether paid hourly or salaried). The model was estimated using a probit regression. The relevant marginal effect is -0.009 (i.e., the amount the likelihood of multiple job holding changes post rulemaking for workers earning between $250 and $455 per week relative to the change for workers earning between $455 and $600), with a standard deviation of 0.006. Thus, while the point estimate shows a decrease in the probability of multiple job holding for affected workers after the 2004 Final Rule took effect, the finding is not statistically significant at conventional thresholds for significance. The Department also used a difference-in-difference-in-differences model to examine whether the share of workers holding multiple jobs increased as a result of the California's increase in the salary threshold from $540 to $640 between 2006 and 2008 and from $640 to $720 between 2014 and 2015. That model can be written as

$$M_i = \beta_0 + \beta_1 T_i + \beta_2 P_i + \beta_3 T_i * P_i + \beta_4 S_i + \beta_5 T_i * S_i + \beta_6 P_i * S_i + \beta_7 T_i * P_i * S_i + \sum_n \beta_n C_{in}$$

where M_i is equal to 1 if worker i has multiple jobs and 0 otherwise, T_i is equal to 1 if worker i earns between the old threshold and the new threshold and 0 if he earns just above the new threshold, P_i is equal to 1 for the post-change period and 0 for the pre-change period, S_i is equal to 1 if worker i is in California and 0 if she is in other states where the salary level was not increased, and C_i is the same set of worker-specific controls used in the DD analysis. The model was estimated using a probit regression. For the

interpreting this result as an indication that the Final Rule will not lead to an increase in the holding of multiple jobs. This rule is estimated to affect approximately three times as many workers as the 2004 rule (for which the Department estimated 1.3 million affected workers), and factors that could not be controlled for in the analysis of the 2004 rule may lead to a different outcome based on this rule.

Reduced Profits

Some commenters, including an HR consultant, a small business owner, and a commenter from the restaurant industry, expressed concern that establishments with small profit margins may lose money or go out of business. The increase in workers' earnings resulting from the revised salary level is a transfer of income from firms to workers, not a cost, and is thus neutral concerning its primary effect on welfare. However, there are potential secondary effects (both costs and benefits) of the transfer due to the potential difference in the marginal utility of income and the marginal propensity to consume or save between workers and business owners. Thus, the Department acknowledges that profits may be reduced due to increased employer costs and transfer payments as a result of this rule, although some of these costs and transfers may be offset by making payroll adjustments or the profit consequences of costs and transfers partially mitigated through increased prices.[182] The Department notes that firms have a broad array of approaches for adjusting to the rulemaking: firms that face robust demand may be able to increase product prices and may make smaller adjustments to base wages or overtime hours;

---

change between 2006 and 2008, the relevant marginal effect is -0.025 with a standard deviation of 0.004, and for the change between 2014 and 2015, the relevant marginal effect is 0.042 with a standard deviation of 0.018. Thus we observe a statistically significant (at conventional thresholds) increase in the share of workers holding multiple jobs in one period but a statistically significant (at conventional thresholds) decrease in the other.

[182] As shown below, because costs and transfers generally compose less than one percent of revenues, the Department expects any such price increases to be minor.

firms that have little ability to raise prices may have to make more substantial changes to wages or other variables. Further, because costs and transfers are on average small relative to payroll and revenues, the Department does not expect this rulemaking to have a significant effect on profits. Additionally, increased payroll may lead to increased consumer spending which may translate into higher profits, offsetting part of the initial reduction in profits. Two business owners who commented separately in support of the Department's proposal cited an increase in sales as a likely consequence of this rulemaking.

Hiring Costs

One of Congress' goals in enacting the FLSA in 1938 was to spread employment to a greater number of workers by effectively raising the wages of employees working more than 40 hours per week. To the extent that firms respond to an update to the salary level test by reducing overtime, 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.

iv. Transfers

1. Overview

Transfer payments occur when income is redistributed from one party to another. The Department has quantified two possible transfers from employers to employees likely to result from this update to the salary level tests: (1) transfers to ensure compliance with the FLSA minimum wage provision; and (2) transfers to ensure compliance with the FLSA overtime pay provision. Transfers in Year 1 to workers from employers due to the minimum wage provision were estimated to be $34.3 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. Transfers to employees from employers due to the overtime pay provision were estimated to be $1,250.8 million, $1,152.3 million of which is from the increased standard salary level, while the remainder is attributable to the increased HCE compensation level. Total Year 1 transfers were estimated to be $1,285.2 million (Table 17).

Table 17: Summary of Year 1 Regulatory Transfers (Millions)

Transfer from Employers to Workers	Standard Salary Level	HCE Compensation Level	Total
Due to minimum wage	$34.3	$0.0	$34.3
Due to overtime pay	$1,152.3	$98.5	$1,250.8
Total transfers	$1,186.6	$98.5	$1,285.2

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. The implicit regular rate of pay is calculated as usual weekly earnings divided by usual weekly hours worked. For those employees whose implicit regular rate of pay is below the minimum wage, the overtime premium was based on the minimum wage as the regular rate of pay.

2. Transfers Due to the Minimum Wage Provision

Transfers from employers to workers to ensure compliance with the higher of the federal or applicable state minimum wage are small compared to the transfers attributed to overtime pay and are only associated with the change in the standard salary level. For purposes of this analysis, the hourly rate of pay is calculated as usual weekly earnings divided by usual weekly

hours worked. In addition to earning below the federal or state minimum wage, this set of workers also works many hours per week. To demonstrate, in order to earn less than the federal minimum wage of $7.25 per hour, but at least $455 per week, these workers must regularly work significant amounts of overtime (since $455/$7.25 = 62.8 hours). The applicable minimum wage is the higher of the federal minimum wage and the state minimum wage as of January 2016. Most affected EAP workers already receive at least the minimum wage; an estimated 11,200 affected EAP workers (less than 0.3 percent of all affected EAP workers) currently 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 and thus would have to be paid at least the minimum wage.[183]

In response to an increase in the regular rate of pay to the minimum wage, employers may reduce the workers' hours, which must be considered when estimating transfers attributed to payment of the minimum wage to newly overtime-eligible workers. In theory, because the quantity of labor hours demanded is inversely related to wages, a higher mandated wage could result in fewer hours of labor demanded. However, the weight of the empirical evidence finds that increases in the minimum wage have caused little or no significant job loss.[184] Thus, in the

[183] 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.

[184] Belman, D., and P. J. Wolfson (2014). What Does the Minimum Wage Do? Kalamazoo, MI: W.E. Upjohn Institute for Employment Research. Dube, A., T. W. Lester, and M. Reich. (2010). Minimum Wage Effects Across State Borders: Estimates Using Contiguous Counties. The Review of Economics and Statistics, 92(4), 945-964. Schmitt, J. (2013). Why Does the Minimum Wage Have No Discernible Effect on Employment? Center for Economic and Policy Research.

case of this regulation, the Department believes that any disemployment effect due to the minimum wage provision would be negligible. This is partially due to the small number of workers affected by this provision. The Department estimates 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 -0.075.[185]

At the new standard salary level ($913 per week), the Department estimates that 11,200 affected EAP workers will on average see an hourly wage increase of $0.91, work 0.7 fewer hours per week, and receive an increase in weekly earnings of $59.10 as a result of coverage by the minimum wage provisions (Table 18). The total change in weekly earnings due to the payment of the minimum wage was estimated to be $660,300 per week ($59.10 x 11,200) or $34.3 million in Year 1.

Table18: Minimum Wage Only: Mean Hourly Wages, Usual Overtime Hours, and Weekly Earnings for Affected EAP Workers, FY2017

	Hourly Wage [a]	Usual Weekly Hours	Usual Weekly Earnings	Total Weekly Transfer (1,000s)
Before Final Rule	$8.13	69.3	$551.2	--
After Final Rule	$9.04	68.6	$610.3	--
Change	$0.91	-0.7	$59.1	$660.3

Note: Pooled data for FY2013-FY2015 projected to reflect FY2017.

[185] This is based on the estimated impact of a change in the minimum wage from $7.25 to $9.00 per hour on the employment of teenagers from the Congressional Budget Office. (2014). The Effects of a Minimum Wage Increase on Employment and Family Income. While an elasticity estimate for adult workers would be more appropriate, the report stated that the elasticity for adults was “about one-third of the elasticity” for teenagers, without providing a specific value. In addition, the literature for adults is more limited. The size of the estimated reduction in hours is thus likely to be an upper bound.

[a] The applicable minimum wage is the higher of the federal minimum wage and the state minimum wage.

Modeling employer adjustments for these workers is a two-step process. First, employers adjust wages and hours to meet the minimum wage requirement, as described here. Then, these workers' hours will be further adjusted in response to the requirement to pay the overtime premium, which is discussed in the following section. The transfers presented here only apply to the minimum wage provision. However, minimum wage transfers impact overtime transfers because the overtime premium is calculated based on the minimum wage, not the worker's original wage. Thus, the two are not entirely separable.

3. Transfers Due to the Overtime Pay Provision

Introduction

The Final Rule will also 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 or hours. Thus, the size of the transfers due to the overtime pay provision will depend largely on how employers respond to the updated salary levels. How employers respond and the ensuing changes in employment conditions will depend on the demand for labor, current wages, employer and employee bargaining power, and other factors. Employers may respond by: (1) paying the required overtime premium to affected workers for the same number of overtime hours at the same implicit regular rate of pay; (2) reducing overtime hours and potentially transferring some of these hours to other workers; (3) increasing workers' salaries to the updated salary or compensation level; (4) reducing the regular rate of pay for workers working overtime; 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.

The simplest approach to estimating these transfer payments would be to multiply an employee's regular rate of pay (after compliance with the minimum wage) by 1.5 for all overtime hours; this is referred to as the "full overtime premium" model.[186] However, due to expected wage and hour adjustments by employers, this would likely overestimate the size of the transfer. Therefore, the Department used a methodology that allows for employer adjustments, such as changes in the regular rate of pay or hours worked. The size of these adjustments is likely to vary depending on the affected worker's salary and work patterns. To model employer responses, the Department used a method that reflects the average response among all employers for all affected workers. However, individual employer responses will vary.

Literature on Employer Adjustments

Two conceptual models are useful for thinking about how employers may respond to reclassifying certain employees as overtime eligible: the "full overtime premium" model and the "employment contract" model.[187] 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.

[186] The implicit regular rate of pay is calculated as usual weekly earnings divided by usual weekly hours worked. For example, the regular rate of pay for an employee previously ineligible for overtime whose usual weekly earnings was $600 and usual weekly hours was 50 would be $12 per hour. Under the full overtime premium model, this employee would receive $660 ((40 hours x $12) + (10 hours x $12 x 1.5)).

[187] The employment contract model is also known as the fixed-job model. 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.

The full overtime premium model is based on what we will refer to as the "labor demand" model of determining wage and hour conditions. In the labor demand model, employers and employees negotiate fixed hourly wages and then subsequently negotiate hours worked, rather than determining both hours and pay simultaneously. This model assumes employees are aware of the hourly wage rate they negotiated and may be more reluctant to accept downward adjustments. The labor demand model would apply if employees had a contract to be paid at an hourly rate, meaning that employers could not reduce the regular rate of pay in response to the requirement to pay a 50 percent premium on hours worked beyond 40 in a week. However, the increase in the marginal cost of labor would lead to a reduction in the hours of labor demanded as long as labor demand is not completely inelastic. The full overtime premium model is a special case of the labor demand model in which the demand for labor is completely inelastic, that is employers will demand the same number of hours worked regardless of the cost.

In the employment contract model, employers and employees negotiate total pay and hours simultaneously, rather than negotiating a fixed hourly wage and then determining hours. Under this model, when employers are required to pay employees an overtime premium, they adjust the employees' implicit hourly rate of pay downward so that when the overtime premium is paid total employee earnings (and thus total employer cost) remain constant, along with the employees' hours. The employer does not experience a change in cost and the employee does not experience a change in earnings or hours. The employment contract model would hold if the workers who are reclassified as overtime protected had an employment agreement specifying set total earnings and hours of work.

The employment contract model tends to be more applicable when overtime hours are predictable, while the labor demand model is generally more applicable to situations where the

need for overtime is unanticipated (for example, where there are unforeseen, short-term increases in demand). However, the employment contract model may not fully hold even for workers who work predictable overtime due to market imperfections, employer incentives, or workers' bargaining power. Four examples are provided.

- Employers are constrained because they cannot reduce an employee's implicit hourly rate of pay below the minimum wage. If the employee's implicit hourly rate of pay before the change is at or below the minimum wage, then employers will not be able to reduce the rate of pay to offset the cost of paying the overtime premium.
- Employees generally have some, albeit limited, bargaining power which may prevent employers from reducing the employee's implicit hourly rate of pay to fully offset increased costs.
- Employers may be hesitant to reduce the employee's implicit hourly rate of pay by the entire amount predicted by the employment contract model because it may hurt employee morale and consequently productivity.[188]
- Employers are often limited in their ability to pay different regular rates of pay to different employees who perform the same work and have the same qualifications because of fairness concerns. In order to keep wages constant across employees and reduce wages for overtime workers, employers would need to reduce the implicit hourly rate of pay for employees who do not work overtime as well as those who do work

[188] For example: Bewley, T. (1999). Why Wages Don't Fall During a Recession. Cambridge, MA: Harvard University Press. Brown, C. & Medoff, J. (1989). The Employer Size Wage Effect. Quarterly Journal of Economics, 97(5), 1027-1059. See also the literature on implicit contracts in labor markets.

overtime. This would reduce total earnings for these non-overtime employees (potentially causing retention problems, productivity losses, and morale concerns).[189]

Therefore, the likely outcome will fall somewhere between the conditions predicted by the full overtime premium and employment contract models. For example, the implicit hourly rate of pay may fall, but not all the way to the wage predicted by the employment contract model, and overtime hours may fall but not be eliminated since the implicit hourly rate of pay has fallen. The Department conducted a literature review to evaluate how the market would adjust to a change in the requirement to pay overtime.

Barkume (2010) and Trejo (1991) empirically tested for evidence of these two competing models by measuring labor market responses to the application of FLSA overtime pay regulations.[190] Both concluded that wages partially adjust toward the level consistent with the employment contract model in response to the overtime pay provision.[191] Barkume found that employee wage rates were adjusted downward by 40 to 80 percent of the amount the employment contract model predicted, depending on modeling assumptions. Earlier research had demonstrated that in the absence of regulation some employers may voluntarily pay workers

---

[189] For example: Fehr & Schmidt. (2007). "A Theory of Fairness Competition and Cooperation." Quarterly Journal of Economics. Vol 97 No. 2 pp. 867-868. Milgram, Paul. (1988). "Employment Contracts Influence Activities and Efficient Organization Design." Journal of Political Economy, Vol. 96 No. 1 pp. 42-60.

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

[191] Since both papers were based on cross-sectional data, findings were assumed to be at the final equilibrium wages. However, studies showing wage contracts are likely to be stickier in the short run than in the long run have limited applicability here since this analysis deals exclusively with salaried workers seeing an increase in their weekly wage while seeing a downward adjustment in their implicit hourly wage rate, and they may be less aware of their implicit hourly wage rate. The Department has modeled a sticky adjustment process by assuming the wage elasticity of demand for labor is smaller in Year 1 than in subsequent years.

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.[192] Thus Barkume assumed that workers would receive an average voluntary overtime pay premium of 28 percent in the absence of an overtime pay regulation. Including this voluntary overtime pay from employers, he estimated that in response to overtime pay regulation, the wage adjusted downward by 80 percent of the amount that would occur with the employment contract model. Conversely, when Barkume assumed workers would receive no voluntary overtime pay premium in the absence of an overtime pay regulation, wages adjusted downward 40 percent of the amount the employment contract model predicted.[193,194] However, while 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.[195]

---

[192] 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.

[193] Barkume's estimates are consistent with Trejo's 1991 finding that the wage adjustment when there is no overtime premium was only about 40 percent of the full employment contract model adjustment. Trejo's estimates range from 25 percent to 49 percent and average 40 percent.

[194] Consider a worker earning $500 and working 50 hours per week. Assuming no overtime premium is paid the imputed hourly rate of pay is $10. Assuming a 28 percent overtime premium, the hourly rate of pay is $9.47 (($9.47 x 40 hours) + ($9.47 x 10 hours x 1.28))=$500. If the hourly rate of pay was fully adjusted to the employment contract model level when overtime pay is newly required, the hourly rate of pay would be $9.09 (($9.09 x 40 hours) + ($9.09 x 10 hours x 1.5))=$500. Forty percent of the adjustment from $10 to $9.09 results in an adjusted regular rate of pay of $9.64. Eighty percent of the adjustment from $9.47 to $9.09 results in an adjusted hourly rate of pay of $9.17. The Department took the average of these two adjusted wages to estimate that the resulting hourly rate of pay would be $9.40.

[195] Barkume (2010) based this assumption on the findings of Bell, D. and Hart, R. (2003). Wages, Hours, and Overtime Premia: Evidence from the British Labor Market. Industrial and

Comments Regarding Transfers

The few commenters who tried to model employer responses generally used or cited the same literature the Department used (in particular, Barkume (2010) and Trejo (1991)). Susann Rohwedder and Jeffrey B. Wenger conducted an analysis for RAND on the impacts of the rulemaking and, like our analysis, found small effects on individual workers' earnings and hours.[196]

Some organizations conducted surveys to evaluate how employers may respond. Although these surveys may be helpful as background information, they generally cannot be used in a quantitative analysis due to issues such as insufficient sample sizes, missing sampling methodology, and missing magnitudes. As an example of the last concern, the American Association of Orthopaedic Executives (AAOE) conducted a survey of their members and found "19% of respondents indicated that they would change the number of staff hours worked in order to avoid paying overtime." The Department agrees firms will generally change staffing hours and has included this in the quantitative analysis. The modeling question is to what degree employers will adjust hours.

Despite the inability to incorporate these survey results into the analysis, they may be informative and select results are presented here.

- The AAOE found "18% [of members] indicated that they would not change their current practice operations. 16% stated that they would increase salaries to the new threshold. 11%

Labor Relations Review, 56(3), 470-480. This study used 1998 data on male, non-managerial, full-time 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] 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.

would change the affected employees to hourly employees, and 4% stated that they would eliminate positions within their practice." This indicates employers will use a variety of mechanisms to reduce transfer payments, as discussed and modeled by the Department.

- The 2015 WorldatWork survey found "73% of respondents stated they would have more nonexempt employees."
- Kansas Bankers Association compiled member banks' analyses of the rule that found "[o]verwhelmingly … the response was not to increase the newly non-exempt salaries to continue to keep the position as an exempt position. In fact, only 2 bank CEOs responded that they would choose to do so. Rather, the overwhelming majority of bank CEOs stated those employees would move to non-exempt status, and overtime would be restricted or prohibited."
- The NAHB presented results from a member survey that found 33 percent of companies indicated a change in company policies, with respect to construction supervisors, would occur. Among those firms, "56% of respondents indicated that they would take steps to minimize overtime, such as cut workers hours."
- ANCOR found "[l]ess than a third of providers would be able to increase the salary of full-time exempt workers to meet the projected threshold."
- Society for Human Resource Management (SHRM) reported that, according to its survey "the most significant result identified was the implementation of restrictive overtime policies leading to potential reduction in employees working overtime, with 70 percent of respondents indicating that would be a likely outcome."
- AGC reported its survey found "74% of AGC-surveyed construction contractors responded that they would likely reclassify some or all of the impacted exempt workers to a non-exempt

hourly status at their current salaries. The survey results also show that: over 60% of respondents expect the proposed rule to result in the institution of policies and practices to ensure that affected employees do not work over 40 hours a week."

- International Public Management Association for Human Resources (IMPA-HR) and the International Municipal Lawyers Association reported from an IPMA-HR survey that "[a]bout 60% said they would convert currently exempt employees to non-exempt and pay them overtime while the same amount would prohibit them from working more than 40 hours per week without approval. Only 1/3 would raise salaries to at least $970 per week."
- National Association of Professional Insurance Agents asked survey respondents with workers who would be converted to nonexempt status and who work overtime whether they would decrease overtime hours; 65 percent responded they would.

Some commenters stated that many employers will respond by reducing hours and base wages more than the Department estimated. The National Association of Manufacturers wrote:

> While in the initial months following a reclassification, most employees tend to come out about the same in terms of total work and total compensation, the steady pressure of the overtime premium tends to result in a gradual reduction of the employee's schedule. The challenge for that employee is that the hourly rate does not normally increase to offset this loss in hours. Instead, the employer looks to give the work to other employees. The scaling back of the employee's weekly working hours can take a significant toll on the employee's earnings, especially given that the wages lost for each hour of overtime eliminated are at premium rates. The net economic effect of the Proposed Rule will be to take working hours and pay away from employees currently classified as exempt and redistribute those hours and pay to other employees.

Some commenters, including Jackson Lewis, the National RV Dealers Association, and the Sheppard Mullin law firm, asserted that many employers may follow the full employment contract model rather than the partial employment contract model used by the Department in the analysis. The Iowa Association of Community Providers wrote that "[i]n order to maintain current payroll budgets, the organizations will need to lower the hourly wages of non-exempt employees, such that their total annual compensation, including overtime payments, remains at the prior year's level." The Construction Industry Round Table asserted that "empirical research generally supports the 'fixed-job' model rather than the 'fixed-wage' model."

Other commenters stated that overtime will be reduced significantly more than the Department estimated in the NPRM. However, little data was provided to support these claims, making them difficult to incorporate into the analysis. For example, Audubon Area Community Services believes that "[b]ecause additional revenue is not an option, our agency would have to reclassify all but 10 of our positions to non-exempt with no overtime allowed by any staff."

The Department's reading and analysis of the literature cited in the rulemaking is that a result between the fixed-job model and the fixed-wage model would occur and thus we modeled our results accordingly. Specifically, based upon Barkume's findings regarding employer responses and transfer payments, we believe the partial employment contract model is most appropriate and consistent with the literature. Therefore, we have not changed the analysis. Several commenters commented on the literature we used to support using the partial employment contract model. The Center for American Progress expressed support for our use of Barkume's analysis and stated that this would result in some transfer payments since employers cannot fully adjust base wages. The Washington Center for Equitable Growth noted the Department "should make clear

that under certain conditions the fixed-wage model underlying [the Department's] analysis implies that some workers will see an increase in hours. If these workers are under-employed, the shift in the composition of those hours from over-worked to under-worked employees will be a welfare-improving consequence of the proposed rule."

Identifying Types of Affected Workers

The Department identified four types of workers whose work characteristics impact how employers were modeled to respond 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.
- Type 4: Workers who regularly work overtime. These workers differ from the Type 3 workers because it is less expensive for the employer to pay the updated salary level than pay overtime and incur managerial costs for these workers.[197]

The Department began by identifying the number of workers in each type. After modeling employer adjustments, transfer payments were then estimated. Type 3 and 4 workers are identified as those who regularly work overtime (CPS variable PEHRUSL1 greater than 40). These workers are divided between Type 3 and Type 4 depending on whether their weekly earnings are raised to the updated EAP salary level or they become nonexempt. Distinguishing Type 3 workers from Type 4 workers is a four step process. First we identify all workers who regularly work overtime. Then we estimate each worker's weekly earnings if they became nonexempt, to which we add weekly managerial costs for each affected worker of $3.53 ($42.31

[197] It is possible that employers will increase the salaries paid to some "occasional" overtime workers to maintain the exemption for the worker, but the Department has no way of identifying these workers.

per hour x (5 minutes/60 minutes)). Lastly, we identify as Type 4 those workers whose expected nonexempt earnings plus weekly managerial costs exceeds the updated standard salary level; those whose expected nonexempt earnings plus weekly managerial costs are less than the new standard salary level are classified as Type 3 workers. The Department assumes 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. Thus, it is appropriate to determine if the additional earnings plus the additional managerial costs for an affected worker exceed the revised salary level. In the NPRM managerial costs were not included in the determination of whether a worker is a Type 3 or Type 4 worker. Therefore, in this Final Rule there are somewhat more Type 4 workers than the NPRM methodology would yield.

Identifying Type 2 workers involves 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). These workers represent those who occasionally work overtime and happened to work overtime in that specific week. The survey (or reference) week is always the pay period that includes the 12th day of the month and contains responses for all twelve months. In a different week the identity of workers who work overtime might differ, but the number working overtime and the hours of overtime worked are similar because the survey week is representative of occasional overtime patterns.

The second step for identifying Type 2 workers in the Final Rule differs from the methodology used in the NPRM. In the NPRM, we used only the first step described above to identify Type 2 workers. Those who did not regularly work overtime and did not work overtime in the survey week were classified as Type 1 workers. As previously discussed, commenters

expressed concerns that the Department underestimated the number of workers who will experience changes in their wages or hours, and therefore that we underestimated costs, because managerial costs are a function of the number of workers who work overtime.

Therefore, for this Final Rule, the Department supplemented the CPS data with data from the Survey of Income and Program Participation (SIPP) in order 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 nonhourly workers worked overtime at some point in a year. Workers already identified as Types 2, 3, and 4, using the methodology in the NPRM, compose 24 percent of affected workers. Therefore, as a second step, 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 39.4 percent of affected workers were Type 2, 3, or 4. Therefore, the Department estimates fewer Type 1 workers and more Type 2 workers than in the NPRM.

Modeling Changes in Wages and Hours

In practice, employers do not seem to adjust wages of regular overtime workers to the full extent indicated by the employment contract model, and thus employees appear to get a small but significant increase in weekly earnings due to overtime pay coverage. Barkume and Trejo found evidence partially supporting both the employment contract model and the full overtime premium model in response to a 50 percent overtime premium requirement: a decrease in the regular rate of pay for workers with overtime (but not the full decrease to the employment contract model level) and a decrease in the amount of overtime worked. Therefore, when modeling employer responses with respect to the adjustment to the regular rate of pay, the

Department used a method that falls somewhere between the employment contract model and the full overtime premium model (i.e., the partial employment contract model).

Barkume reported two methods to estimate this partial employment contract wage, depending on the amount of overtime pay assumed to be paid in the absence of regulation. As noted above, the Department believes both the model assuming a voluntary 28 percent overtime premium and the model assuming no voluntary overtime premium are unrealistic for the affected population. Therefore, lacking more information, the Department determined that an appropriate estimate of the impact on the implicit hourly rate of pay for regular overtime workers after the Final Rule should be determined using the average of Barkume's two estimates of partial employment contract model adjustments: a wage change that is 40 percent of the adjustment toward the amount predicted by the employment contract 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.[198] 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 mid-point between 0 and 28 percent).

Modeling changes in wages, hours, and earnings for Type 1 and Type 4 workers is relatively straightforward. Type 1 affected EAP workers will become overtime eligible, but since they do

[198] 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 note that such an out-of-sample extrapolation has the potential to introduce uncertainty, just as there is uncertainty associated with other effects, such as the replacement of full-time jobs with part-time jobs, where studies have suggested directionally non-beneficial effects that are not statistically significant. Due to the lack of modeling results for salaried employees in the employment contract model, we do not attempt to quantify the magnitude of this uncertainty or potential overestimate.

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 the updated EAP salary level (either the standard salary level or HCE compensation level depending on which test the worker passed). These workers' earnings will increase by the difference between their current earnings and the amount necessary to satisfy the new standard salary requirement or comply with the new total annual compensation level. It is possible employers will increase these workers' hours in response to paying them a higher salary, but the Department has not modeled this potential change.[199]

Modeling changes in wages, hours, and earnings for Type 2 and Type 3 workers is more complex and uses findings from Barkume discussed above. The Department distinguishes those who regularly work overtime (Type 3 workers) from those who occasionally, or irregularly, work overtime (Type 2 workers) because employer adjustment to the Final Rule may differ accordingly. The Department believes that employers are more likely to adjust hours worked and wages for regular overtime workers because their hours are predictable. Conversely, it may be more difficult to adjust hours and wages for occasional overtime workers because employers may be responding to a transient, perhaps unpredicted, shift in market demand for the good or service they provide. In this case, it is likely advantageous for the employer to pay for this occasional overtime rather than to adjust permanent staffing. Additionally, the transient and possibly unpredicted nature of the change may make it difficult to adjust wages for these workers.

The Department treats Type 2 affected workers in two ways due to the uncertainty of the nature of these occasional overtime hours worked. If these workers work extra hours on an

[199] 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 we have chosen not to use her results for the quantification of the effect on hours of an increase in earnings.

unforeseen, short-term, as-needed basis (e.g., to adjust to unanticipated increases in demand), then there may be less opportunity for employers to adjust straight-time wages downward.[200] However, if these workers work extra hours on a foreseen, periodic basis (e.g., work a few extra hours one week each month, but workers do not consider it "regular overtime" because they do not work overtime during three weeks each month), then there may be some opportunity for employers to adjust straight-time wages downward (e.g., so pre- and post-revision monthly income is more similar). That this overtime is periodic and predictable is what makes it much more similar to that worked by Type 3 workers, and provides employers with more opportunity to adjust hours and wages. Since in reality there is likely a mix of these two occasional overtime scenarios, the Department combines models representing these two scenarios when estimating impacts.

Our estimate for how Type 2 workers are affected is based on the assumption that 50 percent of these workers who worked occasional overtime worked expected overtime hours and the other 50 percent worked unexpected overtime.[201] Workers were randomly assigned to these two

---

[200] Employers may be reluctant to reset hourly wage rates to respond to unexpected changes to the need for overtime because the negative impact on worker morale may outweigh the gains from adjusting wages to unexpected shifts in demand. Of relevance is the well-established literature that shows employers do not quickly adjust wages downward in response to downturns in the economy; the same logic applies to our approach to unexpected changes in demand. See, for example: Bewley, T. (1999). Why Wages Don't Fall During a Recession. Cambridge, MA: Harvard University Press. See also Barzel, Y. (1973). The Determination of Daily Hours and Wages. The Quarterly Journal of Economics, 87(2), 220-238.

[201] Trejo's and Barkume's adjustments are averages; excluding some workers (i.e., half of Type 2 workers) from these adjustments could potentially bias the size of the adjustment for the workers who continue to receive the adjustment. This bias would exist if Barkume and Trejo estimated the average adjustment for a sample of workers including irregular overtime workers and the size of the adjustment for these workers differs from other workers. It is not clear whether Trejo's and Barkume's samples include both occasional and regular overtime workers; however, the Department's interpretation is that Trejo includes only workers who usually work overtime and Barkume includes both. If these assumptions are correct, the magnitude of this RIA's adjustment made for the workers whose wages and hours are adjusted would be appropriate if it were

groups. Workers with expected occasional overtime hours were treated like Type 3 affected workers (partial employment contract 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 model). When modeling Type 2 workers' hour and wage adjustments, we treated those identified as Type 2 using the CPS data as representative of all Type 2 workers. We 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, we assume total transfers for the year are equal to 52 times the transfers estimated for the single representative week for which we have 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.[202,203]

Since Type 2 and Type 3 EAP workers work more than 40 hours per week, whether routinely or occasionally, they will receive an overtime premium based on their implicit hourly wage adjusted as described above. Because employers must now pay more for the same number of labor hours, they will seek to reduce those hours; in economics, this is described as a decrease in the quantity of labor hours demanded (a movement to the left along the labor demand curve). It

---

applying Trejo's results but may, due to applying Barkume's, result in an underestimate of the average fall in base wages. We believe the magnitude of any potential bias will be small because the half of Type 2 workers who are occasional, regular overtime workers in the CPS reference week (and thus treated differently) compose only 9 percent of Type 2 and Type 3 workers.

[202] Because these workers do not work overtime every week, the size of the wage and hour adjustments will be smaller than modeled. However, we are only modeling wage and hour adjustments for a subset of workers. If the wage and hour adjustments are linear, then our modeling assumptions should yield the same aggregate results as making smaller adjustments for all workers.

[203] 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.

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-run demand elasticity of -0.20 to estimate the percentage decrease in hours worked resulting from the increase in average hourly wages in Year 1, calculated using the adjusted base wage and the overtime wage premium.[204] The interpretation of the short run demand elasticity in this context is that a 10 percent increase in wages will result in a 2 percent decrease in hours demanded. Transfers projected for years 2 through 10 used a long-run elasticity; this is discussed in section VI.D.x.[205]

For Type 3 affected workers, and the 50 percent of Type 2 affected workers who worked expected overtime, we estimated adjusted total hours worked after making wage adjustments using the partial employment contract model. To estimate adjusted hours worked, we set the percent change in total hours worked equal to the percent change in average wages multiplied by the wage elasticity of labor demand.[206] The percent change in average wages is equal to the adjusted implicit average hourly wage minus the original implicit average hourly wage divided by the original implicit average hourly wage. The original implicit average hourly wage is equal

[204] 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 employment contract model. The Department invited comments on the appropriate elasticity to be used in this analysis, but no relevant comments were received.

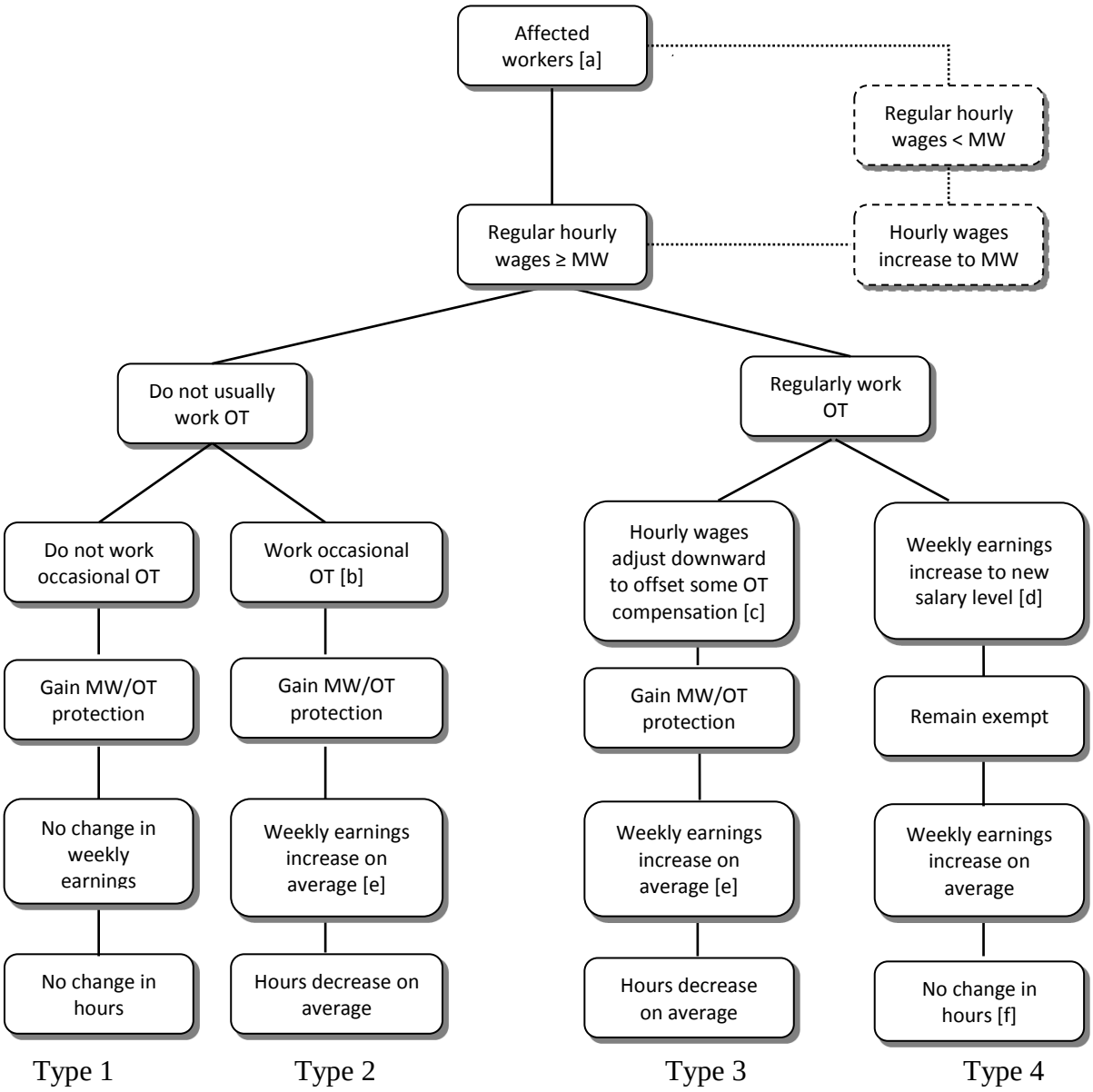
[205] In the short run not all factors of production can be changed and so the change in hours demanded is smaller than in the long run, when all factors are flexible.

[206] 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.

to original weekly earnings divided by original hours worked. The adjusted implicit average hourly wage is equal to adjusted weekly earnings divided by adjusted total hours worked. Adjusted weekly earnings equals the adjusted hourly wage (i.e., after the partial employment contract model adjustment) multiplied by 40 hours plus adjusted hours worked in excess of 40 multiplied by 1.5 times the adjusted hourly wage.

Figure 4 is a flow chart summarizing the four types of affected EAP workers. Also shown are the impacts on exempt status, weekly earnings, and hours worked for each type of affected worker.

Figure 4: Flow Chart of Final Rule's Impact on Earnings and Hours Worked



[a] Affected EAP workers are those who are exempt under the current EAP exemptions and would 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 employment contract model or the labor demand 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] This is what happens on average, although some employers may redistribute hours to reduce overtime, resulting in a decrease in some workers' overall earnings.
[f] 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.

Estimated Number of and Impacts on Affected EAP Workers

The Department projects 4.2 million workers will be affected by either (1) an increase in the standard salary level to the 40th percentile of weekly earnings of full-time salaried workers in the South because they earn salaries of at least $455 per week and less than $913 per week, or (2) an increase in the HCE compensation level to the 90th percentile of earnings of full-time salaried workers nationwide because they only pass the HCE duties test and earn at least $100,000 and less than $134,004 annually. These workers are categorized into the four "types" identified previously. There are 2.6 million Type 1 workers (60.4 percent of all affected EAP workers), those who work 40 hours per week or less and thus will not be paid an overtime premium despite their expected change in status to overtime protected (Table 19). The number of Type 1 workers decreased from the NPRM because some of these workers are now classified as Type 2 workers (as explained above). Type 2 workers, those who are expected to become overtime eligible and do not usually work overtime but do occasionally work overtime and will be paid the overtime premium, total 817,000 (19.3 percent of all affected EAP workers). Type 3 workers, those who regularly work overtime and are expected to become overtime eligible and be paid the overtime premium, are composed of an estimated 759,000 workers (17.9 percent of all affected EAP workers). The number of affected Type 4 workers was estimated to be 96,000 workers (2.3

percent of all affected workers); these are workers who the Department believes will remain exempt because firms will have a financial incentive to increase their weekly salaries to the updated salary and compensation levels, rather than pay a premium for overtime hours.[207]

Table 19: Affected EAP Workers by Type (1,000s), FY2017

	Total	No Overtime (T1)	Occasional Overtime (T2)	Regular Overtime	
				Newly Nonexempt (T3)	Remain Exempt (T4)
Standard salary level	4,163	2,523	815	730	95
HCE compensation level	64.9	32.5	2.7	28.5	1.2
Total	4,228	2,555	817	759	96

Note: Pooled data for FY2013-FY2015 projected to reflect FY2017.
*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. Paid overtime premium pay, so average weekly earnings increase, but regular rate of pay and hours fall for 50 percent of workers who regularly work occasional overtime.
*Type 3: Workers with regular OT who become overtime eligible. Paid overtime premium pay, so average weekly hours increase, but regular rate of pay and hours fall.
*Type 4: Workers with regular OT who remain exempt (i.e., earnings increase to the updated salary level).

The Final Rule will likely impact some affected workers' hourly wages, hours, and weekly earnings. Predicted changes in implicit wage rates are outlined in Table 20; changes in hours in Table 21; and changes in weekly earnings in Table 22. How these will change depends on the type of worker, but on average weekly earnings are unchanged or increase while hours worked are unchanged or decrease.

[207] As previously described, the Department calculated a wage and hour adjustment for all regular overtime workers. Consider, by way of example, a worker who initially earned $900 and worked 70 hours per week. Suppose the partial employment contract adjustment results in a regular rate of pay of $11.94 and 69.5 hours worked per week. After the partial employment contract adjustments, this worker would receive approximately $1,006 per week ((40 x $11.94) + (29.5 x ($11.94 x 1.5)). Since this is greater than the proposed standard salary level, the Department estimated that this worker would have his salary increased to $913 and remain exempt.

Type 1 workers will have no change in wages, hours, or earnings.[208] Estimating changes in the regular rate of pay for Type 3 workers and the 50 percent of Type 2 workers who regularly work occasional overtime requires application of the partial employment contract model, which predicts a decrease in their average regular rates of pay. The Department estimates that employers would decrease these workers' regular hourly rates of pay to the amount predicted by the partial employment contract model adjustment. Employers are 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 remaining 50 percent of Type 2 workers); therefore, their earnings will increase because they will receive the overtime premium for their unpredictable overtime hours. As a group, Type 2 workers currently exempt under the standard test would see a decrease in their average regular hourly wage (i.e., excluding the overtime premium) from $19.00 to $18.92, a decrease of 0.4 percent (Table 20). Type 2 workers paid between $100,000 and the updated HCE compensation level would see an average decrease in their regular hourly wage from $57.73 to $55.02, a decrease of 4.7 percent. However, because 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 would increase.[209]

Type 3 workers will also receive decreases in their regular hourly wage as predicted by the partial employment contract model. Type 3 affected workers paid below the new standard salary

[208] It is possible that these workers may experience an increase in hours and weekly earnings because of transfers of hours from overtime workers. 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.

[209] 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 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.

level would have their regular hourly rate of pay decrease on average from $14.51 to $13.74 per hour, a decrease of 5.3 percent. Type 3 workers paid between $100,000 and the new HCE compensation level would have their regular rate of pay decrease on average from $41.43 to $38.80 per hour, a decrease of 6.3 percent. Again, although regular hourly rates decline, weekly earnings will increase on average because these workers are now eligible for the overtime premium.

Type 4 workers' implicit hourly rates of pay would increase in order for their earnings to meet the updated standard salary level ($913 per week) or the updated HCE annual compensation level ($134,004 annually). The implicit hourly rate for Type 4 affected EAP workers who had earned at least $455 and below $913 per week would increase on average from $17.32 to $17.54 (a 1.3 percent increase). The implicit hourly rate of pay for Type 4 workers who had earned between $100,000 and $134,004 annually would increase on average from $49.97 to $50.76 (a 1.6 percent increase).

Table 20: Average Regular Rate of Pay by Type of Affected EAP Worker, FY2017

	Total	No Overtime (T1)	Occasional Overtime (T2)	Regular Overtime	
				Newly Nonexempt (T3)	Remain Exempt (T4)
Standard Salary Level					
Before Final Rule	$18.39	$19.36	$19.00	$14.51	$17.32
After Final Rule	$18.25	$19.36	$18.92	$13.74	$17.54
Change ($)	-$0.15	$0.00	-$0.08	-$0.77	$0.23
Change (%)	-0.8%	0.0%	-0.4%	-5.3%	1.3%
HCE Compensation Level					
Before Final Rule	$49.62	$56.13	$57.73	$41.43	$49.97
After Final Rule	$48.37	$56.13	$55.02	$38.80	$50.76
Change ($)	-$1.25	$0.00	-$2.72	-$2.63	$0.79
Change (%)	-2.5%	0.0%	-4.7%	-6.3%	1.6%

Note: Pooled data for FY2013-FY2015 projected to reflect FY2017.
*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. Paid overtime premium pay, so average weekly earnings increase, but regular rate of pay and hours fall for 50 percent of workers who regularly work occasional overtime.
*Type 3: Workers with regular OT who become overtime eligible. Paid overtime premium pay, so average weekly earnings increase, but regular rate of pay and hours fall.
*Type 4: Workers with regular OT who remain exempt (i.e., earnings increase to the updated salary level).

Type 1 and Type 4 workers would have no change in hours. Type 1 workers' hours would not change because they do not work overtime and thus the requirement to pay an overtime premium does not affect them. Type 4 workers' hours may increase, but due to lack of data, the Department assumed hours would not change. Half of Type 2 and all Type 3 workers would 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 base wage as predicted by the employment contract model.

Type 2 workers who work occasional overtime hours would be newly overtime eligible and would see a negligible decrease in average weekly hours in weeks where occasional overtime is worked (0.1 percent decrease) (Table 21).[210] This is the average change across all weeks, including weeks without overtime, in which the decrease in hours is zero. Type 2 workers who would no longer earn the updated HCE compensation level would see a decrease in average weekly hours in applicable weeks from 48.5 to 48.2 (0.5 percent). Type 3 workers affected by the increase in the standard salary level would see a decrease in hours worked from 50.8 to 50.3

[210] The Department estimates that half of Type 2 workers (those who work unpredictable overtime hours) will not see a reduction in their hours; however as a group, Type 2 workers are expected to experience a reduction in their hours of work. Because only half these workers experience a change in hours and because they work less overtime on average, the aggregate change is smaller than for Type 3 workers.

hours per week (0.8 percent). Type 3 workers affected by the increase in the HCE compensation level would see an average decrease from 52.4 to 52.0 hours per week (0.7 percent).

Table 21: Average Weekly Hours for Affected EAP Workers by Type, FY2017

	Total	No Overtime Worked (T1)	Occasional OT (T2)	Regular OT	
				Newly Nonexempt (T3)	Remain Exempt (T4)
Standard Salary Level [a]					
Before Final Rule	41.4	38.6	40.3	50.8	53.5
After Final Rule	41.3	38.6	40.3	50.3	53.5
Change ($)	-0.1	0.0	0.0	-0.4	0.0
Change (%)	-0.2%	0.0%	-0.1%	-0.8%	0.0%
HCE Compensation Level [a]					
Before Final Rule	45.5	39.0	48.5	52.4	51.1
After Final Rule	45.3	39.0	48.2	52.0	51.1
Change ($)	-0.2	0.0	-0.3	-0.4	0.0
Change (%)	-0.4%	0.0%	-0.5%	-0.7%	0.0%

Note: Pooled data for FY2013-FY2015 projected to reflect FY2017.
[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. Paid overtime premium pay, so average weekly earnings increase, but regular rate of pay and hours fall for 50 percent of workers who regularly work occasional overtime.
*Type 3: Workers with regular OT who become overtime eligible. Paid overtime premium pay, so average weekly earnings increase, but regular rate of pay and hours fall.
*Type 4: Workers with regular OT who remain exempt (i.e., earnings increase to the updated salary level).

Because Type 1 workers do not experience a change in their regular rate of pay or hours, they would have no change in earnings due to the Final Rule (Table 22). While their hours are not expected to change, Type 4 workers' salaries would increase to the new standard salary level or HCE compensation level (depending on which test they pass). Thus, Type 4 workers' average weekly earnings would increase by $12.70 (1.4 percent) for those affected by the change in the

standard salary level and by $41.58 per week (1.6 percent) for those affected by the HCE compensation level.

Although both Type 2 and Type 3 workers on average experience a decrease in both their regular rate of pay and hours worked, their weekly earnings are expected to increase as a result of the overtime premium. Based on a standard salary level of $913 per week, Type 2 workers' average weekly earnings increase from $751.47 to $760.11, a 1.1 percent increase. The average weekly earnings of Type 2 workers affected by the change in the HCE compensation level were estimated to increase from $2,778.65 to $2,836.63, a 2.1 percent increase. For Type 3 workers affected by the standard salary level, average weekly earnings would increase from $723.86 to $743.83, an increase of 2.8 percent. Type 3 workers affected by the change in the HCE compensation level have an increase in average weekly earnings from $2,136.91 to $2,196.10, an increase of 2.8 percent. Weekly earnings after the standard salary level increased were estimated using the new wage (i.e., the partial employment contract model wage) and the reduced number of overtime hours worked.

Table 22: Average Weekly Earnings for Affected EAP Workers by Type, FY2017

	Total	No Overtime (T1)	Occasional Overtime (T2)	Regular Overtime	
				Newly Nonexempt (T3)	Remain Exempt (T4)
Standard Salary Level [a]					
Before Final Rule	$733.65	$724.45	$751.47	$723.86	$900.30
After Final Rule	$739.13	$724.45	$760.11	$743.83	$913.00
Change ($)	$5.48	$0.00	$8.63	$19.97	$12.70
Change (%)	0.7%	0.0%	1.1%	2.8%	1.4%
HCE Compensation Level [a]					
Before Final Rule	$2,180.55	$2,155.94	$2,778.65	$2,136.91	$2,535.42
After Final Rule	$2,209.75	$2,155.94	$2,836.63	$2,196.10	$2,577.00
Change ($)	$29.19	$0.00	$57.98	$59.19	$41.58
Change (%)	1.3%	0.0%	2.1%	2.8%	1.6%

Note: Pooled data for FY2013-FY2015 projected to reflect FY2017.

[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. Paid overtime premium pay, so average weekly earnings increase, but regular rate of pay and hours fall for 50 percent of workers who regularly work occasional overtime.
*Type 3: Workers with regular OT who become overtime eligible. Paid overtime premium pay, so average weekly earnings increase, but regular rate of pay and hours fall.
*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 all affected workers is expected to increase from $733.65 to $739.13, a change of $5.48 (0.7 percent). However, these figures mask the impact on workers whose hours and earnings will change because Type 1 workers, who do not work overtime, make up more than 60 percent of the pool of affected workers. If Type 1 workers are excluded, the average increase in weekly earnings is $13.91 (1.9 percent). Multiplying the average change of $5.48 by the 4.2 million affected standard EAP workers equals an increase in earnings of $22.8 million per week or $1,187 million in the first year (Table 23). Of the weekly total, $660,000 is due to the minimum wage provision and $22.2 million stems from the overtime pay provision.

For workers affected by the change in the HCE compensation level, average weekly earnings increase by $29.19 ($57.57 if Type 1 workers, who do not work overtime, are excluded). When multiplied by 65,000 affected workers, the national increase in weekly earnings is $1.9 million per week, or $98.5 million in the first year. Thus, total Year 1 transfer payments attributable to this Final Rule total $1,285.2 million

Table 23: Total Change in Weekly and Annual Earnings for Affected EAP Workers by Provision, FY2017

Provision	Total Change in Earnings (1,000s)	
	Weekly	Annual
Total [a]	$24,715	$1,285,162
Standard salary level		
Total	$22,820	$1,186,646
Minimum wage only	$660	$34,338
Overtime pay only [b]	$22,160	$1,152,308
HCE compensation level		
Total	$1,895	$98,515
Minimum wage only	--	--
Overtime pay only [b]	$1,895	$98,515

[a] Due to both the minimum wage and overtime pay provisions and changes in both the standard salary level and the HCE compensation level.
[b] Estimated by subtracting the minimum wage transfer from the total transfer.

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.

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. For example, assume an exempt worker is paid for overtime hours at his regular rate of pay (not paid

the overtime premium but still acquires a benefit from each additional hour worked over 40 in a week). If the employer does not raise the worker's salary to the new level, requiring the overtime premium may cause the employer to reduce the worker's hours to 40 per week. If the worker's regular rate of pay does not increase, the worker will earn less due to the lost hours of work.

Additional Work for Some Workers

Affected workers who remain exempt will see an increase in pay but may also see an increase in workload as Emerge Center and other commenters noted. The Department estimated the net changes in hours, but as noted in section VI.D.iv.3, subpart Modeling Changes in Wages and Hours, did not estimate changes in hours for affected workers whose earnings increase (perhaps most notably those whose salary is increased to the new threshold so they remain overtime exempt).

Reduction in Bonuses and Benefits

Some commenters stated that employers may offset increased labor costs by reducing bonuses or benefits.[211] See, e.g., Greater Philadelphia Chamber of Commerce; Kentucky Society of CPAs; Michigan Association of Certified Public Accountants; Rockingham County, North Carolina. AGC stated that 40 percent of the members it surveyed expected affected employees to lose some fringe benefits. Other commenters, such as AIA-PCI, stated that employers would reduce bonus and incentive pay to newly overtime-eligible workers, offsetting some of the earnings gains achieved through overtime pay. NAHB presented results from a survey

[211] Other commenters asserted that some newly overtime-eligible employees will lose benefits that their employers tie to exempt status. See, e.g., CUPA-HR; National Association of Electrical Distributors; WorldatWork. As the Department explained in section IV.A.iv., we see no compelling reason why employers cannot change their compensation plans to provide such fringe benefits and bonus payments based upon, for example, the employees' job titles rather than based upon their exemption status.

conducted of members concerning overtime of construction supervisors, and stated that of the 33 percent of companies indicating that a change in company policies, with respect to construction supervisors, would occur, 55 percent reported they would "reduce or eliminate bonuses" and 33 percent indicated they would "reduce or eliminate other benefits." This results in approximately 18 percent of respondents predicting reduced bonuses and 11 percent predicting reduced benefits.

Commenters did not provide any data from which to estimate the potential magnitude of changes to benefits or bonuses. Therefore, the Department has not incorporated these impacts into the cost and transfer estimates. Furthermore, the Department believes if employers reduce benefits or bonuses, those reductions will occur instead of the full employer adjustments included in the model; that is, an employer who reduces benefits or bonuses is likely to reduce base wages by a smaller amount. The labor market will constrain to some extent employers' ability to reduce labor costs, regardless of the types of compensation they use to achieve those reductions.

v. 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, in response to commenter concerns that the rulemaking would have a disproportionate impact on low-wage regions and industries, the Department considers costs and transfers by region and by industry.

1. Bounds on Transfer Payments

Because the Department cannot predict employers' precise reaction to the Final Rule, the Department calculated bounds on the size of the estimated transfers from employers to workers

using a variety of assumptions. Since transfer payments are the largest component of this Final Rule, the scenarios considered here are bounds around the transfer estimate. Based on the assumptions made, these bounds do not generate bounded estimates for costs or DWL.

The potential upper limit for transfers occurs with the assumption that the demand for labor is completely inelastic, and therefore neither the implicit regular hourly rate of pay nor hours worked adjust in response to the changes in the EAP standard salary level and HCE annual compensation level. Under this assumption, employers pay workers one and a half times their current implicit hourly rate of pay for all overtime hours currently worked (i.e., the full overtime premium). The potential lower bound occurs when wages adjust completely and weekly earnings are unchanged as predicted by the employment contract model. The Department believes that both the upper bound scenario and the lower bound scenario are unrealistic; therefore, we constructed more credible bounds.

For a more realistic upper bound on transfer payments, the Department assumed that all occasional overtime workers and half of regular overtime workers would receive the full overtime premium (i.e., such workers would work the same number of hours but be paid 1.5 times their implicit initial hourly wage for all overtime hours). Conversely, in the preferred model the Department assumed that only 50 percent of occasional overtime workers and no regular overtime workers would receive the full overtime premium. For the other half of regular overtime workers, the Department assumed in the upper bound method that they would have their implicit hourly wage adjusted as predicted by the partial employment contract model (wage rates fall and hours are reduced but total earnings continue to increase, as in the preferred method). Table 24 summarizes the assumptions described above.

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 employment contract model (in the preferred method their wages adjust based on the partial employment contract model).[212] 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).

Table 24: 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% full EC model adj. 50% full overtime premium	50% partial EC model adj. 50% full overtime premium	100% full overtime premium
Regular Overtime Workers (Type 3)		
100% full EC model adj.	100% partial EC model adj.	50% partial EC model adj. 50% full overtime premium

* Full overtime premium: 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.
* Full employment contract (EC) 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 employment contract model) or (2) the minimum wage.
* Partial employment contract model: Regular rates of pay are partially adjusted to the wage implied by the employment contract model. The resulting regular rate of pay is the midpoint of: (1) a base wage that adjusts 40 percent of the way to the employment contract model wage level, assuming no overtime premium was initially paid and (2) a base wage that adjusts 80 percent of the way to the employment contract model wage level, assuming the workers initially received a 28 percent premium for overtime hours worked.

[212] 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.

The cost and transfer payment estimates associated with the bounds are presented in Table 25. Regulatory familiarization costs and adjustment costs do not vary across the scenarios. These employer costs are a function of the number of affected firms or affected workers, human resource personnel hourly wages, and time estimates. None of these vary based on the assumptions made above. Conversely, 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.[213] Depending on how employers adjust the implicit regular hourly wage, estimated transfers may range from $487.5 million to $2,525.3 million, with the preferred estimate equal to $1,285.2 million.

Table 25: Bounds on Year 1 Cost and Transfer Payment Estimates, FY2017 (Millions)

Cost/Transfer	Lower Transfer Estimate	Preferred Estimate	Upper Transfer Estimate
Direct employer costs			
Reg. familiarization	$272.5	$272.5	$272.5
Adjustment costs	$191.4	$191.4	$191.4
Managerial costs	$0.0	$214.0	$62.4
Total direct employer costs	$463.9	$677.9	$526.2
Transfers	$487.5	$1,285.2	$2,525.3

Note 1: Pooled data for FY2013-FY2015 projected to reflect FY2017.
Note 2: Estimates due to both the minimum wage and overtime pay provisions and changes in both the standard salary level and the HCE compensation level.

2. Impacts by Regions and Industries

In response to commenter concerns that the proposed standard salary level would disproportionately impact low-wage regions and low-wage industries, and requests for additional

[213] In the lower transfer estimate, managerial costs are zero because hours do not change for any Type 2 or Type 3 workers.

information on impacts by region and/or industry, this section presents estimates of the impacts of this Final Rule by region and by industry (see section IV.A.iv.).

PPWO asserted that the Department's probability codes demonstrate that the proposed salary level will disproportionately impact low-wage regions and industries. Specifically, PPWO cited a study that found 100 percent of first-line supervisors of food preparation and serving workers in Mississippi would fall below the new threshold, even though the Department's probability codes state that 10 to 50 percent of employees in this occupation should pass the duties test. The Department estimated based on CPS data for FY2013-FY2015 that about 20 percent of first-line supervisors of food preparation and serving workers in Mississippi in this industry will exceed the Final Rule salary threshold, while only 10 to 50 percent will pass the duties test, which shows the change in the Final Rule mitigates the impact on low-wage regions and industries. Similarly, the National Association of Home Builders (NAHB) analyzed state-level data and found that 50 percent or more of first line construction supervisors in Arkansas, Mississippi, New Mexico, and Tennessee would be affected by the Department's proposal. However, 55 percent of first line supervisors of construction trades and extraction workers in the South earn above the Final Rule's salary threshold, even though only 0 to 10 percent of such workers nationwide are likely to pass the standard duties test. Finally, the National Restaurant Association (NRA) noted, based on a 2014 study, that the median base salary paid to restaurant managers is $47,000 and to crew and shift supervisors is $38,000. As revised, the standard salary level in this Final Rule is approximately equivalent to the 2014 median base salary paid to restaurant managers cited by NRA.

The Department analyzed impacts to low wage regions by comparing the number of affected workers, costs, and transfers across the four Census Regions. The region with the most affected

workers is the South (1.7 million). However, as a share of potentially affected workers in the region, the South is not unduly affected relative to other regions (22 percent are affected compared with 16 to 19 percent in other regions); as a share of all workers in the region, the South is also not unduly affected relative to other regions (3.6 percent are affected compared with 2.7 to 3.2 percent in other regions).

Table 26: Potentially Affected and Affected Workers, by Region, FY2017

Region	Workers Subject to FLSA (Millions)	Potentially Affected Workers (Millions) [a]	Affected Workers			
			Number (Millions) [b]	Percent of Total Affected	Percent of Potentially Affected Workers in Region	Percent of All Workers in Region
All	132.8	22.5	4.2	100%	18.8%	3.2%
Northeast	24.8	4.8	0.8	18.6%	16.4%	3.2%
Midwest	29.5	4.7	0.9	20.8%	18.6%	3.0%
South	48.2	7.8	1.7	41.1%	22.2%	3.6%
West	30.2	5.1	0.8	19.5%	16.0%	2.7%

Note: Pooled data for FY2013-FY2015 projected to reflect FY2017.
[a] Potentially affected workers are EAP exempt workers who are white collar, salaried, not eligible for another (non-EAP) overtime exemption, and not in a named occupation.
[b] Estimated number of workers exempt under the EAP exemptions who would be entitled to overtime protection under the updated salary levels (if their weekly earnings do not increase to the new salary levels).

Total transfers in the first year were estimated to be $1.3 billion (Table 27). As expected, the transfers in the South are the largest portion because the largest number of affected workers is employed in the South. Transfers in the South were estimated to be about 36.5 percent of all transfers, while the South composes 41.1 percent of all affected workers (see section VI.D.ii.), thus, transfers per affected workers are somewhat below average in the South. Annual transfers per worker are $270 in the South and range from $242 to $378 in other regions. Excluding Type

1 workers, whose hours do not change, annual transfers per worker are $699 in the South and range from $664 to $1,004 in other regions.

Table 27: Transfers by Region, FY2017

Region	Total Change in Earnings (Millions) [a]	Percent of Total	Per Affected Worker
Total	$1,285.2	100%	$304.00
Northeast	$189.9	14.8%	$241.86
Midwest	$314.7	24.5%	$357.13
South	$469.3	36.5%	$269.96
West	$311.3	24.2%	$378.28

Note: Pooled data for FY2013-FY2015 projected to reflect FY2017.
[a] Due to both the minimum wage and overtime pay provisions and changes in both the standard salary level and the HCE compensation level.

Direct employer costs are composed of regulatory familiarization costs, adjustment costs, and management costs. Total first year direct employer costs were estimated to be $677.9 million (Table 28). Total direct employer costs were estimated to be the highest in the South ($259.6 million) and lowest in the Northeast ($123.0 million). While the three components of direct employer costs vary as a percent of these total costs by region, the percentage of total direct costs in each region is fairly consistent with the share of all workers in a region. Direct employer costs in each region as a percentage of the total direct costs were estimated to be 18.1 percent in the Northeast, 22.7 percent in the Midwest, 38.3 percent in the South, and 20.9 percent in the West. Once again, these proportions are almost the same as the proportions of the total workforce in each region: 18.5 percent in the Northeast, 22.0 percent in the Midwest, 36.7 percent in the South, and 22.8 percent in the West.

Table 28: Direct Employer Costs by Region, FY2017

Direct Employer Costs [a]	All Regions	Northeast	Midwest	South	West

Costs (Millions)					
Regulatory familiarization	$272.5	$52.6	$59.9	$95.7	$64.3
Adjustment	$191.4	$35.6	$39.9	$78.7	$37.3
Managerial	$214.0	$34.9	$54.1	$85.1	$39.9
Total direct costs	$677.9	$123.0	$153.9	$259.6	$141.5
Percent of Total Costs by Region					
Regulatory familiarization	100%	19.3%	22.0%	35.1%	23.6%
Adjustment	100%	18.6%	20.8%	41.1%	19.5%
Managerial	100%	16.3%	25.3%	39.8%	18.7%
Total direct costs	100%	18.1%	22.7%	38.3%	20.9%

Note: Pooled data for FY2013-FY2015 projected to reflect FY2017.
[a] All costs include both standard salary level costs and HCE compensation level costs.

Another way to compare the relative impacts of this Final Rule by region is to consider the transfers and costs as a proportion of current payroll and current revenues (Table 29). Nationally, direct employer costs are 0.010 percent of payroll. By region, direct employer costs as a percent of payroll are also approximately the same (between 0.009 and 0.012 percent of payroll). Direct employer costs as a percent of revenue are 0.002 percent nationally and in each region.

Transfers as a percent of payroll show greater variation among the regions than costs, but the levels are still very low. Transfers as a percent of payroll range from 0.013 percent in the Northeast to 0.023 percent in the Midwest. As a percent of revenue, transfers range from 0.003 to 0.004 percent. Thus, although there are some slight differences among regions, costs and transfers relative to either current payroll or revenue are less than a tenth of one percent. It is unlikely that a difference of 0.012 percent in costs and transfers as a percentage of payroll between the Northeast (0.022 percent—the lowest percentage) and the Midwest (0.034 percent—the highest percentage) would create any significant regional competitive advantage.

Several commenters expressed concern that this rulemaking will be more costly in low-wage regions due to lower revenue; for example, an individual commenter wrote "a restaurant in NYC taking in a million or more per year may not have any problem paying their manager or managers this proposed minimum salary. However a restaurant in a mid-west town that does say half that or $500,000 in sales, simply cannot afford such a salary." Similarly, the National Funeral Directors Association asserted the rule will "be much more disruptive for funeral homes in smaller rural communities where many of those family-owned businesses are already wrestling with lower revenue levels."

However, regional comparisons must incorporate more than a comparison of a single occupation: while revenues of a typical restaurant in NYC are higher than a typical restaurant in Milwaukee, so are costs including managers' salaries, other employees' wages, food costs and overhead, thus the relative ability of the NYC restaurant to increase managers' salaries might be more apparent than real. In addition, the Department has noted in our analysis that employers will adjust employees' earnings and hours to reduce the impact of the rule beyond the simple calculation of multiplying the overtime premium by the number of overtime hours worked. For example, in Table 22, the Department indicates that on average Type 3 workers will receive a less than three percent increase in weekly earnings. In the restaurant scenario described, this small increase in earnings applies to a fraction of the restaurant's labor force, which in itself is a fraction of total costs and revenues. Therefore, based on the above analysis, the Department does not believe low-wage regions will be unduly affected.

Table 29: Annual Transfers and Costs as Percents of Payroll and of Revenue by Region, FY2017

Region	Payroll	Revenue	Direct Employer Costs	Transfers

	(Billions)	(Billions)	As Percent of Payroll	As Percent of Revenue	As Percent of Payroll	As Percent of Revenue
Total	$6,524	$37,261	0.010%	0.002%	0.020%	0.003%
Northeast	$1,440	$7,492	0.009%	0.002%	0.013%	0.003%
Midwest	$1,393	$8,503	0.011%	0.002%	0.023%	0.004%
South	$2,171	$13,362	0.012%	0.002%	0.022%	0.004%
West	$1,520	$7,905	0.009%	0.002%	0.020%	0.004%

Notes: Pooled data for FY2013-FY2015 projected to reflect FY2017. 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 data from 2014 Annual Survey of Public Employment and Payroll. State and local revenue data from 2012 Census of Governments.

In order to gauge the impact of the final rule on industries, the Department compared estimates of combined direct costs and transfers as a percent of payroll, profits, and revenue, for the 13 major industry groups (Table 30).[214] This provides a common method of assessing the relative impacts 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 are highest in agriculture, other services, and leisure and hospitality. However, the overall magnitude of the relative shares are small, representing less than 0.1 percent of overall payroll costs across industries. The differences between industries are also small, with the range of

[214] Note that the totals in this table for transfers and direct costs 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.

values of total costs and transfers as a percent of payroll ranging from a low of .01 percent (public administration) to a high of 0.09 percent (agriculture).

The Department also estimates transfers and costs as a percent of profits.[215, 216] Benchmarking against profits is potentially helpful in the sense that it provides a measure of the Final Rule's effect against returns to 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 profits impacts reflecting cross-industry variation in market structure.[217] Nonetheless, the overall magnitude of costs and transfers as a percentage of profits are small, representing in all industries except one (transportation and utilities) less than 1.0 percent of overall profits. The differences between industries are also small, with the range of values of total costs and transfers as a percent of profits ranging from a low of .04 percent (financial activities) to a high of 1.46 percent (transportation and utilities).

Finally, the Department's estimates of transfers and costs as a percent of revenue by industry also indicate very small impacts (Table 30). The industries with the largest costs and transfers as a percent of revenue are leisure and hospitality and other services. However, the difference

---

[215] Internal Revenue Service. (2012). Corporation Income Tax Returns. Available at: https://www.irs.gov/pub/irs-soi/12coccr.pdf.

[216] Table 1 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.

[217] 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.

between the leisure and hospitality industry, the industry with the highest costs and transfers as a percent of revenue, and the industry with the lowest costs and transfers as a percent of revenue (public administration) is 0.02 percentage points. Table 30 illustrates that the actual differences in costs relative to revenues are quite small across industry groupings.

Table 30: Annual Transfers, Total Costs, and Transfers and Costs as Percent of Payroll, Revenue, and Profit by Industry, FY2017

Industry	Transfers (Millions)	Direct Costs (Millions)	Costs and Transfers		
			As Percent of Payroll	As Percent of Revenue	As Percent of Profit [a]
All	$1,282.70	$676.70	0.03%	0.01%	0.09%
Agriculture, forestry, fishing, & hunting	$4.10	$1.40	0.09%	0.02%	0.34%
Mining	$11.90	$3.50	0.02%	0.00%	0.08%
Construction	$50.20	$36.60	0.03%	0.01%	0.21%
Manufacturing	$125.60	$46.00	0.03%	0.00%	0.05%
Wholesale & retail trade	$248.50	$117.60	0.05%	0.00%	0.09%
Transportation & utilities	$44.50	$21.80	0.03%	0.01%	1.46%
Information	$48.90	$21.80	0.03%	0.01%	0.08%
Financial activities	$134.90	$79.60	0.03%	0.01%	0.04%
Professional & business services	$181.50	$113.30	0.02%	0.01%	0.14%
Education & health services	$183.70	$114.80	0.03%	0.01%	0.21%
Leisure & hospitality	$142.60	$57.40	0.07%	0.02%	0.40%
Other services	$71.60	$45.20	0.08%	0.02%	0.46%
Public administration	$34.80	$17.70	0.01%	0.00%	[b]

Sources: Private sector payroll and revenue data from 2012 Economic Census. State and local payroll data from 2014 Annual Survey of Public Employment and Payroll. State and local revenue data from 2012 Census of Governments. Profit to revenue ratios calculated from 2012 Internal Revenue Service Corporation Income Tax Returns.
[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 impacts from updating the standard salary level and the HCE compensation level do not unduly affect any of

the regions or industries. The proportion of total costs and transfers in each region is fairly consistent with the proportion of total workers in each region. Additionally, the 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 three-hundredths of a percent of revenue in each region and in each industry.

vi. Deadweight Loss

Deadweight loss (DWL) occurs when a market operates at less than optimal equilibrium output. This typically results from an intervention that sets, in the case of a labor market, wages above their equilibrium level. While the higher wage results in transfers from employers to workers, it also often causes a decrease in the total number of labor hours that are being purchased on the market. DWL is a function of the difference between the wage employers were willing to pay for the hours lost and the wage workers were willing to take for those hours. In other words, DWL represents the total loss in economic surplus resulting from a "wedge" between the employer's willingness to pay and the worker's willingness to accept. DWL may vary in magnitude depending on market parameters, but is typically small when wage changes are small or when labor supply and labor demand are relatively price (wage) inelastic. The estimate of DWL assumes the market meets the theoretical conditions for an efficient market in the absence of this intervention (e.g., all conditions of a perfectly competitive market hold: full information, no barriers to entry, etc.). Since labor markets are generally not perfectly competitive, the Department's estimate of DWL is likely an overestimate.

The DWL resulting from this Final Rule was estimated based on the average decrease in hours worked and increase in hourly wages calculated in section VI.D.iv. As the cost of labor rises due to the requirement to pay the overtime premium, the demand for overtime hours decreases,

which results in fewer hours of overtime worked. To calculate the DWL, the following values must be estimated:

- the increase in average hourly wages for affected EAP workers (holding hours constant),
- the decrease in average hours per worker, and
- the number of affected EAP workers.

Only 50 percent of Type 2 workers with overtime hours worked in the survey week (those who work regular or predictable occasional overtime) and Type 3 workers are included in the DWL calculation because the other workers either do not work overtime (Type 1), continue to work the same number of overtime hours (Type 4), or their employers are unable to adjust their hourly wage because their overtime hours worked are unpredictable (the other 50 percent of Type 2 workers). As described above, after taking into account a variety of potential responses by employers, the Department estimated the average wage change for affected EAP workers whose hours change. Workers impacted by the change in the standard salary level are considered separately from workers impacted by the change in the HCE compensation level.

For workers affected by the revised standard salary level, and who experience a change in hours, average wages (including overtime) will increase by $0.69 per hour prior to employer hour adjustments (Table 31). This represents the size of the wedge between labor supply and labor demand. Average hours will fall by 0.40 per week. These changes result in an average DWL of $0.14 per week per Type 2 (the 50 percent of CPS occasional overtime workers who work foreseeable overtime) and Type 3 worker. An estimated 803,500 workers will be eligible for the overtime premium on some of their hours worked each week after employer adjustments are taken into account. Multiplying the $0.14 per worker per week estimate by the number of affected workers results in a total DWL of $5.8 million in the first year of this Final Rule

attributable to the revised standard salary level (803,500 workers in DWL analysis x $0.14 per worker per week x 52 weeks).

For workers affected by the revised HCE compensation level and who experience a change in hours, the average hourly wage will increase by $2.01 and average hours worked will fall by 0.37 per week. This results in an average DWL of $0.38 per week for each of the estimated 31,200 workers affected by the compensation level who will see their hours fall. Multiplying this per worker estimate by the number of affected workers results in a DWL of $610,000 in the first year attributable to the HCE component of this Final Rule (31,200 workers in DWL analysis x $0.38 per worker x 52 weeks). Thus, total DWL is estimated to be $6.4 million in Year 1, which is small in comparison to the size of the costs and transfers associated with this proposal.[218]

Table 31: Summary of Deadweight Loss Component Values in Year 1

Component	Standard Salary Level	HCE Compensation Level
Average hourly wages (holding hours constant)		
Pre	$14.86	$42.84
Post	$15.55	$44.85
Change	$0.69	$2.01
Average overtime hours		
Pre	10.60	12.03
Post	10.20	11.65
Change	-0.40	-0.37

[218] Very few commenters addressed the Department's DWL calculation in the NPRM. The FL DEO derived their own estimate for deadweight loss in Florida, which if applied nationally would be significantly larger than the Department's DWL estimate. However, FL DEO did not explain how they arrived at their estimate, nor did they note any specific problems with our calculation. Therefore, the Department has not adjusted our DWL calculations. Additionally, FL DEO's concern that the Department's DWL estimate is too low because it is "only $1.58 per worker, per year" divides the DWL costs across all affected workers. If instead these costs are spread across only those workers whose hours or wages change, the cost per worker is larger.

Affected EAP workers	803,476	31,225
DWL		
DWL per worker per week	$0.14	$0.38
Total annual DWL (millions)	$5.78	$0.61

Note: DWL analysis is limited to workers who experience hour adjustments in the reference week (50 percent of Type 2 workers identified in the CPS and Type 3).

Some commenters expressed concern that the rulemaking will lead to a reduction in employment or an increase in unemployment. For example, the National Newspaper Association stated that 41 percent of surveyed members said the proposal would "lead to an overall loss of jobs in the community," and AGC reported 33 percent of surveyed members "expect some positions to be eliminated." See also Erie Sport Store; Michigan Federation for Children and Families; Texas Society of CPAs; Virginia Veterinary Medical Association. One small business owner wrote: "If I find that I am forced to pay additional money to my existing staff ... [m]y current employees will continue to work unwanted hours while another person continues to be unemployed." The Department acknowledges that by increasing the cost of labor, the total number of labor hours demanded is expected to fall. However, the Department has estimated the net decrease in labor hours to be small (334,000 hours per week in Year 1). We expect this reduction in hours to be largest for affected workers who presently work a significant amount of overtime and who will become nonexempt. We believe that most of the reduction in these employees' hours due to the increased marginal cost of their labor will be offset by increased hours for other workers. This may be in the form of hiring of additional staff or increased hours for part-time or exempt employees. By increasing the marginal cost of labor for newly overtime-eligible workers, employers have an incentive to avoid overtime hours worked by newly overtime-eligible workers, spreading work to other employees (which may increase employment), or making other production-related decisions. These effects may offset DWL,

and, as discussed later, may affect social welfare. However, we do not attempt to quantify those effects here.

If firms increase workers' pay to meet the new salary level, rather than paying overtime, however, then we may see these particular workers working longer hours to justify their increase in pay. This could consequently limit the spread of employment that is traditionally recognized as a goal of overtime laws. The Department acknowledges this may occur in some instances, however, we do not attempt to estimate transfers between workers due to uncertainty concerning the prevalence and magnitude of such transfers.

vii. Benefits and Effects Not Discussed Elsewhere

In general, benefits of the rulemaking were not quantified due to data limitations. However, these benefits are discussed qualitatively.

Market inefficiencies may be reflected in employees' choices concerning earnings and hours worked. These inefficiencies may result from the presence of information asymmetries,[219] labor market immobility, and other forms of labor market imperfection that lead to outcomes that differ from models that assume competitive labor markets. For example, empirical research by Wozniak and others[220] indicate that a variety of factors (e.g., educational endowment, exposure to local economic shocks early in work history, and lower earnings) are associated with less effective job search networks and lower labor market mobility. These may arise from a variety of sources, such as less sophistication in eliciting outside offers or less effective search

[219] Stiglitz, Joseph E. (2000) "The Contributions of the Economics of Information to Twentieth Century Economics", Quarterly Journal of Economics 115 (4): 1441-1478.

[220] Wozniak, Abigail (2010) "Are College Graduates More Responsive to Distant Labor Market Opportunities?" Journal of Human Resources 45(3): 994-970. Bound, John and Harry Holzer (200) "Demand Shifts, Population Adjustments, and Labor Market Outcomes during the 1980s" Journal of Labor Economics 18(1): 20-54. . Greenwoods, Michael, J (1997) "Internal Migration in Developed Countries" in Handbook of Population and Family Economics, ed Mark Rosenzweig and Oded Stark. New York: Elsevier Science.

heuristics. Salaried workers at the lower end of the compensation scale are more vulnerable to these inefficiencies than those at the higher end. Such workers are also more likely to be functioning in those parts of the labor market more impacted by trade, technological change, and other factors that may lead to a greater number of job seekers than job vacancies. Given these well documented market imperfections, tailored government intervention can result in social benefits. In a frictionless labor market, we would expect workers to find jobs where, at the margin, their compensation is equivalent to the value of their leisure time. However, labor market frictions of the sort discussed above diminish mobility and therefore lead to suboptimal outcomes for overtime exempt workers with few outside options, specifically, in them having excessive hours of work. In the presence of labor market friction, tailored government intervention can make these workers better off from a social welfare perspective.

1. Strengthening Overtime Protection for Other Workers

In addition to the 4.2 million affected EAP workers who will be newly eligible for overtime protection (absent employer response to increase the salary level to retain the exemption), overtime protection will be strengthened for an additional 8.9 million salaried workers who earn between the current salary level of $455 per week and the updated salary level of $913 per week. These workers, who were previously vulnerable to misclassification through misapplication of the duties test, will now be automatically overtime protected because their salaries fall below the new salary level and therefore they will not be subject to the duties test. These 8.9 million workers include:

• 5.7 million salaried white collar workers who are at particular risk of being misclassified because they currently pass the salary level test but do not satisfy the duties test; and

• 3.2 million salaried workers in blue collar occupations whose overtime protection will be strengthened because their salary will fall below the new salary threshold.[221] (Identification of blue collar workers is explained in section VI.B.iv).

Although these workers are currently entitled to minimum wage and overtime protection, their protection is better assured with the updated salary level. The salary level test is considered a bright-line test because it is immediately clear to employers and employees alike whether or not a worker passes the salary threshold. The duties test (which is the reason employers cannot currently claim the EAP exemption for the above workers) is more subjective and therefore harder to apply. An outdated salary level reduces the effectiveness of this bright-line test. At the new salary level, the number of overtime-eligible white collar salaried workers earning at or above the salary level will decrease by 5.7 million, and if we use our estimate of misclassification of 12.8 percent, then an estimated 732,000 of these workers are currently entitled to overtime protection but their employers do not recognize them as such. Therefore, increasing the salary level is expected to result in less worker misclassification. These reductions will have the greatest impact on workers concentrated in certain occupations and industries as shown in Table 10. Employers will be able to more readily determine their legal obligations and comply with the law. The resulting effects, although unquantified, would be categorized into costs (e.g., increased managerial effort), transfers (e.g., increased payments from employers to workers) and benefits in the same manner as effects are categorized in the analysis of EAP workers who will be newly eligible for overtime protection.

[221] Some workers in this group may be overtime exempt due to another non-EAP exemption.

2. Reduction in Litigation

Reducing the number of white collar employees for whom a duties analysis must be performed in order to determine entitlement to overtime will also reduce some types of litigation related to the EAP exemption. As previously discussed, employer uncertainty about which workers should be classified as EAP exempt has contributed to a sharp increase in FLSA lawsuits over the past decade. Much of this litigation has involved whether employees who satisfy the salary level test also meet the duties test for exemption. See, e.g, Soehnle v. Hess Corp., 399 F. App'x 749 (3d Cir. 2010) (gas station manager earning approximately $654 per week satisfied duties test for executive employee); Morgan v. Family Dollar Stores, Inc., 551 F.3d 1233 (11th Cir. 2008) (store managers earning an average weekly salary of up to $706 did not satisfy duties test for executive exemption).

Setting an appropriate salary level for the standard duties test, and maintaining the salary level with automatic updates, will restore the test's effectiveness as a bright-line method for separating overtime-protected workers from those who may be bona fide EAP workers, and in turn decrease the litigation risk created when employers must apply the duties test to employees who generally are not performing bona fide EAP work. This will vastly reduce legal challenges regarding the duties test for employees earning between the current salary level ($455) and the updated level ($913). See, e.g., Little v. Belle Tire Distribs., Inc., 588 F. App'x 424 (6th Cir. 2014) (applicability of administrative or executive exemption to tire store assistant manager earning $1,100 semi-monthly); Taylor v. Autozone, Inc., 572 F. App'x 515 (9th Cir. 2014) (applicability of executive exemption to store managers earning as little as $800 per week); Diaz v. Team Oney, Inc., 291 F. App'x. 947 (11th Cir. 2008) (applicability of executive duties test to pizza restaurant assistant manager earning $525 per week). Setting the salary level test at the 40th

percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region ($913) will alleviate the need for employers to apply the duties test in these types of cases, which is expected to result in decreased litigation as employers will be able to determine employee exemption status through application of the salary level test without the need to perform a duties analysis. See Weiss Report at 8 (explaining that the salary tests "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 International Association of Fire Fighters (IAFF) concurred, stating that "reducing the number of employees for whom the duties test must be applied will significantly reduce litigation related to the EAP exemption." Other commenters agreed that the proposed rule would make the exemption easier to apply, resulting in savings as a result of reduced litigation. See Comment from 57 labor law professors; American Federation of State, County and Municipal Employees; NELP. Another attorney, commenting on his own, similarly stated that the rule would reduce the potential for the misclassification of employees that often leads to litigation.[222]

The size of the potential social benefits from reducing litigation can be illuminated with the following estimation method. The Department estimated the share of FLSA cases that could potentially be avoided due to the revised salary levels. The Department used data from the U.S.

[222] Some commenters, including the National Association of Manufacturers and Jackson Lewis, expressed concern that the rulemaking will increase rather than decrease litigation costs because there will be a "spike in employees who were unhappy about being reclassified" and disputes about issues such as what is compensable time, the accuracy of time records, and compliance with rest/meal period requirements. See also Wage and Hour Defense Institute. As a number of employee advocates commented, and as the Department explained in section IV.A.iv., we disagree with these employer commenters, and believe an increased salary level that will once again serve as a clear and efficient line of demarcation will reduce litigation.

Court's Public Access to Court Electronic Records (PACER) system and the CPS to estimate the percent of FLSA cases that concern EAP exemptions and are likely to be affected by the final rule and data from a published study of the cost of civil litigation to determine the potential benefits of reduced litigation arising from the final rule.

In order to determine the potential number of cases that would be affected by the Final Rule, the Department obtained a list of all FLSA cases closed in 2014 from PACER (8,256 cases). From this list the Department selected a random sample of 500 cases. For each case in this sample, relevant information was reviewed and the Department identified the cases that were associated with the EAP exemption. The Department found that 12.0 percent of FLSA cases (60 of 500) were related to the EAP exemptions.[223] Next the Department determined what share of these cases could potentially be avoided by an increase in the standard salary level to $913 and an increase in the annual HCE compensation level to $134,004.

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 CPS to determine the share of potentially avoidable EAP cases where workers earn at least $455 but less than $913 per week or at least $100,000 but less than $134,004 annually. From CPS, the Department selected white collar, nonhourly workers as the appropriate reference group for defining the earnings distribution instead of exempt workers because of the simple fact that 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 35.8 percent of white collar nonhourly workers had earnings within these ranges. Applying these findings to the 12 percent of cases associated with

[223] It was not always clear whether the case involved the EAP exemption; when uncertain the Department classified the case as not being related to the EAP exemption to produce a conservative estimate. For example, in cases with multiple allegations (including both EAP and non-EAP issues) the Department classified the case as not being related to the EAP exemption.

the EAP exemption yields an estimated 4.3 percent of FLSA cases may be avoidable.[224] 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.[225]

After estimating the share of cases that might be avoidable, the Department quantified the associated benefit regarding the cost of litigation. The Department drew on a recent study conducted by the Court Statistics Project.[226] The study provides estimates of the costs of litigation related to employment cases, based on time for the various steps of the litigation process (e.g., case initiation, discovery, settlement, trial, etc.) and the costs of staff in providing these activities (e.g., paralegals, junior and senior attorneys, etc.). It then provides quartile estimates (25th percentile, median, and 75th percentile) based on the survey data. The study finds that the median cost for employment litigation is $88,000. Applying this figure, the Department estimated avoided litigation costs resulting from the rule may total approximately $31.2 million per year.[227]

---

[224] If we use the pool of all exempt workers as the reference group, then 32.8 percent of salaried workers earn within these income ranges and an estimated 3.9 percent of FLSA cases may be avoidable (32.8 percent x 12 percent).

[225] There are several reasons why this assumption may not hold. First, workers with lower earnings are less likely to pass the duties test, and thus may be more likely to be misclassified. This may result in an underestimate of the share of cases associated with workers earning between $455 and $913. Conversely, workers with higher earnings may be more likely to bring a lawsuit because lawyers may be more likely to take the case. This may result in an overestimate of the share of cases associated with workers earning between $455 and $913.

[226] Hannaford-Agor, P. and Waters, N. L. (2013). Estimating the Cost of Civil Litigation. Court Statistics Project, 20(1), 1-8. Additional data on the distribution of litigation costs can be found at www.ncsc.org/clcm.

[227] The cost of litigation is estimated to be $53,680 if the case does not go to trial; according to Court Statistics Project, 39 percent of litigation costs are associated with trials ($88,000 x (1-0.39)). Conversely, litigation costs might be significantly higher than estimated here since 25 percent of trial cases exceed costs of $210,800.

3. Uncertainty about Future Overtime Hours and Pay

This Final Rule may have an impact on newly overtime-protected employees who are not currently working much or any overtime, but who will now be entitled to minimum wage and overtime pay protections. These workers may face a lower risk of being asked to work overtime in the future, because they are now entitled to an overtime premium, which could reduce their uncertainty and improve their welfare if they do not desire to work overtime. Additionally, if they are asked to work overtime, they will be compensated for the inconvenience with an overtime premium.[228]

Economic theory suggests that workers tend to assign monetary values to risk or undesirable job characteristics, as evidenced by the presence of compensating wage differentials for undesirable jobs, relative to other jobs the worker can perform in the marketplace.[229] To the extent a compensating wage differential exists, compensation may decrease with the reduction in uncertainty.[230] For this reason, overall compensation would be expected to decrease for workers whose uncertainty decreases. Employees who prefer the reduced uncertainty to the wage premium would experience a net benefit of the rule, and employees who prefer the wage premium to the reduced uncertainty would experience a net detriment as a result of the rule. The Department believes that attempting to model the net monetary value of changes in

[228] Although this statement holds as a comparison between work hours below and above 40 per week, it is not universally valid as a comparison between the state of the world with the rule and the state of the world without the rule.

[229] For a discussion of compensating wage differentials, see Gronberg, T. J., & Reed, W. R. (1994). Estimating Workers' Marginal Willingness to Pay for Job Attributes using Duration Data. Journal of Human Resources, 29(3), 911-931.

[230] In this case, the size of the compensating wage differential is a function of the likelihood of working overtime and the amount of overtime worked. If the probability of working overtime is small then the wage differential may not exist.

uncertainty is not feasible due to its heavy reliance on data that are not readily available, and the potentially questionable nature of the resulting estimates.

4. Work-life Balance

Due to the increase in marginal cost for overtime hours for newly overtime-eligible workers, employers will demand fewer hours from some of the workers affected by this rule.[231] The estimated transfer payment does not take into account the benefit to some workers of working fewer hours in exchange for more (or equal) pay. Therefore, an additional potential benefit of this Final Rule is the increase in time off for some affected EAP workers. On average, affected EAP workers were estimated to work 4.7 minutes less per week after the Final Rule. The effect is much more pronounced when limited to just those workers whose hours are adjusted in a given week (the 50 percent of Type 2 workers who work occasional overtime and are identified in the CPS data and all Type 3 workers); they would on average work 24.0 minutes less per week after the Final Rule. The additional time off may potentially make these workers better off.

However, employers may respond to the rule by increasing hours of work for some other employees—especially those who pass the duties test and whose salaries are either already over the proposed threshold or will be adjusted to be so. For these employees, work-life balance may be harmed by the rule, in some cases without increased pay. For EAP employees whose work hours and pay are both reduced, they may seek second jobs in order to restore pay to its original level, thus similarly impacting work-life balance. The impact of this possible effect is unquantified.

[231] The Department recognizes that not all workers would prefer to work fewer hours and thus some of these workers might experience an adverse impact. The Department has no basis for estimating this potential negative impact.

Several commenters stated that by reducing excessive overtime the rule will improve work-life balance for employees. The Coalition on Human Needs asserted that one outcome of the proposed rule would be that "[e]mployers … will have to acknowledge the value of the 40-hour workweek by … limiting workers['] [hours], thus giving them more time with their families." See also Center for American Progress; EPI. According to the Center for Effective Government "[the] proposed rule would provide more time protections to the parents of over an estimated 9 million children."[232]

Empirical evidence shows that workers in the United States typically work more than workers in other comparatively wealthy countries.[233] Although estimates of the actual level of overwork vary considerably, executive, administrative, and professional occupations have the highest percentage of workers who would prefer to work fewer hours compared to other occupational categories.[234] Therefore, the Department believes that the Final Rule may result in increased time off for a group of workers who may prefer such an outcome. However, the empirical evidence does not allow us to estimate how many workers would prefer fewer hours or how much workers value this additional time off, so it is difficult to monetize the benefit they may receive.

Furthermore, not all workers would prefer to work fewer hours and thus some of these workers might experience an adverse impact. In addition, the estimated work loss represents an

---

[232] Conversely, some commenters believe the rule will hurt work-life balance because workers who become nonexempt may lose flexibility in setting their schedules (see section IV.A.iv.)
[233] For more information, see OECD series, average annual hours actually worked per worker, available at: http://stats.oecd.org/index.aspx?DataSetCode=ANHRS.
[234] Hamermesh, D.S., Kawaguchi, D., Lee, J. (2014). Does Labor Legislation Benefit Workers? Well-Being after an Hours Reduction. IZA DP No. 8077.
Golden, L., & Gebreselassie, T. (2007). Overemployment Mismatches: The Preference for Fewer Work Hours. Monthly Labor Review, 130(4), 18-37.
Hamermesh, D.S. (2014). Not Enough Time? American Economist, 59(2).

average over all affected workers, and some workers may experience a larger reduction in hours.[235]

5. Health

Working long hours is correlated with an increased risk of injury or health problems.[236] Therefore, by reducing overtime hours, some affected EAP workers' health may improve. This would benefit the workers' welfare, their families' welfare, and society since fewer resources would need to be spent on health. Health has also been shown to be highly correlated with productivity.[237] Some affected employees who work large amounts of overtime may see a significant health impact; for example, workers at the 75th and 90th percentiles of hours worked report working 15 and 20 hours of overtime hours per week, respectively. On average, 25 percent of currently exempt employees who work overtime work at least 10 hours of overtime per week. EPI, NELP, and other commenters noted the poor health effects of working long hours. The beneficial health effects of reduced hours for some newly overtime-eligible employees may be partially offset to the extent that hours worked by other employees, especially those who are overtime exempt, increase. These effects have not been quantified.

---

[235] It is possible that some employers may choose to eliminate all overtime for affected workers and hire additional workers or spread the work to existing employees to replace the lost hours. The potential for this adjustment is uncertain, and the Department has found no studies that estimate the potential magnitude of this effect. In addition, an employer may be limited in his or her ability to make such adjustments; many affected employees work only a few hours of overtime each week; affected employees' tasks may not be easily divisible; and hiring new workers and/or managing different work flows will impose additional costs on the employer that will offset the savings from avoiding paying the overtime premium.

[236] Keller, S. M. (2009). Effects of Extended Work Shifts and Shift Work on Patient Safety, Productivity, and Employee Health. AAOHN Journal, 57(12), 497-502. Kivimäki, M. (2015). Long Working Hours and Risk of Coronary Heart Disease and Stroke: A Systematic Review and Meta-Analysis of Published and Unpublished Data for 603,838 Individuals. The Lancet, 386(10005), 1739-1746.

[237] Loeppke, R., Taitel, M., Richling, D., Parry, T., Kessler, R., Hymel, P., et al. (2007). Health and Productivity as a Business Strategy. Journal of Occupational and Environmental Medicine, 49(7), 712-721.

6. Increased Productivity

This Final Rule is expected to increase the marginal cost of some workers' labor, predominately due to the overtime pay requirement since almost all affected EAP workers already earn the federal minimum wage. In light of the increased marginal cost of labor for newly overtime-eligible workers, employers may organize workers' time more efficiently, thus increasing productivity. Other channels that may increase marginal productivity include: worker health (which was addressed above), reduced turnover, and other effects described by efficiency wage theory. Any such net gains would benefit both employers and workers.

Efficiency wages: By increasing earnings this Final Rule may increase a worker's productivity by incentivizing the worker to work harder. Thus the additional cost to firms may be partially offset by higher productivity. In particular, the estimated managerial costs associated with greater monitoring effort may be offset due to this effect. A strand of economic research, commonly referred to as "efficiency wages," considers how an increase in wages may be met with greater productivity.[238] However, this literature tends to focus on firms voluntarily paying higher wages, and thus distinguishing themselves from other firms. Because employer response to this rulemaking will result in wage increases, extrapolating from efficiency wage theory may not be appropriate to estimate the likely effects of the rule.

Some commenters discussed increased productivity as a benefit of the rulemaking, including the AFL-CIO, the American Federation of Teachers, and the IAFF. Individual comments submitted by the National Women's Law Center asserted that paying workers well "will lead to increased productivity, employee loyalty and less worker turn-over" and stated that "the better you treat employees the better the quality of the work they produced."

[238] Akerlof, G. A. (1982). Labor Contracts as Partial Gift Exchange. The Quarterly Journal of Economics, 97(4), 543-569.

Conversely, there are channels through which increasing overtime pay may reduce productivity. For example, some overtime hours may be spread to other workers. If the work requires significant project-specific knowledge or skills, then the new worker receiving these transferred hours may be less productive than the first worker, especially if there is a steep learning curve. However, having another worker versed in the project may be beneficial to the firm if the first worker leaves the firm or is temporarily absent (e.g., sick) or by providing benefits of teamwork (e.g., facilitating information exchange).[239] The relative magnitudes of rule-induced increases and decreases in productivity have not been quantified.

Reduction in turnover: Research demonstrates a correlation between earnings and employee turnover—as earnings increase, employee turnover decreases.[240,241] Reducing turnover may increase productivity, at least partially because new employees have less firm-specific capital (i.e., skills and knowledge that have productive value in only one particular company) and thus are less productive and require additional supervision and training.[242] In short, replacing experienced workers with new workers decreases productivity, and avoiding that will increase productivity. Reduced turnover should also reduce firms' hiring and training costs. As a result, even though marginal labor costs rise, they may rise by less than the amount of the wage change

---

[239] Some commenters believe productivity would decline. See section VI.D.iii.

[240] Howes, Candace. (2005). Living Wages and Retention of Homecare Workers in San Francisco. Industrial Relations, 44(1), 139-163. Dube, A., Lester,T.W., & Reich, M.. (2014). Minimum Wage Shocks, Employment Flows and Labor Market Frictions. IRLE Working Paper #149-13.

[241] Note that this literature tends to focus on changes in earnings for a specific sector or subset of the labor force. The impact on turnover when earnings increase across sectors (as would be the case with this regulation) may be smaller.

[242] Argote, L., Insko, C. A., Yovetich, N., & Romero, A. A. (1995). Group Learning Curves: The Effects of Turnover and Task Complexity on Group Performance. Journal of Applied Social Psychology, 25(6), 512–529. Shaw, J. D. (2011). Turnover Rates and Organizational Performance: Review, Critique, and Research Agenda. Organizational Psychology Review, 1(3), 187-213.

because the higher wages may be offset by lower turnover rates, increased productivity, and reduced hiring costs for firms.

It is difficult to estimate the impact of reduced turnover on worker productivity and firm hiring costs. The potential reduction in turnover is a function of several variables: the current wage, hours worked, turnover rate, industry, and occupation. Additionally, estimates of the cost of replacing a worker who quits vary significantly. Therefore, the Department does not quantify the potential benefit associated with a decrease in turnover attributed to this Final Rule.

7. Reduction in Social Assistance Expenditures

The transfer of income resulting from this Final Rule may result in reduced need for social assistance (and by extension reduced social assistance expenditures by the government). A worker earning the current salary level of $455 per week earns $23,660 annually. If this worker resides in a family of four and is the sole earner, then the family will be considered impoverished. This makes the family eligible for many social assistance programs. Thus, transferring income to these workers may reduce eligibility for government social assistance programs and government expenditures. Several commenters, including Court Appointed Special Advocates and some individual commenters, agreed that the rulemaking would reduce unemployment insurance and social welfare costs.

Benefits for which currently exempt EAP workers may qualify include Medicaid, the Supplemental Nutrition Assistance Program (SNAP), the Temporary Assistance for Needy Families (TANF) program, the Special Supplemental Nutrition Program for Women, Infants, and Children (WIC), and school breakfasts and lunches.[243] Quantifying the impact of this Final Rule

[243] Earned Income Tax Credit (EITC) expenditures could either increase or decrease depending on whether workers are on the "phase-in" or the "phase-out" portion of the EITC-eligibility profile.

on government expenditures is complex and thus not estimated here. In order to conduct such an analysis, the Department would need estimates of the transfer per worker, (as noted earlier in this analysis, these estimates average $13.91 per week across affected workers who work overtime and $5.48 across all affected workers), his or her current income level, other sources of family income, number of family members, state of residence, and receipt of aid.

8. Employment Spreading

Because employers will have an incentive to reallocate excessive overtime hours in some cases (for instance, amongst employees who work so many hours that any increase would lead to minimum wage violations), the Final Rule may result in expanded employment opportunities. Several commenters predicted such an expansion. The Society of St. Vincent de Paul stated that that there will be positive spillover effects that will result in "opportunities for new employment for others to fill the hours previously treated as non-compensable but mandatory managerial duties." The Washington Center for Equitable Growth commented that the Department understated the benefits of the rulemaking "by failing to account for employers' tendency to hire additional workers and to schedule non-overtime work in response to the rule change."

Two estimates of job creation were referenced by commenters. The Washington Center for Equitable Growth referenced an analysis by Goldman Sachs estimating the impact of the proposed change in the standard salary level on employment.[244] Goldman Sachs concluded that an increase in the salary threshold from $455 to $970 would result in a total of 120,000 new hires.[245] Legal Aid Society-Employment Law Center referenced a publication by the NRF

[244] Goldman Sachs. (2015). US Daily: The New Federal Overtime Rules: A Greater Effect on Payrolls than Pay.

[245] Goldman Sachs based its analysis on a difference-in-difference-in-difference (DDD) estimate of the impact of the 2004 regulation. This method assumes the 2004 salary level change is comparable to the proposed salary level change, the short duties test is similar to the standard

which, relying on data from Oxford Economics, estimated that a salary threshold of $970 per week would create 117,100 part-time jobs in the retail industry alone.[246] While the Department has some concerns with Oxford Economics' analysis, as discussed in section VI.D.iii., we agree that in some instances employers may hire additional employees to work hours previously worked by newly nonexempt employees. However, as noted earlier, to the extent the individuals hired for the new jobs are already employed elsewhere, the number of individuals who are employed may not increase by as much as the number of jobs increases. Further, to the extent that employers shift overtime hours of newly overtime-eligible employees to part-time or overtime exempt employees who are already on staff, hiring will not increase.

9. Macroeconomic Benefits

Several commenters asserted that the regulations will benefit the economy as a whole. United Steel Workers stated that "[w]hen the workers have more money to spend, businesses have more customers and more incentive to hire and invest." Democracy for America commented the proposed rule "would go a long way in addressing [wage] disparity, strengthening our economy by providing more income to households that they can turn around and spend at businesses, creating new jobs and growing our GDP." There are potential secondary effects (both costs and benefits) of the transfer due to the potential difference in the marginal utility of income and the marginal propensity to consume between workers and business owners. The transfer may result in societal gain during periods when the economy is operating below potential to the extent that transferring income to workers with a relatively high marginal propensity to consume results in a

---

duties test, and all reduced hours will be transferred to new hires. Accordingly, the Department did not conduct a similar analysis in this Final Rule.

[246] National Retail Federation. (2015). The Hidden Cost Of Overtime Expansion.

larger multiplier effect and impact on GDP. The Department did not attempt to quantify these potential impacts.

viii. Regulatory Alternatives

The Department has chosen to update the standard salary level to the 40th percentile of weekly earnings of all full-time salaried workers in the South. As previously discussed, the Department considered a range of alternatives before selecting this methodology and data set. Table 32 presents the alternative salary and compensation levels, the number of affected workers, and the associated costs and transfers. Regulatory familiarization costs are not included because they do not vary over the alternatives.

Alternative 1 inflates the 2004 standard salary level ($455) to FY2015 dollars using the CPI-U. This is $570 per week. At this salary level 538,000 workers would be affected in Year 1, imposing direct adjustment and managerial costs of $47.9 million, transferring $111.4 million in earnings from employers to employees, and resulting in DWL of $0.4 million. Alternative 2 sets the salary level using the 2004 Final Rule method (the 20th percentile of weekly earnings of full-time salaried workers in the South and retail), resulting in a salary level of $596 per week. At this salary level 683,000 workers would be affected in Year 1, imposing direct adjustment and managerial costs of $61.3 million, transferring $145.4 million in earnings from employers to employees, and resulting in DWL of $0.5 million. Alternative 3 uses the salary level based on the Kantor method for the long duties test, resulting in a level of $684 per week. At this salary level 1.4 million workers would be affected in Year 1, imposing direct adjustment and managerial costs of $133.7 million, transferring $318.1 million in earnings from employers to employees, and resulting in DWL of $1.6 million.

Alternative 4 uses the methodology proposed in the NPRM, setting the standard salary level at the 40th percentile of weekly earnings of full-time salaried workers nationally. For the fourth quarter of 2015 this yields a salary level of $972 per week. At this salary level 4.8 million workers would be affected; Year 1 adjustment and managerial costs would equal $470.1 million, with transfers of $1.5 billion, while DWL would equal $7.3 million. Alternative 5 sets the salary level using the Kantor long test method but generates a level more appropriate to the short duties test by multiplying the result times the average historical ratio between the short and long test salary levels (as explained in section VI.C.iii.). This results in a salary level of $1,019 per week. At this salary level, 5.6 million workers are affected, Year 1 adjustment and managerial costs are $541.2 million; Year 1 transfers are $1.8 billion; and Year 1 DWL is $8.4 million. Alternative 6 inflates the 1975 short duties test salary level using the CPI-U to $1,100 per week in FY2015 dollars. At this salary level, 6.7 million workers are affected; Year 1 adjustment and managerial costs are $665.4 million; Year 1 transfers are $2.4 billion; and Year 1 DWL is $11.7 million.

The Department also examined alternatives to the HCE compensation level. HCE alternative 1 left the current $100,000 annual compensation level unchanged. Therefore, no employer costs, transfers, or DWL are associated with this alternative. HCE alternative 2 inflates the 2004 level using the CPI-U and sets the HCE annual compensation level at $125,320 per year. This compensation level would affect 56,000 workers in Year 1 (compared to 65,000 at the chosen compensation level), impose adjustment and managerial costs on employers of $6.7 million, transfer $72.2 million in earnings from employers to employees, and generate $400,000 in DWL. HCE alternative 3 sets the HCE annual compensation level at $149,894 per year, based upon using the same percentile of full-time salaried workers as in the 2004 Final Rule. This compensation level would affect 72,000 workers in Year 1, impose adjustment and managerial

costs on employers of $9.4 million, transfer $123.0 million in earnings from employers to employees, and generate $800,000 in DWL.

Table 32: Updated Standard Salary and HCE Compensation Levels and Alternatives, Affected EAP Workers, Costs, and Transfers, FY2017

Alternative	Salary Level	Affected EAP Workers (1,000s)	Year 1 Impacts (Millions)		
			Adj. & Managerial Costs [a]	Transfers	DWL [b]
Standard Salary Level (Weekly)					
Alt. #1: Inflate 2004 level	$570	538	$47.9	$111.4	$0.4
Alt. #2: 2004 method	$596	683	$61.3	$145.4	$0.5
Alt. #3: Kantor long test level	$684	1,444	$133.7	$318.1	$1.6
Final	$913	4,163	$397.0	$1,186.6	$5.8
Alt. #4: Proposed	$972	4,837	$470.1	$1,476.8	$7.3
Alt. #5: Kantor short test	$1,019	5,636	$541.2	$1,779.3	$8.4
Alt. #6: Inflate 1975 short test level	$1,100	6,684	$665.4	$2,418.8	$11.7
HCE Compensation Level (Annually)					
Alt. #1: No change	$100,000	0	--	--	--
Alt. #2: Inflate 2004 level	$125,320	56	$6.7	$72.2	$0.4
Final	$134,004	65	$8.4	$98.5	$0.6
Alt. #3: 2004 percentile	$149,894	72	$9.4	$123.0	$0.8

Note: Pooled data for FY2013-FY2015 projected to reflect FY2017.

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

[b] DWL was estimated based on the aggregate impact of both the minimum wage and overtime pay provisions. Since the transfer associated with the minimum wage is negligible compared to the transfer associated with overtime pay, the vast majority of this cost is attributed to the overtime pay provision.

ix. Automatic Updates

1. Background

Between periodic updates to the salary level, nominal wages typically increase, resulting in an increase in the number of workers qualifying for the EAP exemption, even if there has been no

change in their duties or real earnings. Thus, workers whom Congress intended to be covered by the minimum wage and overtime pay provisions of the FLSA may lose those protections. Automatically updating the standard salary level allows this threshold to keep pace with changes in earnings, allowing it to continue to serve as an effective dividing line between potentially exempt and nonexempt workers. Furthermore, automatically updating the standard salary level and the HCE compensation level will provide employers more certainty in knowing that these levels will change by a small amount on a regular basis, rather than the more disruptive increases caused by much larger changes after longer, uncertain increments of time. This will allow firms to better predict short- and long-term costs and employment needs.

In this Final Rule, the Department is including in the regulations a mechanism for automatically updating the salary levels every three years. The Department will reset the standard salary level to keep it at the 40th percentile of weekly wages of full-time salaried workers in the lowest-wage Census Region (currently the South). The HCE annual compensation level will be updated to keep it at the 90th percentile of weekly wages of full-time salaried workers nationally.

2. Updating Methods Considered

In the NPRM the Department sought comments on whether to automatically update the standard salary level and HCE total compensation level using the Consumer Price Index for All Urban Consumers (CPI-U), or using a fixed percentile of earnings. The CPI-U is the most commonly used price index in the U.S. and is calculated monthly by BLS. The CPI-U is the primary index used by the government to index benefit payments, program eligibility levels, and tax payments. The CPI-U holds quantities constant at base levels while allowing prices to

change. The quantities are fixed to represent a "basket of goods and services" bought by the average consumer.

Updating the salary levels based upon the growth rate of earnings at a specified percentile of the weekly earnings distribution is consistent with the Department's historical practice of using salary level as a key criterion for the exemption. The growth rate of earnings reflecting labor market conditions is an appropriate measure of the relative status, responsibility, and independence that characterize exempt workers. While earnings and prices generally mirror one another over time, they do not change in tandem.

3. Comparison of Indices and Decision to Use Earnings Percentiles

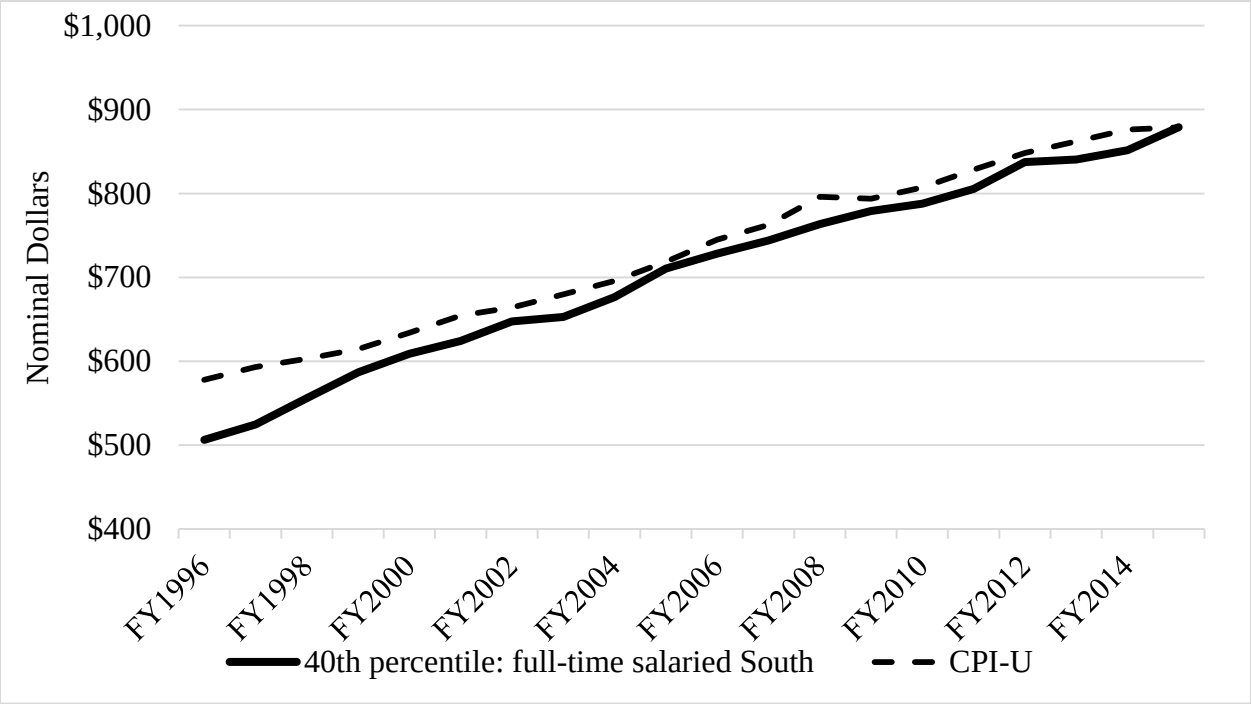
As previously discussed, see section IV.E.iii., the Department believes setting and updating the salary level using the same methodology will best ensure that the salary level test effectively differentiates between overtime-eligible white collar workers and workers who may be bona fide EAP employees who are not entitled to overtime and continues to work effectively with the duties test. Accordingly, the Final Rule provides for updating both the standard salary level and the HCE total compensation requirement using a fixed percentile of weekly earnings (40th percentile of full-time workers in the lowest-wage Census Region for the standard salary level; the annualized value of the 90th percentile of full-time salaried workers nationally for the HCE total compensation level).

While the Department has decided not to automatically update the salary level using the CPI-U, we note that in recent years the CPI-U has grown at a rate closely aligned with the 40th percentile of earnings of full-time salaried workers in the South. Between FY2006 and FY2015 the average annual growth rates for the 40th percentile in the South and the CPI-U have been 2.1

percent and 1.8 percent, respectively. The average growth rate at the 90th percentile of full-time salaried earnings nationwide during the same period was 3.0 percent.

The Department compared the standard salary levels that would have resulted from 1995 to 2015 if (1) the standard salary level was set each year to the 40th percentile of weekly earnings of full-time salaried workers in the South, and (2) the standard salary level was set using the growth in the CPI-U (and setting the level in 2014 to match the 40th percentile earnings level in the South, i.e., $913 per week) (Figure 5). While not identical, the data show that these two methods produced similar results.

Figure 5: Estimated Historical Standard Salary Level with Automatic Updating, FY1996-FY2015



4. Concerns with Use of Fixed Earnings Percentile as Automatic Updating Methodology

As discussed in detail in section IV.E.iii., some commenters expressed concern that automatically updating the salary level using a fixed percentile of earnings would result in the

salary levels growing at too quick a rate. See, e.g., American Bankers Association; AIA-PCI ; Chamber. Specifically, these commenters stated that if the standard salary level is set at a fixed percentile of earnings of full-time salaried workers, and some or all of the newly nonexempt workers are converted to hourly status and thus removed from the data set, earnings at that 40th percentile of salaried workers will quickly rise solely due to the exclusion of these hourly workers (an effect many commenters representing employers referred to as "ratcheting"). Commenters asserted that this may cause growth in the 40th percentile of full-time salaried workers to no longer reflect prevailing economic conditions.

Claims that automatic updating using the fixed percentile approach will lead to the rapid escalation of the salary level are based primarily on the assumption that employers will respond to this rulemaking by converting newly nonexempt workers to hourly pay status. However, the Department believes these concerns are overstated because many affected EAP workers who are reclassified as nonexempt are likely to remain salaried as: (1) an analysis of the 2004 salary level updates did not indicate significant numbers of workers were converted to hourly pay; and (2) an analysis of updates in California's higher salary level did not indicate significant numbers of workers were reclassified as hourly. In any event, the Department's modeling of the impact of automatic updating shows that any potential "ratcheting" effect that may occur would be small, largely because newly nonexempt workers compose a small percentage of the pool of full-time nonhourly workers in the dataset used to establish the salary level.

The analyses below are based on CPS MORG data. As acknowledged in the NPRM, salary status for CPS respondents cannot definitively be determined because workers who indicate they are paid on a salary basis or on some basis other than hourly are all classified as "nonhourly." To consider the possibility this biases our results, we looked at the Panel Study of Income

Dynamics (PSID). The PSID provides additional information concerning salaried versus other nonhourly workers. In the PSID, respondents are asked how they are paid on their main job and are asked for more detail if their response is some way other than salaried or hourly.[247] The available responses include piecework, commission, self-employed/farmer/profits, and by the job/day/mile. None of these options are ones to which employers are likely to change their salaried workers. The share of workers who are not paid on either an hourly or salaried basis is relatively small, about 10 percent of workers in the PSID. Accordingly, grouping nonhourly workers with salaried workers does not negate the following comparisons and conclusions based on CPS data.

Workers May Remain Salaried Even if Nonexempt

The Department disagrees with commenters that suggested that employers will likely (or automatically) convert large numbers of newly nonexempt employees to hourly pay status. In some instances such conversation may occur, for example, if an employee regularly works overtime and the employer is able to adjust his or her regular rate. However, for the majority of affected employees, there will be no incentive for employers to convert them to hourly pay because they do not work overtime. Also, employers may have other incentives to maintain workers' salary status; for example, they may offer salaried positions to attract talent. Commenters highlighted that employees value job characteristics associated with salaried pay—such as earnings predictability—and so employers may pay nonexempt employees on a salary basis to preserve employee morale. Using the CPS MORG data pooled for FY2013-FY2015 and projected to FY2017, the Department estimated that 18.6 percent of white collar workers earning

[247] This question is only asked of "heads" and "wives" in the PSID (i.e., heads of households and their spouses). However, in the 2013 PSID, "heads" and "wives" composed 88 percent of workers.

below $455 per week are nonhourly; based on findings from the PSID, the Department believes most of these nonhourly workers are salaried.

Previous Salary Level Updates did not Indicate Workers Being Converted to Hourly

The Department analyzed employer responses to the 2004 Final Rule and to a series of revisions to California's salary level test for exemption under state law in order to better estimate whether workers who are reclassified as nonexempt are more likely to be paid on an hourly basis. These analyses allow the identification of any potential regulatory impact while controlling for time trends and a broad range of other relevant factors (education, occupation, industry, geographic location, etc.). The Department found no evidence that changes in the salary level for exemption resulted in a statistically significant increase in the percent of full-time white collar workers paid on an hourly basis following either the 2004 Final Rule or the California salary level updates. See section VI.D.iii.5 for discussion of the applicability of these results to this Final Rule.

2004 Final Rule. In 2004, the salary level required to be eligible for exemption increased from $250 per week (short salary level) to $455 (the standard salary level).[248] To estimate the effect of this salary level update on the share of full-time, white collar workers paid hourly, the Department conducted a difference-in-differences (DD) analysis of the 2004 part 541 salary level revisions. The Department modeled two types of differences to include in the analysis:

[248] The 2004 Final Rule increased the salary level from the previous long test level of $155 per week (executive and administrative exemptions) or $170 per week (professional exemption) to $455 per week. For purposes of this analysis, the Department compared the increase from the short test salary level ($250 per week) since the long test was no longer operative due to increases in the minimum wage.

Difference #1 (pre- versus post-rulemaking): January-March 2004 versus January-March 2005,[249]

Difference #2 (workers exempt before, but not after rule compared to workers exempt both before and after the rule): workers earning between $250 and $455 per week versus those earning at least $455 but less than $600.[250]

Using this DD analysis, the Department found no evidence that changes in the salary level for exemption resulted in a statistically significant increase in the percent of full-time white collar workers paid on an hourly basis following the 2004 Final Rule.[251] This can also be demonstrated by looking directly at the share of workers paid hourly; the Department found that following the 2004 Final Rule, the percent of full-time white collar workers who were paid hourly decreased from 74.6 percent to 73.6 percent in the affected earnings range ($250-$455), while it increased from 60.9 percent to 63.6 percent in the earnings range where there were no changes to EAP exemption eligibility. In other words, between the first quarter of 2004 and the first quarter of

---

[249] The 2004 Final Rule was published April 23, 2004 and went into effect August 23, 2004.

[250] In order to isolate the potential effect on earnings due to the 2004 salary changes, we excluded workers in states where the state EAP salary level was higher than the FLSA short salary level (i.e., Alaska, California, Connecticut, Maine and New York).

[251] The shares provided in the text do not control for other covariates. However, using a DD regression approach that includes a full complement of controls (age, education, gender, race, ethnicity, occupation, industry, state of residence, working overtime, multiple job holding), the relevant marginal effect is -0.033 (i.e., the amount the likelihood of being paid hourly changes post rulemaking for workers earning between $250 and $455 per week relative to the change for workers earning $455 or above) and the p-value is 0.118, which is not statistically significant at conventional thresholds for significance. The difference-in-differences model used can be written as

where H_i is equal to 1 if worker i is paid by the hour and 0 otherwise, T_i is equal to 1 if worker i earns at least $250 but less than $455 and 0 if she earns between $455 and $600, P_i is equal to 1 for the post-change period (Jan.-Mar. 2005) and 0 for the pre-change period (Jan.-Mar. 2004), and C_i is the set of worker-specific controls. The model was estimated using a probit regression.

2005, the share of full-time white-collar workers who are paid hourly decreased marginally in the group of potentially affected workers (those earning $250 to $455), whereas in the group earning above the salary level (those earning more than $455 but less than $600) it increased by 2.6 percentage points.

California. The exempt salary level in California is set by statute as equal to twice the state minimum wage for 40 hours worked per week. The salary level has been updated four times in recent years when California raised the state minimum wage: in 2007 (from $540 to $600), 2008 (from $600 to $640), 2014 (from $640 to $720), and 2016 (from $720 to $800). To estimate the effect of the salary level update on the share of white collar workers paid hourly, the Department conducted difference-in-differences-in-differences (DDD) analyses of the revisions to the California exempt salary level for which CPS data were available (2007-2008, and 2014).[252]

The Department modeled three types of differences to include in the analyses:

Difference #1 (pre- versus post-rulemaking):

2007-2008: January-March 2006 versus January-March 2008, and

2014: January-March 2014 versus January-March 2015.[253]

Difference #2 (workers exempt before, but not after rule compared to workers exempt both before and after the rule):

2007-2008: workers earning between $540 and $640 versus those earning at least $640 but less than $740, and

[252] California raised the state minimum wage in January of both 2007 and 2008. These changes were announced jointly in September 2006. Because employers knew that a second increase in the exempt salary level would occur one year after the 2007 increase, the Department expected that they planned their adjustments accordingly rather than treat the two increases as isolated independent events. Therefore the Department considered the combined effects of the 2007 and 2008 changes.

[253] The minimum wage update took place in July 2014.

2014: workers earning between $640 and $720 versus workers earning at least $720 but less than $800.

Difference #3: California workers versus workers in other states where the salary level was not increased.[254]

Using this DDD analysis, the Department found no evidence that changes in the salary level for exemption resulted in a statistically significant increase in the percent of full-time white collar workers paid on an hourly basis.[255] This can also be demonstrated by looking directly at the share of workers paid hourly (using differences one and three). After the 2007-2008 California update, among Californians earning between the old and new salary levels, the share of full-time white collar workers being paid hourly decreased slightly from 73.4 percent to 73.1 percent. Among full-time white collar workers earning comparable amounts in states where the

[254] We excluded Alaska, Connecticut and New York because the state EAP salary levels either: (1) were above the FLSA standard salary level; (2) differed in the time periods considered; or (3) both (1) and (2).

[255] The shares provided in the text do not control for other covariates. However, using a DDD regression approach that includes a full complement of controls (age, education, gender, race, ethnicity, occupation, industry, state of residence, working overtime, multiple job holding), the relevant marginal effect for 2007-2008 is 0.018 and the p-value is 0.612. The marginal effect of the triple difference for 2014 is -0.057 and the p-value is 0.103. Neither of these are statistically significant at conventional thresholds for significance. The difference-in-difference-in-differences model used can be written as

where H_i is equal to 1 if worker i is paid by the hour and 0 otherwise, T_i is equal to 1 if worker i earns between the old threshold and the new threshold and 0 if she earns just above the new threshold, P_i is equal to 1 for the post-change period and 0 for the pre-change period, S_i is equal to 1 if worker i is in California and 0 if she is in other states where the salary level was not increased, and C_i is the set of worker-specific controls. The model was estimated using a probit regression. The Department also performed alternative analyses to check whether these results hold, including (1) a comparison of California and other states looking only at workers with earnings below the revised salary level (i.e., eliminating Difference #2 from the DDD model), and (2) running simplified models without individual controls. None of these checks found a significant increase in the percentage of workers paid on an hourly basis.

salary level did not change, the share of workers being paid hourly increased from 66.2 percent to 67.5 percent. After the 2014 California update, the values increased from 72.0 percent to 74.0 percent in California, and increased from 68.2 percent to 69.4 percent in other states.[256] Neither of these results suggests that the salary updates resulted in a significantly greater percent of affected workers being converted to hourly pay in California as compared to the rest of the United States.

The Department's Modeling of Possible "Ratcheting" Indicates Any Effect Would be Negligible

In a study submitted by the PPWO, Edgeworth Economics estimated the impact that automatic updating using the fixed percentile approach would have on the salary level. They found that "[i]f just one quarter of the full-time non-hourly workers earning less than $49,400 per year ($950 per week) were reclassified as hourly workers, the pay distribution among the remaining non-hourly workers would shift so that the 40th percentile of the 2016 pay distribution would be $54,184 ($1,042 per week), about 9.6 percent higher than it was in 2015." Their estimate was based on the key assumption that one quarter of all full-time nonhourly employees would be converted to hourly pay each year. Accordingly, based on the Department's reading of the Edgeworth Economics' analysis, it appears they converted one quarter of all full-time nonhourly employees earning below the salary level to hourly status. This modeling is inappropriate because it fails to account for whether the employees perform white collar work and are subject to the EAP exemption, and ignores that, at most, employers will only have an incentive to convert affected workers (a small share of all full-time nonhourly employees).

[256] The increase in the proportion of workers paid on an hourly basis in the relevant salary range in California is not statistically different from the increase in the proportion for workers in other states.

Oxford Economics also considered how converting salaried workers to hourly status could influence automatically updated salary levels. In one analysis, they assumed that employers will convert the lowest 40 percent of full-time salaried workers to hourly status in 2016, and that by Year 2 the 40th percentile of the new distribution of salaried workers would be equivalent to the 64th percentile of the original distribution. The Department believes this model is clearly unrealistic. Like Edgeworth Economics, Oxford Economics erroneously assumes that workers who are not affected by the new salary would nonetheless be converted to hourly status.

In another analysis, Oxford Economics estimated employer response to updating the threshold to $970 in 2016. According to their analysis, approximately 695,000, or nearly one third, of the 2,189,000 affected workers will be converted from "salaried exempt" to "hourly nonexempt." Oxford Economics concluded that about two-thirds of these converted employees will have their hourly rates decreased to leave their earnings unchanged, and one third will have their hours reduced to 38 per week. However, neither analysis appears to account for the possibility that employers may continue to pay some newly nonexempt employees on a salary basis, and thus both predictions likely overestimate the number of workers converted to hourly status.

The Department conducted a similar analysis, using what the Department believes are more realistic assumptions, and found a significantly smaller potential impact. The Department considered which affected workers are most likely to be converted from salaried to hourly pay as a result of this rulemaking. Type 4 workers, those whose salaries are increased to the new standard salary level, remain exempt and their method of pay will not change. Type 3 workers, who regularly work overtime and become nonexempt, and Type 2 workers, those who occasionally work overtime and become nonexempt, are the most likely to have their pay status changed. Type 1 workers (who make up more than 60 percent of the affected workers) are

assumed to not work overtime, and employers thus have little incentive to convert them to hourly pay. For this analysis, the Department assumed all Type 2 and Type 3 workers are converted to hourly status to generate a realistic upper bound of the magnitude of any possible ratcheting effect. The Department estimated that the salary level in 2026, after three updates, the salary level as set in the Final Rule (based on weekly earnings of full-time salaried workers in the South) could be approximately 2.5 percent higher than expected due to this effect. This figure is significantly smaller than the estimates provided by the commenters. Furthermore, we believe our estimate is an overestimate because it assumes employers convert all Type 2 and Type 3 workers to hourly status, which, for the reasons discussed above and in section IV.E.iii. of the preamble, the Department believes is a highly unlikely outcome.

x. Projections

1. Methodology

The Department projected affected workers, costs, and transfers forward for ten years. This involved several steps. First, past growth in the earnings distribution was used to estimate future salary levels. Second, workers' earnings, absent a change in the salary levels, were predicted. Third, predicted salary levels and earnings were used to estimate affected workers. Fourth, employment adjustments were estimated and adjusted earnings were calculated. Lastly, costs and transfers were calculated.

First, in years when the salary level is updated, the predicted salary levels are estimated using the historic geometric growth rate between FY2005 and FY2015 in (1) the 40th earnings percentile of full-time salaried workers in the South for the standard salary level and (2) the 90th earnings percentile of full-time salaried workers nationally for the HCE compensation level, projected to the second quarter of the respective years before the updated levels go into effect.

Second, the Department calculated workers' projected earnings in future years by applying the annual projected wage growth rate in the workers' industry-occupation to current earnings, as described in section VI.B.ii. Third, we compared workers' counter-factual earnings (i.e., absent the rulemaking) to the predicted salary levels. If the counter-factual earnings are below the relevant salary 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 FY2017 absent the rule change but have projected earnings in the future year that are less than the relevant salary level. Sampling weights were also adjusted to reflect employment growth as explained in section VI.B.ii.

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.[257] For workers newly affected in Year 2 through Year 10, employers' wage and hour adjustments due to the rulemaking 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).

Very few commenters discussed the Department's projections for Year 2 through Year 10 in the NPRM's analysis. Dan Goldbeck[258] stated, in an article cited by the Association of Energy Service Companies, that in the NPRM, the Department reported only Year 2 and Year 10

[257] 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.
[258] Goldbeck, D. (2015). "White Collar" Overtime Expansion. Regulation Review.

projected estimates, making it "difficult to know the accuracy of this calculation." See also International Bancshares Corporation. In the Final Rule, the Department has included projected costs in each of the nine projected years.

2. Estimated Projections

The Department estimated that in Year 1, 4.2 million EAP workers will be affected, with about 65,000 of these attributable to the revised HCE compensation level. In Year 10, the number of affected EAP workers was estimated to equal 5.3 million with 217,000 attributed to the HCE exemption. The projected number of affected EAP workers accounts for anticipated employment growth by increasing the number of workers represented by the affected EAP workers (i.e., increasing sampling weights).

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 may earn less than $455 in FY2017 but between $455 and $913 in subsequent years; such a worker would be counted as an affected worker. In the absence of this Final Rule he or she would likely have become exempt at some point during the 9 projected years; however, as a result of the Final Rule, this worker remains nonexempt, and is thus affected by the Final Rule. In the NPRM the Department considered these workers separately from affected workers and did not estimate costs and transfers associated with these workers.[259]

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

[259] These workers were not considered in the NPRM because their work patterns are known when they are nonexempt (because they earn less than $455), but those patterns might change if they become exempt (e.g., they may work more hours). However, because a significant number of additional workers are projected to remain nonexempt through this process, the Department chose to include them in the analysis for this Final Rule. To do so, we assume their exempt work patterns will be similar to their nonexempt work patterns.

familiarization costs only occur in Year 1 and years when the salary levels are automatically updated. Thus, in addition to Year 1, some regulatory familiarization costs are expected to occur in Year 4 (FY2020), Year 7 (FY2023), and Year 10 (FY2026).[260] Specifically, the Department added 5 minutes per establishment for regulatory familiarization time to access and read the published notice in the Federal Register with the updated standard salary level and HCE compensation level in years when the salary level is updated. In each of these three years (FY2020, FY2023, and FY2026) regulatory familiarization costs are approximately $23 million (see section VI.D.iii. for details on the methodology for estimating costs).

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 exemptions and those exemptions as modified by the Final Rule is essentially zero. Therefore, projected regulatory familiarization costs for new entrants over the next nine years are zero (although these new entrants will incur regulatory familiarization costs in years when the salary and compensation levels are updated).

Adjustment costs and managerial costs are a function of the number of affected EAP workers and thus will be higher with automatic updating. Adjustment costs will occur in any year in which workers are newly affected. After Year 1, these costs are estimated to be relatively small since the majority of workers affected by this rulemaking are affected in Year 1, and the costs occur almost exclusively in years when the salary is automatically updated. Management costs recur each year for all affected EAP workers whose hours are adjusted. Therefore, managerial costs increase modestly over time as the number of affected EAP workers increases. The

[260] The first update will go into effect January 1, 2020. However, for this economic analysis, the Department modeled the first automatic update to occur at the beginning of FY2020. This is because the analysis is conducted by fiscal year and modeling the update as going into effect a quarter before allows simplification of the analysis with only a negligible impact on estimates.

Department estimated that Year 1 managerial costs would be $214.0 million (section VI.D.iii.); by Year 10 these costs would grow slightly to $255.1 million. In years without automatic updates managerial costs fall slightly since earnings growth will cause some workers to no longer be affected in those years. In all years between 94 and 98 percent of costs are attributable to the revised standard salary level (Table 33).

The Department projected two types of transfers from employers to employees associated with workers affected by the regulation: (1) transfers due to the minimum wage provision and (2) transfers due to the overtime pay provision. Transfers to workers from employers due to the minimum wage provision, estimated to be $34.3 million in Year 1, are projected to decline to $17.8 million in Year 10 as increased earnings over time move workers' regular rate of pay above the minimum wage.[261] Transfers due to overtime pay should grow slightly over time because the number of affected workers will increase, although transfers fall in years between automatic updates. Transfers to workers from employers due to the overtime pay provision increase from $1,250.8 million in Year 1 to $1,589.4 million in Year 10. Workers affected by the revised standard salary level account for between 80 and 92 percent of overtime transfers in all years.

[261] State minimum wages above the federal level as of January 1, 2016 were incorporated and used for projected years. Increases in minimum wages were not projected. If state or federal minimum wages increase between January 1, 2016 and FY2026, then estimated projected minimum wage transfers may be underestimated.

Table 33: Projected Costs and Transfers, Standard and HCE Salary Levels

Fiscal Year (Year #)	Affected EAP Workers (Millions)	Costs				Transfers			DWL [b]
		Reg. Fam.	Adjust-ment [a]	Manag-erial	Total	Due to MW	Due to OT	Total	
		(Millions FY2017$)							
Year									
2017 (1)	4.2	$272.5	$191.4	$214.0	$677.9	$34.3	$1,250.8	$1,285.2	$6.4
2018 (2)	4.0	$0.0	$1.5	$206.6	$208.0	$28.5	$907.9	$936.5	$8.7
2019 (3)	3.9	$0.0	$1.9	$200.6	$202.6	$27.7	$883.9	$911.6	$8.5
2020 (4)	4.6	$22.8	$10.4	$232.5	$265.7	$25.8	$1,221.2	$1,247.0	$9.8
2021 (5)	4.4	$0.0	$2.8	$223.7	$226.5	$24.6	$1,134.7	$1,159.2	$9.6
2022 (6)	4.3	$0.0	$2.8	$217.6	$220.5	$20.5	$1,017.3	$1,037.8	$9.4
2023 (7)	5.0	$23.0	$7.3	$243.4	$273.7	$18.0	$1,404.6	$1,422.6	$10.2
2024 (8)	4.8	$0.0	$2.5	$236.1	$238.6	$15.2	$1,290.0	$1,305.3	$10.0
2025 (9)	4.6	$0.0	$2.2	$230.9	$233.1	$14.4	$1,193.2	$1,207.6	$10.1
2026 (10)	5.3	$23.1	$5.9	$255.1	$284.2	$17.8	$1,589.4	$1,607.2	$11.1
Average Annualized									
3% real rate	--	$37.6	$25.4	$225.0	$288.0	$23.2	$1,178.5	$1,201.6	$9.3
7% real rate	--	$42.4	$29.0	$223.6	$295.1	$23.8	$1,165.3	$1,189.1	$9.2

[a] Adjustment costs occur in all years when there are newly affected workers, including years when the salary level is not updated. Adjustment costs may occur in years without updated salary levels because some workers' projected earnings are estimated using negative earnings growth.
[b] DWL was estimated based on the aggregate impact of both the minimum wage and overtime pay provisions. Since the transfer associated with the minimum wage is negligible compared to the transfer associated with overtime pay, the vast majority of this cost is attributed to the overtime pay provision.

Table 33 also summarizes average 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 average annualized value of $295.1 million per year over ten years when using a 7 percent real discount rate. Of this total, average annualized regulatory familiarization costs were estimated to be $42.4 million. Average annualized adjustment costs were estimated to be $29.0 million. The remaining $223.6 million in average annualized direct costs were accounted for by managerial costs. The average annualized value of total transfers was estimated to equal $1,189.1 million. The largest component of this was the transfer from employers to workers due to overtime pay, which was $1,165.3 million per year, while average annualized transfers due to the minimum wage totaled $23.8 million per year.

The cost to society of fewer hours of labor demanded, expressed as DWL, was estimated to be $6.4 million in Year 1. DWL increases over time and in Year 10 it is projected to equal $11.1 million. DWL increases sharply between Year 1 and Year 2 because the Department assumes the market has had time to fully adjust to the revised standard salary and HCE annual compensation levels by Year 2. In Year 1 employers may not be able to fully adjust wages and hours in response to the rulemaking, so the Department used a short run wage elasticity of labor demand to reflect this constrained response; in Year 2 employers have sufficient time to fully adjust, and a long-run wage elasticity is used. Therefore, the decrease in hours worked is larger in Year 2 than Year 1, and the DWL is also larger. Finally, the Department estimated that average annualized DWL was $9.2 million per year.

A summary of the estimates used in calculating DWL for years 1, 2 and 10 is presented in Table 34. The size of the DWL depends on the change in average hourly wages, the change in average hours, and the number of affected EAP workers with changes in their hours worked.

While the change in average hourly wages generally tends to be fairly similar over time, the number of affected EAP workers increases in years with updated salary levels and falls in other years; together these lead to a slight increase in annual DWL over time.

Table 34: Summary of Projected Deadweight Loss Component Values

Component	Year 1	Future Years	
		Year 2	Year 10
	Standard Salary		
Average hourly wages (holding hours constant)			
Pre	$14.86	$14.94	$17.59
Post [a]	$15.55	$15.45	$18.20
Change	$0.69	$0.51	$0.61
Change in average overtime hours	-0.40	-0.76	-0.79
Affected EAP workers (1,000s)	803	778	903
DWL			
Per worker per week	$0.14	$0.20	$0.24
Nominal annual (millions)	$5.8	$7.9	$11.3
Real annual (millions of FY2017$)	$5.8	$7.9	$9.2
	HCE		
Average hourly wages (holding hours constant)			
Pre	$42.84	$42.51	$45.03
Post [a]	$44.85	$43.96	$46.56
Change	$2.01	$1.45	$1.53
Change in average overtime hours	-0.37	-0.69	-0.68
Affected EAP workers (1,000s)	31	34	83
DWL			
Per worker per week	$0.38	$0.50	$0.52
Nominal annual (millions)	$0.61	$0.88	$2.25
Real annual (millions of FY2017$)	$0.61	$0.87	$1.85

Note: DWL analysis is limited to workers in Types 2 and 3 who experience hour adjustments.

[a] Despite general growth in wages, the average wage may fall slightly from Year 1 to Year 2 because the population has changed.

3. Comparison to Projections with Alternative Methods

This section presents estimated projected impacts without automatic updating and using the CPI-U to automatically update salary levels. Projections without automatic updating are shown so impacts of the initial increase and subsequent increases can be disaggregated. Projections using the CPI-U are included because this alternative was proposed as a potential method in the NPRM.

For the CPI-U method, the Department used the predicted change in annual CPI-U values for FY2017 through FY2026 from the Congressional Budget Office.[262] For example, inflation based on the CPI-U for FY2017, FY2018, and FY2019 is predicted to be 2.2, 2.4, and 2.4 percent, respectively; therefore, the projected salary level for Year 4 (the year of the first salary level update) is $978 ($913 x 1.022 x 1.024 x 1.024). In other years, predicted inflation based on the CPI-U was projected to be 2.4 percent.

Table 35 shows projected numbers of affected workers, costs, and transfers with these alternative methods. With triennial automatic updating as adopted in this Final Rule, the number of affected EAP workers would increase from 4.2 million to 5.3 million over 10 years. With triennial automatic updating using the CPI-U, the number of affected EAP workers would increase from 4.2 million to 5.4 million over 10 years. Conversely, in the absence of automatic updating, the number of affected EAP workers is projected to decline from 4.2 to 3.0 million.

The three costs to employers previously considered are (1) regulatory familiarization costs, (2) adjustment costs, and (3) managerial costs. Regulatory familiarization costs do not vary depending on whether the fixed percentile method or the CPI-U method is used for automatic updating, and are only slightly lower without automatic updating. Adjustment costs and

[262] Congressional Budget Office. (2016). The Budget and Economic Outlook: 2016 to 2026. Pub. No. 51129. Table E-2.

managerial costs are a function of the number of affected EAP workers and so will be higher with automatic updating. Average annualized direct costs were projected to be very similar with the fixed percentile method and the CPI-U method: $295.1 million and $294.7 million, respectively. Average annualized direct costs are lower without automatic updating because fewer workers will be affected ($249.8 million).

Average annualized transfers and DWL follow a similar pattern: estimates are very similar for the fixed percentile method and the CPI-U method, but are lower without automatic updating. Average annualized transfers are $1,189.1 million with the fixed earnings percentile, $1,172.6 million with the CPI-U method, and $873.5 million without automatic updating. Average annualized DWL is $9.2 million with the fixed earnings percentile, $9.2 million with the CPI-U method, and $7.7 million without automatic updating.

Table 35: Comparison of Projected Costs and Transfers with Alternative Methods, Standard and HCE Salary Levels

Fiscal Year (Year #)	Affected EAP Workers			Costs			Transfers			DV	
	Fixed Perc.	Without Updates	CPI-U	Fixed Perc.	Without Updates	CPI-U	Fixed Perc.	Without Updates	CPI-U	Fixed Perc.	Wit Upc
	(Millions)			(Millions FY2017$)							
Year											
2017 (1)	4.2	4.2	4.2	$677.9	$677.9	$677.9	$1,285.2	$1,285.2	$1,285.2	$6.4	$6
2018 (2)	4.0	4.0	4.0	$208.0	$208.0	$208.0	$936.5	$936.5	$936.5	$8.7	$8
2019 (3)	3.9	3.9	3.9	$202.6	$202.6	$202.6	$911.6	$911.6	$911.6	$8.5	$8
2020 (4)	4.6	3.8	4.5	$265.7	$197.8	$258.7	$1,247.0	$878.7	$1,176.1	$9.8	$8
2021 (5)	4.4	3.6	4.4	$226.5	$190.4	$222.6	$1,159.2	$834.9	$1,079.4	$9.6	$8
2022 (6)	4.3	3.5	4.2	$220.5	$181.7	$218.8	$1,037.8	$793.2	$1,006.7	$9.4	$7
2023 (7)	5.0	3.3	5.0	$273.7	$173.4	$278.1	$1,422.6	$753.3	$1,416.7	$10.2	$7
2024 (8)	4.8	3.2	4.8	$238.6	$164.9	$239.5	$1,305.3	$711.9	$1,306.4	$10.0	$7
2025 (9)	4.6	3.1	4.6	$233.1	$157.6	$232.8	$1,207.6	$669.7	$1,175.1	$10.1	$7
2026 (10)	5.3	3.0	5.4	$284.2	$150.7	$292.1	$1,607.2	$649.2	$1,678.0	$11.1	$7
Average Annualized											
3% real rate	--	--	--	$288.0	$238.7	$287.9	$1,201.6	$855.9	$1,185.9	$9.3	$7
7% real rate	--	--	--	$295.1	$249.8	$294.7	$1,189.1	$873.5	$1,172.6	$9.2	$7

Appendix A: Methodology for Estimating Exemption Status

The number of workers exempt under the FLSA's part 541 regulations is unknown. It is neither reported by employers to any central agency nor asked in either an employee or establishment survey.[263] The Department estimated the number of exempt workers using the following methodology. This methodology is based largely on the approach used during the 2004 revisions.[264] This appendix expands on the methodology description in the Final Rule.

A.1 The Duties Tests Probability Codes

The CPS MORG data do not include information about job duties. To determine whether a worker meets the duties test the Department employs the methodology it used in the 2004 Final Rule. Each occupation is assigned a probability representing the odds that a worker in that occupation would pass the duties test. For the EAP duties test, the five probability intervals are:

- Category 0: Occupations not likely to include any workers eligible for the EAP exemptions.
- Category 1: Occupations with probabilities between 90 and 100 percent.
- Category 2: Occupations with probabilities between 50 and 90 percent.
- Category 3: Occupations with probabilities between 10 and 50 percent.
- Category 4: Occupations with probabilities between 0 and 10 percent.[265]

The occupations identified in this classification system represent an earlier occupational classification scheme (the 1990 Census Codes). Therefore, an occupational crosswalk was used to map the previous occupational codes to the 2002 Census occupational codes which are used in

[263] RAND recently released results from a survey conducted to estimate EAP exempt workers. 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.
[264] 69 FR 22196-22209 (Apr. 23, 2004).
[265] Table A2 lists the probability codes by occupation used to estimate exemption status.

the CPS MORG 2002 through 2010 data.[266,267] When the new occupational category was comprised of more than one previous occupation, the Department assigned a probability category using the weighted average of the previous occupations' probabilities, rounded to the closest category code.

Next, the Department must determine which workers to classify as exempt. For example, the probability codes indicate that out of every ten public relation managers between five and nine are exempt; however, the Department does not know which five to nine workers are exempt. Exemption status could be randomly assigned but this would bias the earnings of exempt workers downward, since higher paid workers are more likely to perform the required duties. Therefore, the probability of being classified as exempt should increase with earnings. First, the Department assigned the upper bound of the probability range in each exemption category to workers with top-coded weekly earnings. For all other white collar salaried workers earning at least $455 per week in each exemption category,[268] the Department estimated the probability of exemption for each worker in the data based on both occupation and earnings using a gamma distribution.[269] For the gamma distribution, the shape parameter alpha was set to the squared quotient of the sample mean divided by the sample standard deviation, and the scale parameter beta was set to the sample variance divided by the sample mean. These parameter calculations

---

[266] To match 1990 Census Codes to the corresponding 2000 Census Codes see: http://www.census.gov/people/io/methodology/.
To translate the 2000 Census Codes into the 2002 Census Codes each code is multiplied by 10.

[267] Beginning January 2011, the MORG data use the 2010 Census Codes. The Department translates these codes into the equivalent 2002 Census Codes to create continuity. The crosswalk is available at: http://www.census.gov/people/io/methodology/.

[268] Also included are all workers who are in occupational categories associated with named occupations.

[269] A gamma distribution is a general type of statistical distribution that is based on two parameters, in this case alpha and beta. The gamma distribution was chosen because during the 2004 revision it fit the data the best of the non-linear distributions considered, which included normal, lognormal, and gamma. 69 FR 22204-08.

are based on the method described in the 2004 rulemaking, except for the use of the standard deviation instead of the standard error.[270] Table A1 shows that the expected number of exempt workers is similar when using a gamma distribution method and assigning the midpoint of each probability code range to all workers in that probability code. After determining the probabilities of exemption for each worker in the data (dependent on both occupation and earnings), the Department randomly assigns exemption status to each worker, conditional on the worker's probability of exemption.

Table A1: Comparison of EAP-Exempt Worker Estimates [a]

Probability Code Category	Midpoint Probability	Gamma Distribution Model
High probability of exemption (1)	23,134,055	23,165,165
Probably exempt (2)	4,808,003	4,792,536
Probably not exempt (3)	1,675,615	1,644,144
Low or no probability of exemption (4)	277,473	287,310
Total	29,895,146	29,889,154

[a] Numbers shown are the expected value of the number of workers exempt in each of the four probability code categories.

The 2004 Final Rule assigned probabilities for whether workers in each occupation would pass the HCE abbreviated duties test if they earned $100,000 or more in total annual compensation; these probabilities are:

- Category 0: Occupations not likely to include any workers eligible for the HCE exemption.
- Category 1: Occupations with a probability of 100 percent.
- Category 2: Occupations with probabilities between 94 and 96 percent.

[270] Since the sample standard deviation is much larger than the standard error, using the sample standard deviation to calculate the shape and location parameters resulted in probabilities that vary more with earnings.

- Category 3: Occupations with probabilities between 58.4 and 60 percent.
- Category 4: Occupations with a probability of 15 percent.

Like under the standard test, there is a positive relationship between earnings and exemption status; however, unlike the standard test, the relationship for the HCE analysis can be represented well with a linear earnings function. Once individual probabilities are determined, workers are randomly assigned to exemption status.

A.2 Other Exemptions

There are many other exemptions to the minimum wage and overtime pay provisions of the FLSA. Accordingly, in the 2004 Final Rule, the Department excluded workers in agriculture and certain transportation occupations from the analysis. The Department now is, in addition, estimating those workers who fall under one of the other exemptions in section 13(a) of the FLSA, because such workers are exempt from both minimum wage and overtime pay under the relevant section and would remain exempt regardless of any changes to the EAP exemption. In fact, many of the workers estimated below as falling within one of the section 13(a) exemptions will already have been excluded from the analysis because they are paid on an hourly basis or are in a blue collar occupation. The methodology for identifying the workers who fall under the section 13(a) exemptions is explained here and is based generally on the methodology the Department used in 1998 when it issued its last report under section 4(d) of the FLSA.

A.2.1 Section 13(a)(1) Outside Sales Workers

Outside sales workers are a subset of the section 13(a)(1) exemptions, but since they are not affected by the salary regulations they are not discussed in detail in the preamble. Outside sales workers are included in occupational category “door-to-door sales workers, news and street vendors, and related workers” (Census code 4950). This category is composed of workers who

both would and would not qualify for the outside sales worker exemption; for example, street vendors would not qualify. Therefore, the percentage of these workers that qualify for the exemption was estimated. The Department believes that, under the 1990 Census Codes system, outside sales workers were more or less uniquely identified with occupational category "street & door-to-door sales workers" (277). Therefore, the Department exempts the share of workers in category 4950 who would have been classified as code 277 (43 percent) under the old classification system.

A.2.2 Agricultural Workers

Similar to the 2004 analysis, the Department excluded agricultural workers from the universe of affected employees. In the 2004 Final Rule all workers in agricultural industries were excluded; however, here only workers also in select occupations were excluded since not all workers in agricultural industries qualify for the agricultural overtime pay exemptions. This method better approximates the true number of exempt agricultural workers and provides a more conservative estimate of the number of affected workers. Industry categories include: "crop production" (0170), "animal production" (0180), and "support activities for agriculture and forestry" (0290). Occupational categories include all blue collar occupations (identified with the probability codes), "farm, ranch, and other agricultural managers" (0200), "general and operations managers" (0020), and "first-line supervisors/managers of farming, fishing, and forestry workers" (6000).

A.2.3 Other Section 13(a) Exemptions

The following methodology relies mainly on CPS MORG data but also incorporates alternative data sources when necessary.

<u>Section 13(a)(3): Seasonal amusement and recreational establishment</u>

Any employee of an amusement or recreational establishment may be exempt from minimum wage and overtime pay if the establishment meets either of the following tests: (a) it operates for seven months or less during any calendar year, or (b) its revenue for the six lowest months of the year is less than one-third of the other six months of such year. Amusement and recreational establishments are defined as "establishments frequented by the public for its amusement or recreation," and "typical examples of such are the concessionaires at amusement parks and beaches."[271] In the CPS MORG data the Department identifies general amusement and recreation in the following industry categories:

- "independent artists, performing arts, spectator sports, and related industries" (8560),
- "museums, art galleries, historical sites, and similar institutions" (8570),
- "bowling centers" (8580),
- "other amusement, gambling, and recreation industries" (8590), and
- "recreational vehicle parks and camps, and rooming and boarding houses" (8670).[272]

The CPS MORG data does not provide information on employers' operating information or revenue. Using Business Employment Dynamics (BED) data, the Department estimated the share of leisure and hospitality employees working for establishments that are closed for at least one quarter a year.[273] Although not technically the same as the FLSA definition of "seasonal,"

[271] § 779.385.

[272] The Department does not believe that all employees in this industry category would qualify for this exemption. However, we had no way to segregate in the data employees who would and would not qualify for exemption.

[273] Seasonal employment was calculated by taking the difference in employment between establishment openings (all establishments that are either opening for the first time or reopening) and establishment births (establishments that are opening for the first time)—resulting in employment in only establishments reopening. Similarly, seasonal employment was estimated by taking the difference in employment between establishment closings and establishment deaths. These two estimates were then averaged. The analysis is limited to the leisure and hospitality industry. Since the exemption is limited to workers in "establishments frequented by

this is the best available approximation of "seasonal" employees. The Department estimated that 2.8 percent of amusement and recreational workers will be exempt.

The 1998 section 4(d) report estimated the number of exempt workers by applying an estimate determined in 1987 by a detailed report from the Employment Standards Administration. The Department chose not to use this estimate because it is outdated.

Section 13(a)(3) also exempts employees of seasonal religious or non-profit educational centers, but many of these workers have already been excluded from the analysis either as religious workers (not covered by the FLSA) or as teachers (professional exemption) and so are not estimated.

Section 13(a)(5): Fishermen

Any employee, such as a fisherman, employed in the catching, harvesting, or farming of fish or other aquatic life forms, is exempt from minimum wage and overtime pay. Fishermen are identified in occupational categories "fishers and related fishing workers" (6100) and "ship and boat captains and operators" (9310) and the industry category "fishing, hunting, and trapping" (0280). Workers identified in both these occupational and industry categories are considered exempt.

Section 13(a)(8): Small, local newspapers

This exemption from minimum wage and overtime pay applies to any employee employed by a newspaper with circulation of less than 4,000 and circulated mainly within the county where published. Newspaper employees are identified in the following occupational categories:

- "news analysts, reporters and correspondents" (2810),

---

the public for its amusement or recreation" the Department must assume the rate of employment in seasonal establishments, relative to all establishments, is equivalent across these amusement or recreation establishments and all leisure and hospitality establishments.

- “editors” (2830),
- “technical writers” (2840),
- “writers and authors” (2850), and
- “miscellaneous media and communication workers” (2860).

The exemption is limited to the industry category “newspaper publishers” (6470). To limit the exemption to small, local papers, the Department limits the exemption to employees in rural areas. Although employment in a rural area is not synonymous with employment at a small newspaper, this is the best approach currently available. Alternatively, the Department could use data from Dun and Bradstreet (D&B) as was done in the 1998 section 4(d) report. This data would provide information on which establishments are in rural areas; from this the Department could estimate the share of employment in rural areas. This approach would be much more time intensive but would not necessarily provide a better result.

Section 13(a)(10): Switchboard operators

An independently owned public telephone company that has not more than 750 stations may claim the minimum wage and overtime pay exemption for its switchboard operators. “Switchboard operators, including answering service”, are exempt under occupation code 5010 and industry classifications “wired telecommunications carriers” (6680) and “other telecommunications carriers” (6690). Using the 2012 Economic Census, the Department estimated that 1.6 percent of employees in the telecommunication industry (NAICS 517) are employed by firms with fewer than ten employees (the estimated level of employment necessary to service seven hundred and fifty stations). According to the 1998 section 4(d) report, fewer than 10,000 workers were exempt in 1987 and so at that time the Department did not develop a methodology for estimating the number exempt.

Section 13(a)(12): Seamen on foreign vessels

Any employee employed as a seaman on a vessel other than an American vessel is exempt from minimum wage and overtime pay. Seamen are identified by occupational categories:

- "sailors and marine oilers" (9300),
- "ship and boat captains and operators" (9310), and
- "ship engineers" (9570).

The CPS MORG data do not identify whether the vessel is foreign or domestic. The best approach the Department has devised is to assume that the number of workers in the occupation "deep sea foreign transportation of freight" (SIC 441) in 2000 is roughly equivalent to the number of workers on foreign vessels.[274] The 2001 Occupational Employment Statistics estimates there were 13,290 workers in this occupation and thus that number of seamen are assigned exempt status on a random basis.

Section 13(a)(15): Companions

Domestic service workers employed to provide "companionship services" for an elderly person or a person with an illness, injury, or disability are not required to be paid the minimum wage or overtime pay. Companions are classified under occupational categories:

- "nursing, psychiatric, and home health aides" (3600) and
- "personal and home care aides" (4610).

And industry categories:

- "home health care services" (8170),
- "individual and family services" (8370), and
- "private households" (9290).

[274] The SIC classification system has been replaced with NAICS; thus, more recent data are not available.

All the workers who fall within these occupational and industry categories were previously excluded from the analysis because they are in occupations where workers have no likelihood of qualifying for the section 13(a)(1) exemption.

Section 13(a)(16): Criminal investigators

The criminal investigator must be employed by the federal government and paid "availability pay."[275] Criminal investigators are identified in occupational categories:

- "detectives and criminal investigators" (3820),
- "fish and game wardens" (3830), and
- "private detectives and investigators" (3910).

This exemption was not mentioned in the 1998 section 4(d) report. The Department exempts all workers in the occupations identified above and employed by the federal government (PEIO1COW value equal to one).

Section 13(a)(17): Computer workers

Computer workers who meet the duties test are exempt under two sections of the FLSA. Salaried computer workers who earn a weekly salary of not less than $455 are exempt under section 13(a)(1) and computer workers who are paid hourly are exempt under section 13(a)(17) if they earn at least $27.63 an hour. Occupations that may be considered exempt include: "computer and information systems managers" (110), "computer scientists and systems analysts" (1000), "computer programmers" (1010), "computer software engineers" (1020), "computer support specialists" (1040), "database administrators" (1060), "network and computer systems

[275] Availability pay is compensation for hours when the agent must be available to perform work over and above the standard 40 hours per week. See http://www.opm.gov/oca/pay/HTML/AP.HTM.

administrators" (1100), "network systems and data communications analysts" (1110), "computer operators" (5800), and "computer control programmers and operators" (7900).

To identify computer workers exempt under section 13(a)(17), the Department restricts the population to workers who are paid on an hourly basis and who earn at least $27.63 per hour. To determine which of these workers pass the computer duties test, we use the probabilities of exemption assigned to these occupations by the Department and assume a linear relationship between earnings and exemption status. Note that none of these workers are impacted by the rulemaking because they are paid on an hourly basis.

A.2.4 Section 13(b) Exemptions

Section 13(b)(1): Motor carrier employees

This exemption eliminated overtime pay for "any employee with respect to whom the Secretary of Transportation has power to establish qualifications and maximum hours of service pursuant to the provisions of Section 31502 of Title 49."[276] In essence, these are motor carrier workers, identified by industry category "truck transportation" (6170).

To be exempt, these workers must engage in "safety affecting activities." Examples of exempt occupations include: "driver, driver's helper, loader, or mechanic."[277] The relevant occupational categories are:

- "electronic equipment installers and repairers, motor vehicles" (7110),
- "automotive service technicians and mechanics" (7200),
- "bus and truck mechanics and diesel engine specialists" (7210),

[276] 49 U.S.C. 31502. The text of the law is available at: http://www.gpo.gov/fdsys/pkg/USCODE-2011-title49/html/USCODE-2011-title49-subtitleVI-partB-chap315-sec31502.htm.
[277] Fact Sheet #19: The Motor Carrier Exemption under the Fair Labor Standards Act (FLSA).

- "heavy vehicle and mobile equipment service technicians and mechanics" (7220), and
- "driver/sales workers and truck drivers" (9130).[278]

Section 13(b)(2): Rail carrier employees

Section 13(b)(2) exempts "any employee of an employer engaged in the operation of a rail carrier subject to part A of subtitle IV of Title 49."[279] This includes industrial category "rail transportation" (6080). The 1998 methodology did not include occupational requirements but the 2004 methodology did, so this restriction was included. Occupations are limited to:

- "locomotive engineers and operators" (9200),
- "railroad brake, signal, and switch operators" (9230),
- "railroad conductors and yardmasters" (9240), and
- "subway, streetcar, and other rail transportation workers" (9260).

Section 13(b)(3): Air carrier employees

This section exempts employees subject to the "provisions of title II of the Railway Labor Act."[280] In essence, this exempts air carrier employees, identified by industry category "air transportation" (6070). The 1998 methodology did not include occupational requirements but the 2004 methodology did, so this restriction was included. Occupations are limited to "aircraft pilots and flight engineers" (9030) and "aircraft mechanics and service technicians" (7140).

Section 13(b)(6): Seamen

---

[278] The 2004 methodology used 1990 Census codes 505, 507, and 804 which crosswalk to these occupations. However, occupations 605, 613, and 914 (included in the 1990 Census code 804) were excluded because under the new classification system they were deemed irrelevant.

[279] 49 U.S.C. 10101-11908. Text of the law is available at: http://www.gpo.gov/fdsys/pkg/USCODE-2013-title49/pdf/USCODE-2013-title49-subtitleIV-partA.pdf.

[280] 45 U.S.C. 181 et seq. Available at: http://www.gpo.gov/fdsys/pkg/USCODE-2013-title45/html/USCODE-2013-title45-chap8-subchapII.htm.

Occupational categories include "sailors and marine oilers" (9300), "ship and boat captains and operators" (9310), and "ship engineers" (9570).[281] The exemption is limited to the "water transportation" industry (6090).

Section 13(b)(10): Salesmen, partsmen, or mechanics

The Department limited this exemption to workers employed in a "nonmanufacturing establishment primarily engaged in the business of selling such vehicles or implements to ultimate purchasers." Industry classifications include: "automobile dealers" (4670) and "other motor vehicle dealers" (4680). In the 2004 Final Rule, the industry was limited to 1990 Census code 612 which became Census code "automobile dealers" (4670). Category 4680 ("other motor vehicle dealers") is also included here in keeping with the 1998 section 4(d) report methodology.

The 1998 methodology did not include an occupational restriction; however, the 2004 methodology limited the exemption to automobiles, trucks, or farm implement sales workers and mechanics.

Automobiles, trucks, or farm implement sales workers include:

- "parts salespersons" (4750), and
- "retail salespersons" (4760).[282]

Mechanics include:

- "electronic equipment installers and repairers, motor vehicles" (7110),
- "automotive body and related repairers" (7150),
- "automotive glass installers and repairers" (7160),

[281] The 2004 methodology used 1990 Census codes 828, 829, and 833 which crosswalk to these occupations. However, occupation 952 (dredge, excavating, and loading machine operators) was excluded because under the new classification system it was deemed irrelevant.

[282] The 2004 methodology used codes 263 and 269 which crosswalk to these codes plus a few others which have been deemed irrelevant and excluded (4700, 4740, and 4850).

- “automotive service technicians and mechanics” (7200),
- “bus and truck mechanics and diesel engine specialists” (7210),
- “heavy vehicle and mobile equipment service technicians and mechanics” (7220),
- “small engine mechanics” (7240), and
- “miscellaneous vehicle and mobile equipment mechanics, installers, and repairers” (7260).[283]

Table A2: Probability Codes by Occupation

2002 Census Code	Occupation	Probability Code
10	Chief executives	1
20	General and operations managers	1
40	Advertising and promotions managers	1
50	Marketing and sales managers	1
60	Public relations managers	2
100	Administrative services managers	1
110	Computer and information systems managers	1
120	Financial managers	1
130	Human resources managers	1
140	Industrial production managers	1
150	Purchasing managers	1
160	Transportation, storage, and distribution managers	1
200	Farm, ranch, and other agricultural managers	3
210	Farmers and ranchers	0
220	Construction managers	1
230	Education administrators	1
300	Engineering managers	1
310	Food service managers	3
320	Funeral directors	2
330	Gaming managers	2
340	Lodging managers	3
350	Medical and health services managers	1
360	Natural sciences managers	1
400	Postmasters and mail superintendents	0

[283] The 2004 methodology used codes 505, 506, 507, and 514 which generally crosswalk to these codes. A few additional codes were added which were deemed relevant (7240 and 7260).

410	Property, real estate, and community association managers	3
420	Social and community service managers	1
430	Managers, all other	1
500	Agents and business managers of artists, performers, and athletes	2
510	Purchasing agents and buyers, farm products	2
520	Wholesale and retail buyers, except farm products	2
530	Purchasing agents, except wholesale, retail, and farm products	2
540	Claims adjusters, appraisers, examiners, and investigators	2
560	Compliance officers, except agriculture, construction, health and safety, and transportation	3
600	Cost estimators	1
620	Human resources, training, and labor relations specialists	2
700	Logisticians	1
710	Management analysts	2
720	Meeting and convention planners	2
730	Other business operations specialists	2
800	Accountants and auditors	1
810	Appraisers and assessors of real estate	3
820	Budget analysts	2
830	Credit analysts	2
840	Financial analysts	2
850	Personal financial advisors	2
860	Insurance underwriters	1
900	Financial examiners	3
910	Loan counselors and officers	2
930	Tax examiners, collectors, and revenue agents	1
940	Tax preparers	2
950	Financial specialists, all other	2
1000	Computer scientists and systems analysts	1
1010	Computer programmers	2
1020	Computer software engineers	1
1040	Computer support specialists	1
1060	Database administrators	1
1100	Network and computer systems administrators	1
1110	Network systems and data communications analysts	1
1200	Actuaries	1
1210	Mathematicians	1
1220	Operations research analysts	1
1230	Statisticians	1
1240	Miscellaneous mathematical science occupations	1
1300	Architects, except naval	1
1310	Surveyors, cartographers, and photogrammetrists	3
1320	Aerospace engineers	1

1330	Agricultural engineers	1
1340	Biomedical engineers	1
1350	Chemical engineers	1
1360	Civil engineers	1
1400	Computer hardware engineers	1
1410	Electrical and electronic engineers	1
1420	Environmental engineers	1
1430	Industrial engineers, including health and safety	1
1440	Marine engineers and naval architects	1
1450	Materials engineers	1
1460	Mechanical engineers	1
1500	Mining and geological engineers, including mining safety engineers	1
1510	Nuclear engineers	1
1520	Petroleum engineers	1
1530	Engineers, all other	1
1540	Drafters	4
1550	Engineering technicians, except drafters	4
1560	Surveying and mapping technicians	4
1600	Agricultural and food scientists	1
1610	Biological scientists	1
1640	Conservation scientists and foresters	1
1650	Medical scientists	1
1700	Astronomers and physicists	1
1710	Atmospheric and space scientists	1
1720	Chemists and materials scientists	1
1740	Environmental scientists and geoscientists	1
1760	Physical scientists, all other	3
1800	Economists	2
1810	Market and survey researchers	2
1820	Psychologists	1
1830	Sociologists	2
1840	Urban and regional planners	3
1860	Miscellaneous social scientists and related workers	2
1900	Agricultural and food science technicians	4
1910	Biological technicians	4
1920	Chemical technicians	4
1930	Geological and petroleum technicians	4
1940	Nuclear technicians	4
1960	Other life, physical, and social science technicians	4
2000	Counselors	2
2010	Social workers	3
2020	Miscellaneous community and social service specialists	3
2040	Clergy	0

2050	Directors, religious activities and education	0
2060	Religious workers, all other	0
2100	Lawyers	1
2110	Judges, magistrates, and other judicial workers	1
2140	Paralegals and legal assistants	4
2150	Miscellaneous legal support workers	3
2200	Postsecondary teachers	1
2300	Preschool and kindergarten teachers	2
2310	Elementary and middle school teachers	1
2320	Secondary school teachers	1
2330	Special education teachers	1
2340	Other teachers and instructors	1
2400	Archivists, curators, and museum technicians	1
2430	Librarians	1
2440	Library Technicians	4
2540	Teacher assistants	4
2550	Other education, training, and library workers	1
2600	Artists and related workers	2
2630	Designers	1
2700	Actors	1
2710	Producers and directors	1
2720	Athletes, coaches, umpires, and related workers	2
2740	Dancers and choreographers	1
2750	Musicians, singers, and related workers	1
2760	Entertainers and performers, sports and related workers, all other	1
2800	Announcers	2
2810	News analysts, reporters and correspondents	3
2820	Public relations specialists	3
2830	Editors	3
2840	Technical writers	3
2850	Writers and authors	2
2860	Miscellaneous media and communication workers	2
2900	Broadcast and sound engineering technicians and radio operators	4
2910	Photographers	1
2920	Television, video, and motion picture camera operators and editors	2
2960	Media and communication equipment workers, all other	4
3000	Chiropractors	1
3010	Dentists	1
3030	Dietitians and nutritionists	3
3040	Optometrists	1
3050	Pharmacists	1
3060	Physicians and surgeons	1
3110	Physician assistants	2

3120	Podiatrists	1
3130	Registered nurses	1
3140	Audiologists	2
3150	Occupational therapists	3
3160	Physical therapists	2
3200	Radiation therapists	3
3210	Recreational therapists	2
3220	Respiratory therapists	3
3230	Speech-language pathologists	2
3240	Therapists, all other	2
3250	Veterinarians	1
3260	Health diagnosing and treating practitioners, all other	1
3300	Clinical laboratory technologists and technicians	3
3310	Dental hygienists	3
3320	Diagnostic related technologists and technicians	3
3400	Emergency medical technicians and paramedics	3
3410	Health diagnosing and treating practitioner support technicians	4
3500	Licensed practical and licensed vocational nurses	4
3510	Medical records and health information technicians	4
3520	Opticians, dispensing	0
3530	Miscellaneous health technologists and technicians	2
3540	Other healthcare practitioners and technical occupations	3
3600	Nursing, psychiatric, and home health aides	0
3610	Occupational therapist assistants and aides	0
3620	Physical therapist assistants and aides	0
3630	Massage therapists	0
3640	Dental assistants	0
3650	Medical assistants and other healthcare support occupations	4
3700	First-line supervisors/managers of correctional officers	2
3710	First-line supervisors/managers of police and detectives	3
3720	First-line supervisors/managers of fire fighting and prevention workers	3
3730	Supervisors, protective service workers, all other	3
3740	Fire fighters	0
3750	Fire inspectors	0
3800	Bailiffs, correctional officers, and jailers	0
3820	Detectives and criminal investigators	0
3830	Fish and game wardens	0
3840	Parking enforcement workers	0
3850	Police and sheriff’s patrol officers	0
3860	Transit and railroad police	0
3900	Animal control workers	0
3910	Private detectives and investigators	4
3920	Security guards and gaming surveillance officers	0

3940	Crossing guards	0
3950	Lifeguards and other protective service workers	0
4000	Chefs and head cooks	0
4010	First-line supervisors/managers of food preparation and serving workers	3
4020	Cooks	0
4030	Food preparation workers	0
4040	Bartenders	0
4050	Combined food preparation and serving workers, including fast food	0
4060	Counter attendants, cafeteria, food concession, and coffee shop	0
4110	Waiters and waitresses	0
4120	Food servers, nonrestaurant	0
4130	Dining room and cafeteria attendants and bartender helpers	0
4140	Dishwashers	0
4150	Hosts and hostesses, restaurant, lounge, and coffee shop	4
4160	Food preparation and serving related workers, all other	0
4200	First-line supervisors/managers of housekeeping and janitorial workers	4
4210	First-line supervisors/managers of landscaping, lawn service, and groundskeeping workers	3
4220	Janitors and building cleaners	0
4230	Maids and housekeeping cleaners	0
4240	Pest control workers	0
4250	Grounds maintenance workers	0
4300	First-line supervisors/managers of gaming workers	1
4320	First-line supervisors/managers of personal service workers	4
4340	Animal trainers	4
4350	Nonfarm animal caretakers	0
4400	Gaming services workers	0
4410	Motion picture projectionists	0
4420	Ushers, lobby attendants, and ticket takers	0
4430	Miscellaneous entertainment attendants and related workers	0
4460	Funeral service workers	0
4500	Barbers	0
4510	Hairdressers, hairstylists, and cosmetologists	0
4520	Miscellaneous personal appearance workers	0
4530	Baggage porters, bellhops, and concierges	0
4540	Tour and travel guides	0
4550	Transportation attendants	0
4600	Child care workers	0
4610	Personal and home care aides	0
4620	Recreation and fitness workers	2
4640	Residential advisors	0
4650	Personal care and service workers, all other	0
4700	First-line supervisors/managers of retail sales workers	2

4710	First-line supervisors/managers of non-retail sales workers	2
4720	Cashiers	4
4740	Counter and rental clerks	4
4750	Parts salespersons	4
4760	Retail salespersons	4
4800	Advertising sales agents	2
4810	Insurance sales agents	2
4820	Securities, commodities, and financial services sales agents	2
4830	Travel agents	4
4840	Sales representatives, services, all other	3
4850	Sales representatives, wholesale and manufacturing	3
4900	Models, demonstrators, and product promoters	4
4920	Real estate brokers and sales agents	3
4930	Sales engineers	3
4940	Telemarketers	4
4950	Door-to-door sales workers, news and street vendors, and related workers	4
4960	Sales and related workers, all other	3
5000	First-line supervisors/managers of office and administrative support workers	1
5010	Switchboard operators, including answering service	4
5020	Telephone operators	4
5030	Communications equipment operators, all other	4
5100	Bill and account collectors	4
5110	Billing and posting clerks and machine operators	4
5120	Bookkeeping, accounting, and auditing clerks	4
5130	Gaming cage workers	4
5140	Payroll and timekeeping clerks	4
5150	Procurement clerks	4
5160	Tellers	4
5200	Brokerage clerks	4
5210	Correspondence clerks	4
5220	Court, municipal, and license clerks	4
5230	Credit authorizers, checkers, and clerks	3
5240	Customer service representatives	3
5250	Eligibility interviewers, government programs	3
5260	File Clerks	4
5300	Hotel, motel, and resort desk clerks	4
5310	Interviewers, except eligibility and loan	4
5320	Library assistants, clerical	4
5330	Loan interviewers and clerks	3
5340	New accounts clerks	4
5350	Order clerks	4
5360	Human resources assistants, except payroll and timekeeping	4
5400	Receptionists and information clerks	4

5410	Reservation and transportation ticket agents and travel clerks	4
5420	Information and record clerks, all other	4
5500	Cargo and freight agents	4
5510	Couriers and messengers	4
5520	Dispatchers	4
5530	Meter readers, utilities	4
5540	Postal service clerks	4
5550	Postal service mail carriers	4
5560	Postal service mail sorters, processors, and processing machine operators	4
5600	Production, planning, and expediting clerks	4
5610	Shipping, receiving, and traffic clerks	4
5620	Stock clerks and order fillers	0
5630	Weighers, measurers, checkers, and samplers, recordkeeping	4
5700	Secretaries and administrative assistants	4
5800	Computer operators	4
5810	Data entry keyers	4
5820	Word processors and typists	4
5830	Desktop publishers	4
5840	Insurance claims and policy processing clerks	3
5850	Mail clerks and mail machine operators, except postal service	4
5860	Office clerks, general	4
5900	Office machine operators, except computer	4
5910	Proofreaders and copy markers	4
5920	Statistical assistants	4
5930	Office and administrative support workers, all other	4
6000	First-line supervisors/managers of farming, fishing, and forestry workers	4
6010	Agricultural inspectors	3
6020	Animal breeders	3
6040	Graders and sorters, agricultural products	0
6050	Miscellaneous agricultural workers	0
6100	Fishers and related fishing workers	0
6110	Hunters and trappers	0
6120	Forest and conservation workers	0
6130	Logging workers	0
6200	First-line supervisors/managers of construction trades and extraction workers	4
6210	Boilermakers	0
6220	Brickmasons, blockmasons, and stonemasons	0
6230	Carpenters	0
6240	Carpet, floor, and tile installers and finishers	0
6250	Cement masons, concrete finishers, and terrazzo workers	0
6260	Construction laborers	0
6300	Paving, surfacing, and tamping equipment operators	0
6310	Pile-driver operators	0

6320	Operating engineers and other construction equipment operators	0
6330	Drywall installers, ceiling tile installers, and tapers	0
6350	Electricians	0
6360	Glaziers	0
6400	Insulation workers	0
6420	Painters, construction and maintenance	0
6430	Paperhangers	0
6440	Pipelayers, plumbers, pipefitters, and steamfitters	0
6460	Plasterers and stucco masons	0
6500	Reinforcing iron and rebar workers	0
6510	Roofers	0
6520	Sheet metal workers	0
6530	Structural iron and steel workers	0
6600	Helpers, construction trades	0
6660	Construction and building inspectors	3
6700	Elevator installers and repairers	0
6710	Fence erectors	0
6720	Hazardous materials removal workers	0
6730	Highway maintenance workers	0
6740	Rail-track laying and maintenance equipment operators	0
6750	Septic tank servicers and sewer pipe cleaners	0
6760	Miscellaneous construction and related workers	0
6800	Derrick, rotary drill, and service unit operators, oil, gas, and mining	0
6820	Earth drillers, except oil and gas	0
6830	Explosives workers, ordnance handling experts, and blasters	0
6840	Mining machine operators	0
6910	Roof bolters, mining	0
6920	Roustabouts, oil and gas	0
6930	Helpers--extraction workers	0
6940	Other extraction workers	0
7000	First-line supervisors/managers of mechanics, installers, and repairers	3
7010	Computer, automated teller, and office machine repairers	0
7020	Radio and telecommunications equipment installers and repairers	0
7030	Avionics technicians	0
7040	Electric motor, power tool, and related repairers	0
7050	Electrical and electronics installers and repairers, transportation equipment	0
7100	Electrical and electronics repairers, industrial and utility	0
7110	Electronic equipment installers and repairers, motor vehicles	0
7120	Electronic home entertainment equipment installers and repairers	0
7130	Security and fire alarm systems installers	0
7140	Aircraft mechanics and service technicians	0
7150	Automotive body and related repairers	0
7160	Automotive glass installers and repairers	0

7200	Automotive service technicians and mechanics	0
7210	Bus and truck mechanics and diesel engine specialists	0
7220	Heavy vehicle and mobile equipment service technicians and mechanics	0
7240	Small engine mechanics	0
7260	Miscellaneous vehicle and mobile equipment mechanics, installers, and repairers	0
7300	Control and valve installers and repairers	0
7310	Heating, air conditioning, and refrigeration mechanics and installers	0
7320	Home appliance repairers	0
7330	Industrial and refractory machinery mechanics	0
7340	Maintenance and repair workers, general	0
7350	Maintenance workers, machinery	0
7360	Millwrights	0
7410	Electrical power-line installers and repairers	0
7420	Telecommunications line installers and repairers	0
7430	Precision instrument and equipment repairers	0
7510	Coin, vending, and amusement machine servicers and repairers	0
7520	Commercial divers	4
7540	Locksmiths and safe repairers	0
7550	Manufactured building and mobile home installers	0
7560	Riggers	0
7600	Signal and track switch repairers	0
7610	Helpers--installation, maintenance, and repair workers	0
7620	Other installation, maintenance, and repair workers	0
7700	First-line supervisors/managers of production and operating workers	3
7710	Aircraft structure, surfaces, rigging, and systems assemblers	0
7720	Electrical, electronics, and electromechanical assemblers	0
7730	Engine and other machine assemblers	0
7740	Structural metal fabricators and fitters	0
7750	Miscellaneous assemblers and fabricators	0
7800	Bakers	0
7810	Butchers and other meat, poultry, and fish processing workers	0
7830	Food and tobacco roasting, baking, and drying machine operators and tenders	0
7840	Food batchmakers	0
7850	Food cooking machine operators and tenders	0
7900	Computer control programmers and operators	4
7920	Extruding and drawing machine setters, operators, and tenders, metal and plastic	0
7930	Forging machine setters, operators, and tenders, metal and plastic	0
7940	Rolling machine setters, operators, and tenders, metal and plastic	0
7950	Cutting, punching, and press machine setters, operators, and tenders, metal and plastic	0
7960	Drilling and boring machine tool setters, operators, and tenders, metal and	0

	plastic	
8000	Grinding, lapping, polishing, and buffing machine tool setters, operators, and tenders, metal and plastic	0
8010	Lathe and turning machine tool setters, operators, and tenders, metal and plastic	0
8020	Milling and planing machine setters, operators, and tenders, metal and plastic	0
8030	Machinists	0
8040	Metal furnace and kiln operators and tenders	0
8060	Model makers and patternmakers, metal and plastic	0
8100	Molders and molding machine setters, operators, and tenders, metal and plastic	0
8120	Multiple machine tool setters, operators, and tenders, metal and plastic	0
8130	Tool and die makers	0
8140	Welding, soldering, and brazing workers	0
8150	Heat treating equipment setters, operators, and tenders, metal and plastic	0
8160	Lay-out workers, metal and plastic	0
8200	Plating and coating machine setters, operators, and tenders, metal and plastic	0
8210	Tool grinders, filers, and sharpeners	0
8220	Metalworkers and plastic workers, all other	0
8230	Bookbinders and bindery workers	0
8240	Job printers	0
8250	Prepress technicians and workers	0
8260	Printing machine operators	0
8300	Laundry and dry-cleaning workers	0
8310	Pressers, textile, garment, and related materials	0
8320	Sewing machine operators	0
8330	Shoe and leather workers and repairers	0
8340	Shoe machine operators and tenders	0
8350	Tailors, dressmakers, and sewers	0
8360	Textile bleaching and dyeing machine operators and tenders	0
8400	Textile cutting machine setters, operators, and tenders	0
8410	Textile knitting and weaving machine setters, operators, and tenders	0
8420	Textile winding, twisting, and drawing out machine setters, operators, and tenders	0
8430	Extruding and forming machine setters, operators, and tenders, synthetic and glass fibers	0
8440	Fabric and apparel patternmakers	0
8450	Upholsterers	0
8460	Textile, apparel, and furnishings workers, all other	0
8500	Cabinetmakers and bench carpenters	0
8510	Furniture finishers	0
8520	Model makers and patternmakers, wood	0
8530	Sawing machine setters, operators, and tenders, wood	0
8540	Woodworking machine setters, operators, and tenders, except sawing	0

8550	Woodworkers, all other	0
8600	Power plant operators, distributors, and dispatchers	0
8610	Stationary engineers and boiler operators	0
8620	Water and liquid waste treatment plant and system operators	0
8630	Miscellaneous plant and system operators	0
8640	Chemical processing machine setters, operators, and tenders	0
8650	Crushing, grinding, polishing, mixing, and blending workers	0
8710	Cutting workers	0
8720	Extruding, forming, pressing, and compacting machine setters, operators, and tenders	0
8730	Furnace, kiln, oven, drier, and kettle operators and tenders	0
8740	Inspectors, testers, sorters, samplers, and weighers	0
8750	Jewelers and precious stone and metal workers	0
8760	Medical, dental, and ophthalmic laboratory technicians	0
8800	Packaging and filling machine operators and tenders	0
8810	Painting workers	0
8830	Photographic process workers and processing machine operators	0
8840	Semiconductor processors	0
8850	Cementing and gluing machine operators and tenders	0
8860	Cleaning, washing, and metal pickling equipment operators and tenders	0
8900	Cooling and freezing equipment operators and tenders	0
8910	Etchers and engravers	0
8920	Molders, shapers, and casters, except metal and plastic	0
8930	Paper goods machine setters, operators, and tenders	0
8940	Tire builders	0
8950	Helpers--production workers	0
8960	Production workers, all other	0
9000	Supervisors, transportation and material moving workers	3
9030	Aircraft pilots and flight engineers	4
9040	Air traffic controllers and airfield operations specialists	3
9110	Ambulance drivers and attendants, except emergency medical technicians	0
9120	Bus drivers	0
9130	Driver/sales workers and truck drivers	0
9140	Taxi drivers and chauffeurs	0
9150	Motor vehicle operators, all other	0
9200	Locomotive engineers and operators	0
9230	Railroad brake, signal, and switch operators	0
9240	Railroad conductors and yardmasters	0
9260	Subway, streetcar, and other rail transportation workers	0
9300	Sailors and marine oilers	0
9310	Ship and boat captains and operators	0
9570	Ship engineers	4
9340	Bridge and lock tenders	0

9350	Parking lot attendants	0
9360	Service station attendants	0
9410	Transportation inspectors	0
9420	Other transportation workers	0
9500	Conveyor operators and tenders	0
9510	Crane and tower operators	0
9520	Dredge, excavating, and loading machine operators	0
9560	Hoist and winch operators	0
9600	Industrial truck and tractor operators	0
9610	Cleaners of vehicles and equipment	0
9620	Laborers and freight, stock, and material movers, hand	0
9630	Machine feeders and offbearers	0
9640	Packers and packagers, hand	0
9650	Pumping station operators	0
9720	Refuse and recyclable material collectors	0
9730	Shuttle car operators	0
9740	Tank car, truck, and ship loaders	0
9750	Material moving workers, all other	0

Appendix B. Additional Tables

Table B1: Estimated Number of Potentially Affected EAP Workers with the Current and Updated Salary Levels, by Detailed Industry, Projected for FY2017

Industry	Potentially Affected EAP Workers (Millions) [a]	Not-Affected (Millions) [b]	Affected (Millions) [c]	Affected as Share of Potentially Affected
Total [d]	22.5	18.3	4.2	19%
Agriculture	0.0	0.0	0.0	19%
Forestry, logging, fishing, hunting, and trapping	0.0	0.0	0.0	6%
Mining	0.2	0.2	0.0	10%
Construction	0.8	0.7	0.1	16%
Nonmetallic mineral product manufacturing	0.1	0.1	0.0	11%
Primary metals and fabricated metal products	0.2	0.2	0.0	13%
Machinery manufacturing	0.3	0.3	0.0	10%
Computer and electronic product manufacturing	0.6	0.5	0.0	8%
Electrical equipment, appliance manufacturing	0.1	0.1	0.0	9%

Transportation equipment manufacturing	0.6	0.5	0.0	8%
Wood products	0.0	0.0	0.0	18%
Furniture and fixtures manufacturing	0.0	0.0	0.0	19%
Miscellaneous and not specified manufacturing	0.3	0.3	0.0	14%
Food manufacturing	0.2	0.1	0.0	17%
Beverage and tobacco products	0.1	0.1	0.0	9%
Textile, apparel, and leather manufacturing	0.1	0.1	0.0	19%
Paper and printing	0.1	0.1	0.0	20%
Petroleum and coal products manufacturing	0.1	0.1	0.0	9%
Chemical manufacturing	0.4	0.4	0.0	9%
Plastics and rubber products	0.1	0.1	0.0	15%
Wholesale trade	0.8	0.7	0.1	17%
Retail trade	1.6	1.2	0.4	26%
Transportation and warehousing	0.5	0.4	0.1	20%
Utilities	0.3	0.2	0.0	11%
Publishing industries (except internet)	0.2	0.2	0.0	15%
Motion picture and sound recording	0.0	0.0	0.0	54%
Broadcasting (except internet)	0.2	0.1	0.0	21%
Internet publishing and broadcasting	0.1	0.0	0.0	10%
Telecommunications	0.4	0.3	0.0	13%
Internet service providers and data processing services	0.0	0.0	0.0	20%
Other information services	0.1	0.0	0.0	31%
Finance	2.0	1.7	0.3	14%
Insurance	1.1	0.9	0.2	19%
Real estate	0.3	0.3	0.1	24%
Rental and leasing services	0.1	0.0	0.0	26%
Professional and technical services	4.0	3.5	0.5	13%
Management of companies and enterprises	0.1	0.1	0.0	24%
Administrative and support services	0.5	0.4	0.1	26%
Waste management and remediation services	0.1	0.0	0.0	23%
Educational services	0.9	0.7	0.2	26%
Hospitals	1.1	0.9	0.2	22%
Health care services, except hospitals	1.3	1.0	0.3	25%
Social assistance	0.4	0.2	0.2	38%
Arts, entertainment, and recreation	0.4	0.3	0.1	33%
Accommodation	0.1	0.1	0.0	21%
Food services and drinking places	0.3	0.2	0.1	30%
Repair and maintenance	0.1	0.1	0.0	35%
Personal and laundry services	0.1	0.0	0.0	37%
Membership associations and organizations	0.4	0.3	0.1	29%

Private households	0.0	0.0	0.0	21%
Public administration	0.8	0.6	0.2	24%

Note: Pooled data for FY2013 through FY2015.
[a] 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 would be entitled to overtime protection under the updated salary levels (if their weekly earnings do not increase to the new salary levels).
[d] Columns may not sum to total due to rounding.

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. See 5 U.S.C. 604. If the rule is not expected to have a significant economic impact on a substantial number of small entities, the RFA allows an agency to certify such, in lieu of preparing an analysis. See 5 U.S.C. 605. The Chief Counsel for Advocacy of the Small Business Administration was notified of this Final Rule upon submission of the rule to OMB under E.O. 12866.

Based on commenters' concerns that the IRFA did not clearly explain the Department's analysis of costs and payroll increases for small businesses, the Department reorganized and expanded on our analysis from that included in the NPRM. Commenters also requested that the Department include more detailed industry-specific information. In response, the Department has expanded the industry breakdown to the Census's 51 industries categorization. The Department was not able to provide more granular data due to small sample sizes causing imprecise estimates.

Table 36: Overview of Costs to Small Businesses, All Employees at Establishment Affected Methodology

Small Business Costs	Cost
Direct and Payroll Costs	
Average total cost per affected entity [a]	$3,265
Range of total costs per affected entity [a]	$847-$75,059
Average percent of revenue per affected entity [a]	0.17%
Average percent of payroll per affected entity [a]	0.87%
Average percent of small business profit	0.14%
Direct Costs	
Regulatory familiarization	
Time (first year)	1 hour per establishment
Time (update years)	5 minutes per establishment
Hourly wage	$36.22
Adjustment	
Time (first year affected)	75 minutes per newly affected worker
Hourly wage	$36.22
Managerial	
Time (weekly)	5 minutes per affected worker
Hourly wage	$42.31
Payroll Increases	
Average payroll increase per affected entity [a]	$2,516
Range of payroll increases per affected entity [a]	$647-$54,430

[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.

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

The Fair Labor Standards Act (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. It is widely recognized that the

general requirement that employers pay a premium rate of pay for all hours worked over 40 in a workweek is a cornerstone of the Act, grounded in two policy objectives. The first is to spread employment (or in other words, reduce involuntary unemployment) by incentivizing employers to hire more employees rather than requiring existing employees to work longer hours. The second policy objective is to reduce overwork and its detrimental effect on the health and well-being of workers.

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. Such employees typically receive more monetary and non-monetary benefits than most blue collar and lower-level office workers. 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 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. Throughout the regulatory history of the FLSA, the Department has considered the salary level test the "best single test" of exempt status. Stein Report at 19. This bright-line test is easily observed, objective, and clear. Id.

The Department has periodically updated the regulations governing these tests since the FLSA's enactment in 1938, most recently in 2004 when, among other revisions, the Department created the standard duties test and paired it with a salary level test of $455 per week. As a result of inflation, the real value of the salary threshold has fallen significantly since its last update, making it inconsistent with Congress' intent to exempt only "bona fide" EAP workers.

The standard salary level and the total compensation level required for highly compensated employees (HCE) have not been updated since 2004. As a result, the standard salary level has declined considerably in real terms relative to both its 2004 and 1975 values (see section VI.A.ii.). This is problematic because the exemption now covers workers who were never intended to be within the exemption, removing them from minimum wage and overtime protection. Similarly, the HCE annual compensation requirement is out of date; by the Final Rule's effective date the share of workers earning above $100,000 annually will have more than tripled since it was adopted in 2004. Therefore, the Department believes this rulemaking is necessary in order to restore the effectiveness of these levels.

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 salary levels were designed to operate as a ready guide to assist employers in deciding which employees were more likely to meet the duties tests for the exemptions. If left unchanged, however, the effectiveness of the salary level test as a means of determining exempt status diminishes as employees' wages increase over time.

In order to restore the ability of the standard salary level and the HCE compensation requirements to serve as appropriate bright-line tests between overtime protected employees and those who may be bona fide EAP employees, this rulemaking increases the minimum salary level to come within the exemption from the FLSA minimum wage and overtime requirements as an EAP employee from $455 to the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (currently the South, $913 a week) for the standard test, and from $100,000 to the annualized value of the 90th percentile of weekly earnings of full-time salaried workers nationally ($134,004 per year) for the HCE test. The Department reached the final standard salary and HCE total compensation levels after considering available data on actual salary levels currently being paid in the economy, publishing a proposed rule, reviewing more than 270,000 timely comments, and considering a range of alternatives. In order to ensure that these levels continue to function appropriately in the future, the rule also includes a provision to automatically update these salary levels every three years.

B. The Agency's Response to the Public Comments

Many of the issues raised by small businesses in the public comments received on the proposed rule are described in the preamble and RIA above, which we incorporate herein. Nevertheless, the significant issues raised by representatives of small businesses and the U.S. Small Business Administration's Office of Advocacy (Advocacy) are repeated here.

Most of the comments received concerning small businesses centered on the burden that the proposed salary level would impose on small entities. Some commenters expressed concern that the expected cost increase from the rule would disproportionately affect small entities. For example, the Wisconsin Agri-Business Association stated that the proposed rule's increased labor costs "will be felt most by small businesses" because they do not have the ability to adjust

to increased costs "without detriment to their business or the people they employ." Similarly, the Small Business Legislative Council (SBLC) explained that small businesses (and especially new business) tend to operate on very narrow margins, and so such businesses would be disproportionately affected by this rule. Other comments stated more generally that the proposed salary level would impose significant burdens on small businesses. See, e.g., Nebraska Chamber of Commerce and Industry, Northeastern Retail Lumber Association.

Accordingly, many commenters suggested the Department adopt some forms of differential treatment for small entities. The Greater Philadelphia Chamber of Commerce urged that "a lower compensation threshold be extended to small businesses and nonprofits, which can be expected to bear the greatest burden of complying with the proposed rule as presently written." The American Society of Association Executives and the International Association of Lighting Designers stated that the Department "should either set a lower salary level applicable to all employers or set the minimum salary level at a lower percentile of the national average for nonprofit and/or small employers." See also American Osteopathic Association; Kentucky Pharmacists Association. The Greene Law Firm recommended excluding from the proposed salary level increase employers that qualify as "small businesses" for their industries according to the North American Industry Classification System (NAICS) codes. The Maine Department of Labor "agree[d] that consideration should not focus on the size of the employer," but, citing the FLSA's coverage principles, stated that "[b]usinesses with low annual dollar volumes should not be held to the same [salary] level as large corporations." Finally, the Association for Enterprise Opportunity, the California Association for Micro Enterprise Opportunity, and Women Impacting Public Policy each requested an exemption for small businesses that fall below the $500,000 per year threshold for enterprise coverage under the FLSA.

Consistent with the history of the part 541 regulations, the Department declines to create a lower salary level requirement for employees employed at small entities, or to exclude such employees from the salary level test entirely. As we noted in 2004, while "the FLSA itself does provide special treatment for small entities under some of its exemptions . . . the FLSA's statutory exemption for white-collar employees in section 13(a)(1) contains no special provision based on size of business," 69 FR 22238. In the 78-year history of the part 541 regulations defining the EAP exemption, the salary level requirements have never varied according to the size or revenue of the employer. Cf. Stein Report at 5-6 (rejecting proposals to set varying regional salary levels); see also 69 FR 22238 (stating that implementing differing salary levels based on business size industry-by-industry "would present the same insurmountable challenges" as adopting regional or population-based salary levels).

Congress established the threshold for enterprise coverage under the FLSA (not less than $500,000 in annual gross volume of sales made or business done).[284] All employees of an FLSA-covered enterprise are entitled to the FLSA's protection, unless the employee meets the criteria for exemption from the FLSA's minimum wage and/or overtime pay provisions. Employees of firms which are not covered enterprises under the FLSA may still be subject to the FLSA's protections if they are individually engaged in interstate commerce or in the production of goods for interstate commerce, or in any closely-related process or occupation directly essential to such production. Such employees include those who: work in communications or transportation; regularly use the mails, telephones or interstate communication, or keep records

[284] The FLSA also applies to certain "named" activities, regardless of the annual dollar volume of those enterprises. Named enterprises include the operation of a hospital, an institution primarily engaged in the care of the sick, the aged, or the mentally ill who reside on the premises; a school for mentally or physically disabled or gifted children; a preschool, an elementary or secondary school, or an institution of higher education (whether operated for profit or not for profit); or an activity of a public agency. 29 U.S.C. 203(s)(1)(B)-(C).

of interstate transactions; handle, ship, or receive goods moving in interstate commerce; regularly cross state lines in the course of employment; or work for independent employers who contract to do clerical, custodial, maintenance, or other work for firms engaged in interstate commerce or in the product of goods for interstate commerce. The Department does not have the authority to create an exemption from the FLSA's individual coverage provision.

Several small business commenters raised concerns about the impact that the proposed salary level would have on small entities in low-wage regions and industries. See, e.g., Association for Enterprise Opportunity; Credit Union National Association; National Federation of Independent Businesses (NFIB); Society of Independent Gasoline Marketers of America. Kinecta Federal Credit Union stated that "the Department of Labor has clearly failed to adequately consider the potential impact of this rule on small businesses."

The Department recognizes that many small employers operate in low-paying regions or industries, and we have historically accounted for small employers when setting the salary level. See Weiss Report at 14-15 (setting the long test salary level for executive employees "slightly lower than might be indicated by the data" in part to avoid excluding "large numbers of the executives of small establishments from the exemption"). This Final Rule is no exception, as the Department is setting the salary level at the 40th percentile of weekly earnings of full-time salaried employees in the lowest-wage Census Region (as opposed to nationally) in part to account for low-wage employers, including small entities. This change from the methodology contained in the NPRM results in a lower standard salary level than proposed. The final standard

salary level represents the 20th percentile of likely exempt employees working in small establishments.[285]

The National Small Business Association and several other small business commenters asserted that "[m]any small businesses have no, or very few, non-exempt employees with most workers being salaried professionals or administrative employees. They do not have timekeeping and payroll systems in place that can accommodate the addition of many more non-exempt employees. Thus, the burden of these changes will fall much more heavily on small businesses than on their larger competitors." Similarly, NFIB stated that "small companies typically lack specialized compliance personnel" to adjust to new regulations, forcing business owners to oversee compliance efforts themselves or pay for outside consultation. The Louisiana Small Business Advisory Council similarly stated: "The cost of compliance for small businesses will be much greater than estimated by the DOL. Lots of small businesses have a minimal number of non-exempt employees, with most workers being salaried professionals or administrative employees." Identical or nearly identical "campaign" comments from small businesses also stated that "[s]mall businesses are often not equipped to monitor the activities of their employees in order to regulate their time. Companies with fewer than 20 employees rarely have a dedicated HR department, so the creation of new hourly reporting and tracking requirements are likely to be a much greater burden on these companies that do not currently face them. The result will be confusion and excess cost for individual business owners."

The Department believes that most, if not all, small businesses, like larger businesses, employ a mix of exempt and overtime-protected workers. As such, employers already have policies and systems in place for scheduling workers and monitoring overtime hours worked and

[285] The Department does not know which employees work for small businesses and therefore randomly assigns workers to small businesses.

the corresponding overtime premium pay. The Department recognizes that the Final Rule will result in the reclassification of some workers of small businesses from exempt to nonexempt, and expects that employers will modify their existing policies and systems to accommodate this change.

NFIB asserted that "the IRFA underestimates compliance costs because it does not take into account business size when estimating the time it takes to read, comprehend and implement the proposed changes." The Louisiana Small Business Advisory Council similarly commented that the Department underestimated adjustment costs, stating that small businesses "do not have timekeeping and payroll systems in place that can accommodate the addition of new, non-exempt employees."

In the Final Rule, the Department has clarified the explanation of our method for estimating the number of affected workers employed by small firms, and the number of small firms affected. The Department also reconsidered its estimate of the number of affected workers who work some overtime and increased in this Final Rule its estimate of affected workers who work overtime to 40 percent, up from 24 percent in the IRFA. Additionally, in response to comments, the Department has increased estimated regulatory familiarization and adjustment costs in the Final Rule.

Because there was insufficient data to estimate the number of affected workers employed by a typical small entity, the Department presented in the IRFA a range of results based on the assumption that only one employee per small firm was affected (the lower bound), and, alternatively, based on the assumption that all employees in a small firm were affected (the upper bound estimate of impacts per small establishment). Assuming the upper bound scenario, that all employees in a firm were affected, the IRFA showed that on average, costs and payroll increases

for small affected firms were less than 0.9 percent of payroll and less than 0.2 percent of revenues. The largest impacts were found in the food services and drinking places industry, where costs and payroll increases composed 0.84 percent of revenues. Due to the mix of exempt and overtime-protected workers employed by small businesses, the actual impact in this industry would almost certainly be smaller than shown in this upper bound scenario analysis.

The Department's adjustment cost estimate in the IRFA of one hour per newly affected worker was meant to be an average across all establishments. The Department acknowledges that some small businesses may face higher costs because of this rulemaking; however, since there is no data indicating the magnitude of this cost (compared to other businesses), the Department has not distinguished between establishment sizes in the cost estimates. However, in response to comments, the Department has increased the average adjustment time from one hour to 75 minutes per affected worker and we have added additional time for regulatory familiarization.

The Department received many comments in response to our proposal in the NPRM to automatically update the standard salary and HCE total annual compensation requirements. As discussed in section IV.E.i., some commenters asserted that the automatic updating mechanism introduced in this rulemaking may violate the RFA. For example, Seyfarth Shaw urged the Department to not proceed with automatic updating in part because this mechanism would "effectively bypass" this authority. The Partnership to Protect Workplace Opportunity (PPWO) raised similar RFA concerns and characterized the Department's rulemaking as a "'super-proposal,' deciding once and for all what (in the Department's belief) is best without consideration of its impact now or in the future." PPWO further stated that "it would not be possible for the Department to accurately estimate the impact of the automatic increases in future years as the workforce and the economy are always changing."

The RFA requires a regulatory flexibility analysis to accompany any agency final rule promulgated under 5 U.S.C. 553. See 5 U.S.C. 603-604. In accordance with this requirement, this section estimates the future costs of automatic updating using the fixed percentile method. The RFA only requires that such analyses accompany rulemaking, and commenters have not cited any RFA provision that would require the Department to conduct a new regulatory flexibility analysis before each automatic salary level update. In response to PPWO's concern about this rulemaking setting the salary level updating process "once and for all," we reiterate that this Final Rule does not preclude further rulemaking should the Department determine that future conditions indicate that revisions to the salary level updating methodology may be warranted.

Several commenters addressed the potential effects that an annual automatic updating mechanism could have on small entities. Advocacy commented that the Department should analyze the impact of updates on small businesses. The NFIB and the Small Business Legislative Council asserted that annual automatic updates to the standard salary level would create perpetual budgeting uncertainty for small entities, and objected that, under our proposal, small employers would only know the updated salary level 60 days before it takes effect. The Maine Department of Labor asserted that small businesses "lack the budget flexibility to provide annual raises to all exempt workers," while the National Grocers Association and Pizza Properties commented that annual automatic updates might reduce the prevalence or effectiveness of performance-based incentive pay. Several small business commenters, including Alpha Graphics and many individual employers who did not name their organizations, worried that automatic updating would likely "escalate the salary threshold level to an inappropriately high level in a matter of a few years."

Some small business commenters supported the idea of automatic updating, provided the Department make other salary level changes. See, e.g., Board Game Barrister (favoring annual updating using the CPI-U after the new salary level is phased in); Corporate Payroll Services (agreeing that salary level "should be indexed to inflation," but favoring a lower initial salary level); Think Patented (favoring updating using "the Current Population Survey Weekly Earnings Index, not the CPI-U")(emphasis in comment). The Society of Independent Gasoline Marketers of America, which favored a lower salary level in part to protect small business fuel retailers, supported automatically updating the standard salary threshold every three to five years "using a fixed percentile of wages based on data sets that take into account regional and industry wage disparities." See also Wisconsin Bankers Association (supporting automatic updates to regionally-adjusted salary level every five years). ANCOR and several non-profit care providers stated that "steadier, more predictable" salary level changes "will likely benefit providers who will be able to adjust to smaller, more frequent changes better than to larger, less frequent ones."

As explained earlier, this Final Rule introduces a mechanism to automatically update the standard salary and HCE total annual compensation thresholds, but with a number of important adjustments from the options considered in the NPRM. First, the Department will update the standard salary level by using regional data—specifically, the 40th percentile of weekly earnings of full-time salaried workers in the lowest wage Census Region—rather than national data. Second, future automatic updates to the standard salary and HCE compensation thresholds will take place every three years, rather than annually. Finally, the Department will publish the updated standard salary and HCE compensation thresholds at least 150 days before they take effect, instead of just 60 days. We believe that these three significant changes appropriately

address the concerns raised by small business commenters, while ensuring that the earnings thresholds for the EAP exemption will remain effective and up to date over time. The triennial automatic updating mechanism introduced in this Final Rule should benefit employers of all sizes going forward by avoiding the uncertainty and disruptiveness of larger increases that would likely occur as a result of irregular updates.

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

SBA's Office of Advocacy (Advocacy) expressed similar concerns as those expressed by other small business commenters, based upon its listening sessions and roundtables regarding the NPRM. Advocacy stated that it was concerned that the IRFA did not properly analyze the numbers of small businesses affected by this regulation and underestimated their compliance costs, and stated that the Department should publish a supplemental IRFA to reanalyze small business impacts. The comment stated that the IRFA "analyzes small entities very broadly, not fully considering how the economic impact affects various categories of small entities differently." The comment emphasized that the Department should not have analyzed industries by general 2- or 3-digit NAICS codes when "more specific data are readily available," and should have evaluated the impact on small non-profits and small governmental jurisdictions. As presented below, the Department revised its analysis in this FRFA to display the impact on industries using 6-digit NAICS codes, rather than the 2- and 3-digit codes, in order to present a more detailed assessment of specific impacts.[286]

[286] The Department estimates the number of small businesses and their employees using SUSB data and the SBA size standards at the 6-digit NAICS level. The most detailed industry level in the CPS is the 3-digit Census code level (262 industries total), which is considerably less granular than 6-digit NAICS. Moreover, there is not always a clear one-to-one correspondence between the Census and NAICS codes; 3-digit Census industry codes correspond to a mix of 4-digit, 5-digit, and even occasionally partial 6-digit industries. See https://usa.ipums.org/usa/volii/indcross03.shtml for a crosswalk between Census industry codes

Advocacy also stated that the Department should have analyzed and considered the impact of the proposed standard salary level in light of regional and industry differences. As explained in the preamble and in the economic impact analysis, the Final Rule differs from the proposed rule in that it bases the standard salary level on earnings in the lowest-wage Census Region, which is currently the South. This change will provide relief not only to small businesses and others in low-wage industries and regions, but also to small non-profit entities and small governmental jurisdictions. As previously explained, the Department believes that the standard salary level set in this Final Rule effectively distinguishes between employees who are overtime eligible and those who may be bona fide executive, administrative, or professional employees, without necessitating a return to a duties test that sets specific limits on the performance of nonexempt work, like the more detailed "long" duties test that existed before 2004. The new salary level not only accounts for the growth in salaries that has taken place since the salary level was updated in 2004, but also addresses the Department's conclusion that the 2004 salary threshold was set too low in light of that rulemaking's switch to a single duties test that no longer set any specific limits on the performance of nonexempt work. Setting a salary level in this Final Rule significantly below the level proposed by the Department would have required a more rigorous duties test than the current standard duties test in order to effectively distinguish between white collar employees who are overtime protected and those who may be bona fide EAP employees. Commenters representing employers overwhelmingly opposed DOL making changes to the duties test and stated that changes to the duties test are more burdensome for businesses. Further, by adjusting the Final Rule salary level to focus on the lowest-wage Census Region instead of a national level, we have removed the effect of the three higher earnings Census

---

and NAICS. While results can be tabulated at the 3-digit Census level, small sample sizes render statistical inference unreliable.

Regions on the salary level, ensuring the salary level is not driven by earnings in high- or even middle-wage regions of the country. We note that the South Census Region—the same region on which the Department relied in setting the salary level in 2004—is comprised of the three lowest-wage Census divisions. The Department believes that the lower standard salary level set in the Final Rule is appropriate for small businesses.

Advocacy also stated that the IRFA underestimated the regulatory familiarization, adjustment, managerial costs, and payroll costs, of the proposed rule on small entities, especially because small entities often have limited or no human resources personnel on staff. As discussed elsewhere in the preamble and the economic impact analysis, the FRFA increases the number of affected workers who work overtime, accounts for additional regulatory familiarization time each year that salary levels are adjusted and accounts for additional adjustment costs by increasing the adjustment time to 75 minutes per affected worker.[287] Moreover, the Department expects that small entities will rely upon compliance assistance materials provided by the Department, including the small entity compliance guide we will publish, or industry associations to become familiar with the Final Rule. Additionally, we note that the Final Rule is quite limited in scope as it primarily makes changes to the salary component of the part 541 regulation, even though the NPRM had raised questions about whether we also should make changes to the duties tests for exemption, which would have required more time to understand. With regard to adjustment costs, as noted above, the Department has increased the number of affected workers who work overtime and increased adjustment costs. The estimated 75 minutes per employee for adjustment costs is an average –allotting the full 75 minutes for the approximately 60 percent of the employees who do not work overtime (Type 1 employees) and

[287] The estimates of regulatory familiarization and adjustment costs are averages and some small entities may take more or less time to comply with this rule.

those whose salaries are well below the new standard salary level or only occasionally work overtime—even though employers actually will need to spend little to no time considering those workers. This leaves several hours for employers to consider how to respond with regard to other employees. Finally, as previously mentioned, 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. We believe that applying those same policies and systems to the workers whose exemption status changes will, on average, not require more than five minutes per week per worker who works overtime in managerial time cost, as employers will rely on policies such as a prohibition against working overtime without express approval or a standard weekly schedule of assigned hours. The Department notes that most affected employees who work overtime do not work large amounts of overtime hours and we therefore do not believe that employers will spend hours managing the time of these employees. Seventy-five percent of currently exempt employees average less than 10 hours of overtime per week. The Department believes that an average of 5 additional minutes per week managing the hours of each newly exempt worker who works overtime is appropriate.

As shown in Table 41, the Department estimates that there will be a range of costs for small entities from this rule, ranging from $847 to $75,059. Advocacy commented that small businesses were concerned that the Department's estimates of compliance costs were neither transparent nor accurate; and that small businesses have told Advocacy that their payroll costs would be significantly more costly than estimated by the Department. The Department does not believe there was sufficient information from small business commenters to determine the accuracy of those higher estimates.

Advocacy also suggested that the Department consider non-financial impacts that it asserted would accrue to small entities, such as the potential for lower employee morale or the loss of scheduling flexibility if employees are converted from salaried to hourly. The Department addresses these and other possible impacts that cannot be quantified in the preamble and economic impact analysis. As explained above, even if an employee is reclassified as nonexempt, there is no requirement that the employer convert the employee's pay status from salaried to hourly. Employers may choose to continue to pay these formerly exempt workers a salary (with the overtime premium for hours in excess of 40 in those weeks when the employee works overtime). In addition, as we noted in the preamble, based on the available research the Department does not believe that workers will experience the significant change in flexibility that some employers envisioned if the employer reclassifies them as nonexempt. See section IV.A.iv. The Department believes that while individual experiences vary, the rule would benefit employees in a variety of ways (e.g., through an increased salary, overtime earnings when the employee has to work extra hours, time off). Further, a study by Lonnie Golden[288], referenced by the National Employment Law Project (NELP), found using data from the General Social Survey (GSS) that "[i]n general, salaried workers at the lower (less than $50,000) income levels don't have noticeably greater levels of work flexibility that they would 'lose' if they became more like their hourly counterparts."

Advocacy also expressed concern "that the proposed rule does not count worker bonuses or commissions as part of the salary computation." The Department notes that the Final Rule, for the first time, does modify the salary basis rule to permit employers to count nondiscretionary

[288] Golden, L. (2014). Flexibility and Overtime Among Hourly and Salaried Workers. Economic Policy Institute.

bonuses and other nondiscretionary incentive payments such as commissions toward up to ten percent of the standard salary level requirement (see section IV.C.).

Finally, Advocacy suggested that the Department gradually phase in any changes to the salary level, and provide longer than the four months provided in 2004 for the implementation of the rule, suggesting we provide small businesses up to 12-18 months. As discussed in the preamble, the Department does not believe a phase-in is necessary given that this Final Rule adopts a methodology resulting in a lower salary level than the proposed methodology, and the Department will automatically update the salary level every three years rather than annually as proposed. Further, even though this Final Rule changes only salary-related requirements, unlike the 2004 rule which completely updated part 541 including the duties requirements, the Department is providing more than 180 days of notice to all employers before the Final Rule's effective date of December 1, 2016, and we will provide at least 150 days of notice of future automatic updates to the salary requirement.

C. Description of the Number of Small Entities and Employees 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 to classify entities as small in effect as of February 26, 2016 for the purpose of this analysis. 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 many 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 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.[289]

ii. Number of Small Entities and Employees

The Department obtained data from several different sources to determine the number of small entities and employment in these entities for each industry. However, the Statistics of U.S. Businesses (SUSB, 2012) was used for most industries. Industries for which the Department used data from alternative sources include credit unions,[290] commercial and non-commercial banks,[291] agriculture,[292] and public administration.[293] The Department used the latest available data in each case, so data years differ between sources.[294]

In the SUSB data, for each industry, the total number of small establishments and employees is organized into categories defined using employment, annual revenue, and assets. The Department combined these categories with the corresponding SBA standards to estimate the proportion of establishments and workers in each industry who are considered small or employed

---

[289] See http://www.sba.gov/advocacy/regulatory-flexibility-act for details.
[290] National Credit Union Association. (2010). 2010 Year End Statistics for Federally Insured Credit Unions.
[291] Federal Depository Insurance Corporation. (2015). Statistics on Depository Institutions - Compare Banks. Available at: https://www5.fdic.gov/SDI/index.asp.
[292] United States Department of Agriculture. (2014). 2012 Census of Agriculture: United States Summary and State Data: Volume 1, Geographic Area Series, Part 51. Available at: http://www.agcensus.usda.gov/Publications/2012/Full_Report/Volume_1,_Chapter_1_US/usv1.pdf.
[293] Hogue, C. (2012). Government Organization Summary Report: 2012. Available at: http://www2.census.gov/govs/cog/g12_org.pdf.
[294] Industry data are not displayed if the sample size of affected workers in small establishments is less than 10.

by a small entity. The general methodological approach was to classify all establishments or employees in categories below the SBA cutoff as in "small entity" employment.[295] If a cutoff fell in the middle of a defined category, a uniform distribution of employees across that bracket was assumed in order to determine what proportion should be classified as in small entity employment. The Department assumed that the small entity distribution across revenue categories for other depository institutions, which was not separately represented in FDIC asset data, was similar to that of credit unions. The share of employment estimated as small was applied to the CPS data. This is necessary for estimating affected workers in small entities.

The Department also estimated the number of small establishments by employer type (non-profit, for profit, government). The calculation of number of establishments by employer type is similar to the calculation of number of establishments by industry. However, instead of using SUSB data by industry, the Department used SUSB data by Legal Form of Organization for non-profit and for profits 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 population of their underlying jurisdiction, allowing us to estimate the number of governments that are small. The Department calculated the number of affected small employees from CPS data by tabulating observations where the respondent is both employed by a non-profit/for profit/government entity and is flagged as being employed in a small establishment. However, it should be noted that CPS respondents are flagged as employed in a small business based on their industry and the industry distribution of employment in small firms. Therefore, this methodology assumes the propensity of a business to be small is not correlated with employer type.iii. Number of Small Entities Impacted by the Final Rule

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

Table 37 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.)[296] Based on the methodology described above, the Department found that of the 7.5 million establishments relevant to this analysis, more than 80 percent (6.0 million) are small by SBA standards. These small establishments employ almost 50 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 a third of total payroll ($2.3 trillion of $6.5 trillion).[297]

Table 37: 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	7,514.8	6,049.5	136,307.0	49,768.7	$6,465.8	$2,275.5
Industry						
Agriculture	9.1	8.4	[c]	[c]	[c]	[c]
Forest., log., fish., hunt., and trap.	12.9	12.6	[c]	[c]	[c]	[c]
Mining	28.9	23.3	1,041.1	420.3	$74.2	$29.6
Construction	652.9	634.3	7,458.5	4,704.7	$364.3	$229.3

[296] SUSB reports data by size designations where the size designations are based on "enterprises" (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 chose to base the analysis on the number of establishments rather than firms for a more conservative estimate (potential overestimate) of the number of small businesses.

[297] Since information is not available about 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.

Nonmetallic mineral prod. manuf.	15.2	11.7	400.6	192.3	$20.1	$9.5
Prim. metals and fab. metal prod.	60.1	56.4	1,623.1	999.0	$80.3	$48.7
Machinery manufacturing	24.2	22.1	1,312.5	715.2	$73.7	$39.1
Computer and elect. prod. manuf.	13.2	11.8	1,283.3	598.8	$95.4	$44.8
Electrical equip., appliance manuf.	5.8	5.0	[c]	[c]	[c]	[c]
Transportation equip. manuf.	11.8	10.2	2,340.0	600.1	$141.6	$34.0
Wood products	13.7	12.6	386.7	260.6	$15.6	$10.6
Furniture and fixtures manuf.	16.3	15.9	380.8	274.7	$14.7	$10.6
Misc. and not spec. manuf.	29.6	28.5	1,355.5	801.2	$71.0	$41.4
Food manufacturing	25.8	22.7	1,676.7	769.2	$65.9	$28.3
Beverage and tobacco products	5.1	4.5	279.4	138.3	$15.1	$7.1
Textile, app., and leather manuf.	16.2	15.7	532.8	365.5	$21.2	$14.1
Paper and printing	32.0	29.8	880.4	491.1	$42.0	$22.6
Petroleum and coal prod. manuf.	2.2	1.2	[c]	[c]	[c]	[c]
Chemical manufacturing	13.3	10.6	1,316.6	538.3	$87.2	$34.3
Plastics and rubber products	12.7	10.6	502.0	235.9	$23.3	$10.6
Wholesale trade	420.5	334.7	3,474.1	1,572.2	$184.6	$82.5
Retail trade	1,063.8	685.4	15,618.2	5,224.8	$520.6	$191.1
Transport. and warehousing	214.5	170.7	5,780.1	1,481.6	$274.7	$65.6
Utilities	17.8	7.6	1,264.6	260.0	$81.1	$15.8
Publishing ind. (ex. internet)	27.1	20.9	562.0	242.9	$33.2	$14.0
Motion picture and sound recording	24.9	21.7	332.6	119.4	$17.2	$6.5
Broadcasting (except internet)	9.6	5.3	580.2	129.1	$34.3	$7.3
Internet publishing and broadcasting	6.9	5.8	[c]	[c]	[c]	[c]
Telecommunications	49.2	11.1	961.6	189.1	$64.9	$12.4

Internet serv. providers and data	14.0	9.2	[c]	[c]	[c]	[c]
Other information services	3.6	3.1	258.4	75.9	$11.5	$3.1
Finance	298.2	115.0	4,440.6	689.2	$295.9	$46.7
Insurance	176.3	137.6	2,613.4	670.4	$159.2	$40.6
Real estate	295.7	251.5	1,886.0	1,150.2	$91.8	$55.5
Rental and leasing services	54.0	26.9	374.0	109.7	$16.5	$4.4
Professional and technical services	859.2	778.9	8,793.5	4,164.1	$626.8	$288.4
Management of companies and enterprises	52.2	32.2	181.9	55.1	$10.0	$3.2
Admin. and support services	363.7	310.7	4,905.9	2,186.4	$174.7	$73.5
Waste manag. and remed. services	23.8	17.8	524.3	209.9	$23.7	$9.4
Educational services	95.9	84.0	13,615.2	3,008.1	$675.4	$142.1
Hospitals	6.7	1.6	6,979.2	336.9	$384.5	$18.9
Health care services, except hospitals	663.8	545.6	10,000.5	4,754.6	$424.1	$200.8
Social assistance	163.3	133.1	2,829.2	1,567.8	$94.9	$49.7
Arts, entertainment, and recreation	125.1	115.1	2,591.0	1,255.8	$89.0	$43.5
Accommodation	64.2	53.7	1,511.1	557.6	$50.7	$18.7
Food services and drinking places	598.5	470.6	8,534.3	2,315.2	$197.2	$53.6
Repair and maintenance	211.2	196.4	1,572.6	1,167.9	$63.5	$45.9
Personal and laundry services	212.7	186.2	1,586.7	1,185.9	$46.1	$34.4
Membership associations & organizations	307.1	296.3	1,991.2	1,458.7	$90.1	$65.1
Private households	[b]	[b]	[c]	[c]	[c]	[c]
Public administration [d]	90.1	72.8	7,076.8	689.9	$419.4	$35.6
Employer Type						
Non-profit, private[e]	566.7	489	9,658.10	3,997.00	$472.70	$176.10
For profit, private	6,865.10	5,491.30	105,094.30	43,310.80	$4,849.50	$1,979.40

Government (state and local)	90.1	72.8	17,819.60	2,460.90	$896.60	$120.00

Note: Establishment data are from the Survey of U.S. Businesses 2012; worker and payroll data from CPS MORG using pooled data for FY2013-FY2015 projected to reflect FY2017.
[a] Excludes the self-employed and unpaid workers.
[b] SUSB does not provide information on private households.
[c] Data not displayed because sample size of affected workers in small establishments is less than 10.
[d] Establishment number represents the total number of governments, including state and local. Data from Government Organization Summary Report: 2012.
[e] 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 reliable way of estimating this population. The estimates also do not exclude workers at non-covered enterprises who are not individually covered (because the estimates assume all workers are employed by covered entities). Although not excluding workers who work for non-covered enterprises would only impact a small percentage of workers generally, it may have a larger impact (and result in a larger overestimate) for workers in non-profits because when determining enterprise coverage only revenue derived from business operations, not charitable activities, are included.

iv. Number of Affected Small Entities and Employees

For this Final Rule analysis, to estimate the probability that an exempt EAP worker 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 1 out of every 2 exempt EAP workers in this industry is expected to be employed by a small establishment.[298] The Department applied these probabilities to the population of exempt EAP workers in order to find the number of workers (total exempt EAP workers and total affected by the rule) employed by small entities. No data are available to determine whether small businesses (or small businesses in specific industries) are more or less likely than non-small

[298] 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, over half of these industry codes contain 7 or fewer observations, including one fifth that have one or zero observations. The Department does not consider any breakdowns based on these numbers reliable.

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.[299]

The Department estimated that 1.6 million of the 4.2 million affected workers (37.1 percent) are employed by small entities (Table 38). This composes about 3.1 percent of the 49.8 million workers employed by small entities. The sectors with the highest total number of affected workers employed by small establishments are: professional and technical services (256,800); health care services, except hospitals (148,900); and retail trade (147,000). The sectors with the largest percent of small business workers who are affected include: management of companies and enterprises (8.9 percent); motion picture and sound recording (7.6 percent); and insurance (7.2 percent).

Table 38: 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	136,307.0	49,768.7	4,227.6	1,567.5
Industry				
Agriculture	[c]	[c]	[c]	[c]
Forest., log., fish., hunt., and trap.	[c]	[c]	[c]	[c]
Mining	1,041.1	420.3	21.8	11.8
Construction	7,458.5	4,704.7	127.3	83.1
Nonmetallic mineral prod. manuf.	400.6	192.3	7.1	3.9
Prim. metals and fab. metal prod.	1,623.1	999.0	29.5	18.1
Machinery manufacturing	1,312.5	715.2	32.1	17.4
Computer and elect. prod. manuf.	1,283.3	598.8	47.9	22.1
Electrical equip., appliance manuf.	[c]	[c]	[c]	[c]
Transportation equip. manuf.	2,340.0	600.1	47.9	14.0

[299] 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.

Wood products	386.7	260.6	7.0	4.8
Furniture and fixtures manuf.	380.8	274.7	7.9	5.6
Misc. and not spec. manuf.	1,355.5	801.2	44.4	26.9
Food manufacturing	1,676.7	769.2	27.5	13.1
Beverage and tobacco products	279.4	138.3	5.9	2.8
Textile, app., and leather manuf.	532.8	365.5	16.1	10.4
Paper and printing	880.4	491.1	25.8	14.3
Petroleum and coal prod. manuf.	[c]	[c]	[c]	[c]
Chemical manufacturing	1,316.6	538.3	37.7	12.7
Plastics and rubber products	502.0	235.9	12.1	6.5
Wholesale trade	3,474.1	1,572.2	144.5	62.1
Retail trade	15,618.2	5,224.8	417.9	147.0
Transport. and warehousing	5,780.1	1,481.6	101.8	23.3
Utilities	1,264.6	260.0	31.1	6.9
Publishing ind. (ex. internet)	562.0	242.9	32.3	14.7
Motion picture and sound recording	332.6	119.4	22.6	9.1
Broadcasting (except internet)	580.2	129.1	38.5	8.2
Internet publishing and broadcasting	[c]	[c]	[c]	[c]
Telecommunications	961.6	189.1	44.7	7.7
Internet serv. providers and data	[c]	[c]	[c]	[c]
Other information services	258.4	75.9	21.4	4.0
Finance	4,440.6	689.2	277.0	46.3
Insurance	2,613.4	670.4	199.3	48.3
Real estate	1,886.0	1,150.2	78.4	44.9
Rental and leasing services	374.0	109.7	15.9	5.1
Professional and technical services	8,793.5	4,164.1	538.1	256.8
Management of companies and enterprises	181.9	55.1	16.3	4.9
Admin. and support services	4,905.9	2,186.4	136.9	49.7
Waste manag. and remed. services	524.3	209.9	12.8	5.9
Educational services	13,615.2	3,008.1	230.2	44.0
Hospitals	6,979.2	336.9	241.5	13.2
Health care services, except hospitals	10,000.5	4,754.6	329.3	148.9
Social assistance	2,829.2	1,567.8	155.2	91.5
Arts, entertainment, and recreation	2,591.0	1,255.8	124.4	66.9
Accommodation	1,511.1	557.6	26.6	11.5
Food services and drinking places	8,534.3	2,315.2	84.0	26.1
Repair and maintenance	1,572.6	1,167.9	36.0	27.3
Personal and laundry services	1,586.7	1,185.9	23.0	16.3
Membership associations & organizations	1,991.2	1,458.7	115.8	84.5
Private households	[c]	[c]	[c]	[c]
Public administration [d]	7,076.8	689.9	201.4	16.5

Employer Type				
Non-profit, private [e]	9,658.10	3,997.00	456.2	216.2
For profit, private	105,094.30	43,310.80	3,308.80	1,306.80
Government (state and local)	17,819.60	2,460.90	451.7	44.5

Note: Establishment data are from the Survey of U.S. Businesses 2012; worker data are from CPS MORG using pooled data for FY2013-FY2015 projected to reflect FY2017.
[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 to 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 governments, including state and local.
[c] Data not displayed because sample size of affected workers in small establishments is less than 10.
[e] 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 reliable way of estimating this population. The estimates also do not exclude workers at non-covered enterprises who are not individually covered (because the estimates assume all workers are employed by covered entities). Although not excluding workers who work for non-covered enterprises would only impact a small percentage of workers generally, it may have a larger impact (and result in a larger overestimate) for workers in non-profits because when determining enterprise coverage only revenue derived from business operations, not charitable activities, are included.

The Department estimated a range of impacts for small entities. To estimate the number of small establishments that will be affected because they employ affected workers the Department assumed that each small establishment employs no more than one affected worker, meaning that at most 1.6 million of the 6.0 million small establishments will employ an affected worker.[300] Thus, these assumptions provide an upper bound estimate of the number of affected small establishments (although it provides a lower bound estimate of the impact per small establishment because costs are spread over a larger number of establishments).[301]

The impacts experienced by an establishment, measured by regulatory costs and payroll increases incurred relative to its financial resources (e.g., payroll or revenues), will increase as

[300] This assumes 1.6 million of the 4.2 million affected workers are employed in small businesses (see Table 3).
[301] Note that if we underestimated the number of affected workers employed by small businesses, then we underestimated the upper bound of the number of affected small businesses.

the share of its workers that are affected increases.[302] The most severe impacts are most likely to be incurred by establishments in which all employees are affected workers, regardless of establishment size. 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 assumes 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.[303] The average number of employees in a small establishment is the number of workers employed by small establishments 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. Since SUSB data provides no information on how affected workers are distributed between these entities, the Department calculated an upper and a lower bound of affected employees per small entity (which, in turn, is associated with an lower and upper bound of the number of affected

[302] Larger establishments are likely to have larger costs than smaller firms since impacts (measured by the absolute dollar value of costs and transfers) will increase as establishment size increases; an establishment employing 50 affected workers will pay greater costs and transfers than one employing 10 affected workers. However, when measured as a percent of payroll and revenues, an establishment with 10 affected employees out of 20 total employees should experience fairly similar impacts as those experienced by an establishment employing 50 affected workers out of 100 employees.

[303] 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.

small entities—and an upper and lower bound of impact per entity; the fewer affected employees, the lower the cost per entity).

Table 38 summarizes the estimated number of affected workers employed by small establishments and the expected range for the number of affected small establishments by industry. The Department estimated that the rule will affect 1.6 million workers who are employed by somewhere between 210,800 and 1.6 million small establishments; this composes from 3.5 percent to 25.9 percent of all small establishments. It also means that from 4.5 million to 5.9 million small establishments incur no more than minimal regulatory familiarization costs (i.e., 6.0 million minus 1.6 million equals 4.5 million; 6.0 million minus 210,000 equals 5.9 million, using rounded values). The table also presents the average number of affected employees per establishment using the method where 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 (Table 37) by the number of small businesses (Table 37) (applicable to both methods).

Table 39: Number of Small Affected Establishments and Employees by Industry and Employer Type

Industry	Affected Workers (1,000s)	Number of 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	1,567.5	1,567.5	210.8	7.4	376.1
Industry					
Agriculture	[d]	[d]	[d]	[d]	[d]

Forest., log., fish., hunt., and trap.	[d]	[d]	[d]	[d]	[d]
Mining	11.8	11.8	0.7	18.0	1,268.4
Construction	83.1	83.1	11.2	7.4	361.5
Nonmetallic mineral prod. manuf.	3.9	3.9	0.2	16.4	808.4
Prim. metals and fab. metal prod.	18.1	18.1	1.0	17.7	863.7
Machinery manufacturing	17.4	17.4	0.5	32.4	1,771.8
Computer and elect. prod. manuf.	22.1	22.1	0.4	50.8	3,800.1
Electrical equip., appliance manuf.	[d]	[d]	[d]	[d]	[d]
Transportation equip. manuf.	14.0	14.0	0.2	58.9	3,337.6
Wood products	4.8	4.8	0.2	20.7	841.2
Furniture and fixtures manuf.	5.6	5.6	0.3	17.3	669.8
Misc. and not spec. manuf.	26.9	26.9	1.0	28.1	1,454.3
Food manufacturing	13.1	13.1	0.4	33.9	1,245.8
Beverage and tobacco products	2.8	2.8	0.1	30.5	1,570.2
Textile, app., and leather manuf.	10.4	10.4	0.4	23.2	896.8
Paper and printing	14.3	14.3	0.9	16.5	758.7
Petroleum and coal prod. manuf.	[d]	[d]	[d]	[d]	[d]
Chemical manufacturing	12.7	12.7	0.3	51.0	3,244.6
Plastics and rubber products	6.5	6.5	0.3	22.2	1,000.2
Wholesale trade	62.1	62.1	13.2	4.7	246.5
Retail trade	147.0	147.0	19.3	7.6	278.8
Transport. and warehousing	23.3	23.3	2.7	8.7	384.2
Utilities	6.9	6.9	0.2	34.1	2,075.4
Publishing ind. (ex. internet)	14.7	14.7	1.3	11.6	671.5
Motion picture and sound recording	9.1	9.1	1.7	5.5	299.1
Broadcasting (except internet)	8.2	8.2	0.3	24.2	1,363.6
Internet publishing and broadcasting	[d]	[d]	[d]	[d]	[d]
Telecommunications	7.7	7.7	0.4	17.1	1,118.1
Internet serv. providers and data	[d]	[d]	[d]	[d]	[d]
Other information services	4.0	4.0	0.2	24.3	979.4
Finance	46.3	46.3	7.7	6.0	406.3
Insurance	48.3	48.3	9.9	4.9	295.1
Real estate	44.9	44.9	9.8	4.6	220.7
Rental and leasing services	5.1	5.1	1.3	4.1	162.2
Professional and technical services	256.8	256.8	48.0	5.3	370.2
Management of companies and enterprises	4.9	4.9	2.9	1.7	100.1
Admin. and support services	49.7	49.7	7.1	7.0	236.5
Waste manag. and remed. services	5.9	5.9	0.5	11.8	529.8
Educational services	44.0	44.0	1.2	35.8	1,691.5
Hospitals	13.2	13.2	0.1	214.7	12,069.1

Health care services, except hospitals	148.9	148.9	17.1	8.7	368.0
Social assistance	91.5	91.5	7.8	11.8	373.2
Arts, entertainment, and recreation	66.9	66.9	6.1	10.9	377.9
Accommodation	11.5	11.5	1.1	10.4	348.2
Food services and drinking places	26.1	26.1	5.3	4.9	113.9
Repair and maintenance	27.3	27.3	4.6	5.9	233.5
Personal and laundry services	16.3	16.3	2.6	6.4	184.6
Membership associations & organizations	84.5	84.5	17.2	4.9	219.8
Private households	[d]	[d]	[d]	[d]	[d]
Public administration [e]	16.5	16.5	1.7	9.5	489.0
Employer Type					
Non-profit, private [f]	216.2	216.2	26.4	8.2	$360.20
For profit, private	1,306.80	1,306.80	165.7	7.9	$360.50
Government (state and local)	44.5	44.5	1.3	33.8	$1,646.70

Note: Establishment data are from the Survey of U.S. Businesses 2012; worker and payroll data from CPS MORG using pooled data for FY2013-FY2015 projected to reflect FY2017.
[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 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 impacts 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 7.42 workers (4.70 million employees divided by 634,330 small establishments). This method assumes if an establishment is affected then all 7.42 workers are affected. Therefore, in the construction industry this method estimates there are 11,200 small affected establishments (83,100 affected small workers divided by 7.42).
[d] Data not displayed because sample size of affected workers in small establishments is less than 10.
[e] Establishment number represents the total number of state and local governments.
[f] 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 reliable way of estimating this population. The estimates also do not exclude workers at non-covered enterprises who are not individually covered (because the estimates assume all workers are employed by covered entities). Although not excluding workers who work for non-covered enterprises would only impact a small percentage of workers generally, it may have a larger impact (and result in a larger overestimate) for workers in non-profits because when

determining enterprise coverage only revenue derived from business operations, not charitable activities, are included.

v. Projected Impacts to Affected Small Entities

For small entities, the Department projected annual per-entity costs and payroll increases, including: regulatory familiarization costs, adjustment costs, managerial costs, and payroll increases to employees. The Department estimates a range for the number of small affected establishments and the impacts they incur. However, few establishments are likely to incur the costs, payroll increases, and impacts at the upper end of this range because it seems unlikely that all employees at a small firm are workers affected by this Final Rule. While the upper and lower bounds are likely over- and under-estimates, respectively, of regulatory costs and increased payroll per small establishment, the Department believes that this range of costs and payroll increases provides the most accurate characterization of the impacts of the rule on small employers.[304] 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

[304] 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.

expects that many, if not most, entities will incur smaller costs, payroll increases, and impacts relative to establishment size.

As a result of this rule, the Department expects total direct employer costs will range from $157.9 million to $206.8 million for affected small establishments (Table 40) in the first year after the promulgation of the Final Rule. An additional $162.3 million to $211.5 million in regulatory familiarization costs will be incurred by small establishments that do not employ affected workers. The three industries with the highest total number of affected workers in small establishments (professional and technical services; healthcare services, except hospitals; and retail trade) account for about 35 percent of the costs. The largest cost per establishment is expected to be incurred in the hospitals industry ($20,629 using the method where all employees are affected), although the costs are not expected to exceed 0.17 percent of payroll. The largest impact as a share of payroll is projected to be incurred in the food services and drinking places industry, where estimated direct costs compose 0.45 percent of average entity payroll.

Table 40: 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	$206.8	$132	0.04%	$157.9	$749	0.20%
Industry						
Agriculture	[c]	[c]	[c]	[c]	[c]	[c]
Forest., log., fish., hunt., and trap.	[c]	[c]	[c]	[c]	[c]	[c]
Mining	$1.6	$132	0.01%	$1.2	$1,765	0.14%
Construction	$11.0	$132	0.04%	$8.4	$748	0.21%

Nonmetallic mineral prod. manuf.	$0.5	$132	0.02%	$0.4	$1,613	0.20%
Prim. metals and fab. metal prod.	$2.4	$132	0.02%	$1.8	$1,734	0.20%
Machinery manufacturing	$2.3	$132	0.01%	$1.7	$3,145	0.18%
Computer and elect. prod. manuf.	$2.9	$132	0.00%	$2.1	$4,905	0.13%
Electrical equip., appliance manuf.	[c]	[c]	[c]	[c]	[c]	[c]
Transportation equip. manuf.	$1.8	$132	0.00%	$1.3	$5,690	0.17%
Wood products	$0.6	$132	0.02%	$0.5	$2,023	0.24%
Furniture and fixtures manuf.	$0.7	$132	0.02%	$0.5	$1,696	0.25%
Misc. and not spec. manuf.	$3.6	$132	0.01%	$2.6	$2,734	0.19%
Food manufacturing	$1.7	$132	0.01%	$1.3	$3,287	0.26%
Beverage and tobacco products	$0.4	$132	0.01%	$0.3	$2,963	0.19%
Textile, app., and leather manuf.	$1.4	$132	0.01%	$1.0	$2,265	0.25%
Paper and printing	$1.9	$132	0.02%	$1.4	$1,618	0.21%
Petroleum and coal prod. manuf.	[c]	[c]	[c]	[c]	[c]	[c]
Chemical manufacturing	$1.7	$132	0.00%	$1.2	$4,923	0.15%
Plastics and rubber products	$0.9	$132	0.01%	$0.6	$2,168	0.22%
Wholesale trade	$8.2	$132	0.05%	$6.4	$487	0.20%
Retail trade	$19.4	$132	0.05%	$14.8	$767	0.28%
Transport. and warehousing	$3.1	$132	0.03%	$2.3	$869	0.23%
Utilities	$0.9	$132	0.01%	$0.7	$3,308	0.16%
Publishing ind. (ex. internet)	$1.9	$132	0.02%	$1.5	$1,152	0.17%
Motion picture and sound recording	$1.2	$132	0.04%	$0.9	$564	0.19%
Broadcasting (except internet)	$1.1	$132	0.01%	$0.8	$2,352	0.17%
Internet publishing and broadcasting	[c]	[c]	[c]	[c]	[c]	[c]
Telecommunications	$1.0	$132	0.01%	$0.7	$1,673	0.15%
Internet serv. providers and data	[c]	[c]	[c]	[c]	[c]	[c]
Other information services	$0.5	$132	0.01%	$0.4	$2,363	0.24%
Finance	$6.1	$132	0.03%	$4.7	$611	0.15%
Insurance	$6.4	$132	0.04%	$5.0	$503	0.17%
Real estate	$5.9	$132	0.06%	$4.7	$475	0.22%
Rental and leasing services	$0.7	$132	0.08%	$0.5	$428	0.26%
Professional and technical services	$33.9	$132	0.04%	$26.4	$549	0.15%
Management of companies and enterprises	$0.6	$132	0.13%	$0.6	$200	0.20%
Admin. and support services	$6.6	$132	0.06%	$5.0	$711	0.30%
Waste manag. and remed. services	$0.8	$132	0.02%	$0.6	$1,167	0.22%
Educational services	$5.8	$132	0.01%	$4.3	$3,471	0.21%
Hospitals	$1.8	$132	0.00%	$1.3	$20,629	0.17%
Health care services, except hospitals	$19.7	$132	0.04%	$14.9	$872	0.24%

Social assistance	$12.1	$132	0.04%	$9.1	$1,166	0.31%
Arts, entertainment, and recreation	$8.8	$132	0.03%	$6.6	$1,082	0.29%
Accommodation	$1.5	$132	0.04%	$1.1	$1,032	0.30%
Food services and drinking places	$3.4	$132	0.12%	$2.7	$508	0.45%
Repair and maintenance	$3.6	$132	0.06%	$2.8	$607	0.26%
Personal and laundry services	$2.2	$132	0.07%	$1.7	$647	0.35%
Membership associations & organizations	$11.2	$132	0.06%	$8.7	$508	0.23%
Private households	[c]	[c]	[c]	[c]	[c]	[c]
Public administration	$2.2	$132	0.03%	$1.6	$945	0.19%
Employer Type						
Non-profit, private [d]	$28.70	$133	0.04%	$21.80	$824	0.23%
For profit, private	$177.40	$136	0.04%	$136.10	$821	0.23%
Government (state and local)	$5.20	$116	0.01%	$3.60	$2,723	0.17%

Note: pooled data for FY2013-FY2015 projected to reflect FY2017.

[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 because sample size of affected workers in small establishments is less than 10.

[d] 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 reliable way of estimating this population. The estimates also do not exclude workers at non-covered enterprises who are not individually covered (because the estimates assume all workers are employed by covered entities). Although not excluding workers who work for non-covered enterprises would only impact a small percentage of workers generally, it may have a larger impact (and result in a larger overestimate) for workers in non-profits because when determining enterprise coverage only revenue derived from business operations, not charitable activities, are included.

Average weekly earnings for affected EAP workers in small establishments are expected to increase by about $6.51 per week per affected worker, using the partial employment contract model[305] described in section VI.D.iv.[306] This would lead to $530.4 million in additional annual

[305] As explained in section VI.D.iv., the partial employment contract model reflects the Department's determination that an appropriate estimate of the impact on the implicit hourly rate of pay for regular overtime workers after the Final Rule should be determined using the average

wage payments to employees in small entities (less than 0.7 percent of aggregate affected establishment payroll; Table 40). The largest payroll increases per establishment are expected in the sectors of hospitals (up to $54,430 per entity); food manufacturing (up to $26,158 per entity); and transportation equipment manufacturing (up to $20,666 per entity). However, average payroll increases per establishment exceed 2 percent of average payroll in only two sectors: food services and drinking places (3.53 percent) and food manufacturing (2.10 percent).

Table 41: 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	$530.4	$338	0.09%	$2,516	0.67%
Industry					
Agriculture	[b]	[b]	[b]	[b]	[b]
Forest., log., fish., hunt., and trap.	[b]	[b]	[b]	[b]	[b]
Mining	$6.0	$509	0.04%	$9,184	0.72%
Construction	$35.9	$433	0.12%	$3,209	0.89%
Nonmetallic mineral prod. manuf.	$0.8	$193	0.02%	$3,176	0.39%
Prim. metals and fab. metal prod.	$3.0	$163	0.02%	$2,893	0.33%
Machinery manufacturing	$4.1	$238	0.01%	$7,704	0.43%
Computer and elect. prod. manuf.	$8.6	$390	0.01%	$19,810	0.52%
Electrical equip., appliance manuf.	[b]	[b]	[b]	[b]	[b]
Transportation equip. manuf.	$4.9	$351	0.01%	$20,666	0.62%
Wood products	$3.0	$639	0.08%	$13,238	1.57%
Furniture and fixtures manuf.	$0.5	$95	0.01%	$1,638	0.24%
Misc. and not spec. manuf.	$12.8	$477	0.03%	$13,420	0.92%
Food manufacturing	$10.1	$772	0.06%	$26,158	2.10%

of Barkume's two estimates of partial employment contract model adjustments: a wage change that is 40 percent of the adjustment toward the amount predicted by the employment contract 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.

[306] 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.

Beverage and tobacco products	$0.7	$238	0.02%	$7,263	0.46%
Textile, app., and leather manuf.	$2.9	$283	0.03%	$6,565	0.73%
Paper and printing	$6.9	$478	0.06%	$7,883	1.04%
Petroleum and coal prod. manuf.	[b]	[b]	[b]	[b]	[b]
Chemical manufacturing	$2.7	$208	0.01%	$10,599	0.33%
Plastics and rubber products	$2.2	$338	0.03%	$7,518	0.75%
Wholesale trade	$22.2	$357	0.14%	$1,677	0.68%
Retail trade	$67.4	$458	0.16%	$3,492	1.25%
Transport. and warehousing	$8.9	$382	0.10%	$3,314	0.86%
Utilities	$0.4	$62	0.00%	$2,103	0.10%
Publishing ind. (ex. internet)	$3.1	$212	0.03%	$2,466	0.37%
Motion picture and sound recording	$6.6	$724	0.24%	$3,979	1.33%
Broadcasting (except internet)	$2.6	$312	0.02%	$7,540	0.55%
Internet publishing and broadcasting	[b]	[b]	[b]	[b]	[b]
Telecommunications	$0.9	$112	0.01%	$1,917	0.17%
Internet serv. providers and data	[b]	[b]	[b]	[b]	[b]
Other information services	$1.1	$270	0.03%	$6,541	0.67%
Finance	$22.6	$488	0.12%	$2,922	0.72%
Insurance	$7.0	$145	0.05%	$708	0.24%
Real estate	$17.1	$382	0.17%	$1,746	0.79%
Rental and leasing services	$1.0	$197	0.12%	$806	0.50%
Professional and technical services	$62.7	$244	0.07%	$1,304	0.35%
Management of companies and enterprises	$1.9	$378	0.38%	$647	0.65%
Admin. and support services	$15.9	$319	0.13%	$2,246	0.95%
Waste manag. and remed. services	$1.5	$252	0.05%	$2,970	0.56%
Educational services	$7.4	$168	0.01%	$6,019	0.36%
Hospitals	$3.4	$253	0.00%	$54,430	0.45%
Health care services, except hospitals	$26.3	$176	0.05%	$1,536	0.42%
Social assistance	$19.2	$210	0.06%	$2,473	0.66%
Arts, entertainment, and recreation	$35.0	$522	0.14%	$5,697	1.51%
Accommodation	$5.7	$492	0.14%	$5,115	1.47%
Food services and drinking places	$21.3	$817	0.72%	$4,019	3.53%
Repair and maintenance	$21.2	$776	0.33%	$4,612	1.98%
Personal and laundry services	$6.6	$404	0.22%	$2,571	1.39%
Membership associations & organizations	$30.2	$357	0.16%	$1,757	0.80%
Private households	[b]	[b]	[b]	[b]	[b]
Public administration	$5.1	$310	0.06%	$2,936	0.60%
Employer Type					
Non-profit, private [c]	$72.60	$336	0.19%	$2,745	0.76%

For profit, private	$449.20	$344	0.02%	$2,711	0.75%
Government (state and local)	$8.60	$194	0.16%	$6,541	0.40%

Note: pooled data for FY2013-FY2015 projected to reflect FY2017.
[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 because sample size of affected workers in small establishments is less than 10.
[c] 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 reliable way of estimating this population. The estimates also do not exclude workers at non-covered enterprises who are not individually covered (because the estimates assume all workers are employed by covered entities). Although not excluding workers who work for non-covered enterprises would only impact a small percentage of workers generally, it may have a larger impact (and result in a larger overestimate) for workers in non-profits because when determining enterprise coverage only revenue derived from business operations, not charitable activities, are included.

Table 42 presents estimated first year direct costs and payroll increases combined per establishment and those 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. Under this scenario, an affected small establishment is expected to incur between $200 and $20,629 in direct costs (Table 40) and between $647 and $54,430 in additional payroll to employees (Table 41) in the first year after the promulgation of the Final Rule. Combined costs and payroll increases per establishment range from $847 in management of companies and enterprises to $75,059 in the hospitals sector (Table 41).[307] Combined costs and payroll increases compose more than 2 percent of average establishment payroll in three sectors: food services and drinking places (3.97 percent), food manufacturing (2.36 percent), and repair and maintenance (2.24 percent). In all other sectors, they range from 0.3 percent to 1.8 percent of payroll.

[307] When a single affected worker is employed, combined costs and transfers by industry are projected to range from $194 (in utilities) to $949 (in food services and drinking places) per establishment.

However, comparing costs and payroll increases to payrolls overstates the impact to 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.[308] 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 (1.08 percent).

Table 42: 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	$688.3	$3,265	0.87%	0.17%
Industry				
Agriculture	[c]	[c]	[c]	[c]
Forest., log., fish., hunt., and trap.	[c]	[c]	[c]	[c]
Mining	$7.2	$10,950	0.86%	0.13%
Construction	$44.3	$3,956	1.09%	0.24%
Nonmetallic mineral prod. manuf.	$1.1	$4,790	0.59%	0.11%
Prim. metals and fab. metal prod.	$4.7	$4,627	0.54%	0.12%
Machinery manufacturing	$5.8	$10,849	0.61%	0.13%
Computer and elect. prod. manuf.	$10.8	$24,715	0.65%	0.15%
Electrical equip., appliance manuf.	[c]	[c]	[c]	[c]
Transportation equip. manuf.	$6.3	$26,35	0.79%	0.13%

[308] The ratio of revenues to payroll for small businesses ranged from 2.14 (social assistance) to 43.69 (petroleum and coal products manufacturing), with an average over all sectors of 5.15. The Department used this estimate of revenue, instead of small business revenue reported directly from the 2012 SUSB so revenue aligned with projected payrolls in FY2017.

		6		
Wood products	$3.5	$15,261	1.81%	0.31%
Furniture and fixtures manuf.	$1.1	$3,334	0.50%	0.12%
Misc. and not spec. manuf.	$15.5	$16,154	1.11%	0.28%
Food manufacturing	$11.4	$29,445	2.36%	0.22%
Beverage and tobacco products	$1.0	$10,227	0.65%	0.08%
Textile, app., and leather manuf.	$4.0	$8,829	0.98%	0.16%
Paper and printing	$8.3	$9,501	1.25%	0.28%
Petroleum and coal prod. manuf.	[c]	[c]	[c]	[c]
Chemical manufacturing	$3.9	$15,522	0.48%	0.04%
Plastics and rubber products	$2.8	$9,685	0.97%	0.15%
Wholesale trade	$28.6	$2,163	0.88%	0.06%
Retail trade	$82.2	$4,260	1.53%	0.15%
Transport. and warehousing	$11.2	$4,183	1.09%	0.25%
Utilities	$1.1	$5,411	0.26%	0.02%
Publishing ind. (ex. internet)	$4.6	$3,618	0.54%	0.19%
Motion picture and sound recording	$7.5	$4,543	1.52%	0.40%
Broadcasting (except internet)	$3.4	$9,892	0.73%	0.26%
Internet publishing and broadcasting	[c]	[c]	[c]	[c]
Telecommunications	$1.6	$3,591	0.32%	0.05%
Internet serv. providers and data	[c]	[c]	[c]	[c]
Other information services	$1.5	$8,905	0.91%	0.36%
Finance	$27.3	$3,533	0.87%	0.31%
Insurance	$12.0	$1,211	0.41%	0.09%
Real estate	$21.8	$2,220	1.01%	0.22%
Rental and leasing services	$1.6	$1,234	0.76%	0.19%
Professional and technical services	$89.0	$1,853	0.50%	0.20%
Management of companies and enterprises	$2.4	$847	0.85%	0.17%
Admin. and support services	$20.9	$2,957	1.25%	0.56%
Waste manag. and remed. services	$2.1	$4,137	0.78%	0.20%
Educational services	$11.6	$9,489	0.56%	0.22%
Hospitals	$4.6	$75,059	0.62%	0.27%
Health care services, except hospitals	$41.2	$2,408	0.65%	0.28%
Social assistance	$28.3	$3,639	0.98%	0.45%
Arts, entertainment, and recreation	$41.6	$6,779	1.79%	0.59%
Accommodation	$6.8	$6,148	1.77%	0.44%

Food services and drinking places	$24.0	$4,527	3.97%	1.08%
Repair and maintenance	$23.9	$5,219	2.24%	0.63%
Personal and laundry services	$8.2	$3,218	1.74%	0.60%
Membership associations & organizations	$38.9	$2,266	1.03%	0.26%
Private households	[c]	[c]	[c]	[c]
Public administration	$6.8	$3,881	0.79%	0.22%
Employer Type				
Non-profit, private [d]	$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 data for FY2013-FY2015 projected to reflect FY2017.
[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 2012 Census of Governments.
[c] Data not displayed because sample size of affected workers in small establishments is less than 10.
[d] 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 reliable way of estimating this population. The estimates also do not exclude workers at non-covered enterprises who are not individually covered (because the estimates assume all workers are employed by covered entities). Although not excluding workers who work for non-covered enterprises would only impact a small percentage of workers generally, it may have a larger impact (and result in a larger overestimate) for workers in non-profits because when determining enterprise coverage only revenue derived from business operations, not charitable activities, are included.

The Department also considered costs and payroll increases relative to profits (Table 43). The denominator is all profits in an industry, rather than profits per affected establishment. In Table 42 we compared costs and payroll increases to payroll and revenue per establishment; therefore, the numbers in Table 42 and Table 43 are not directly comparable. The broader denominator was used for the profit analysis to be consistent with the profit analysis conducted for the 2004 Final Rule. Due to the broader denominator, total costs and payroll increases in this table include regulatory familiarization costs to non-affected small establishments. Additionally, this

table differs from Table 42 because it is conducted at the more aggregated 13 major industry level. This is due to data limitations in the profit data.[309, 310]

Benchmarking against profit is potentially helpful in the sense that it provides a measure of the Final Rule's effect against returns to investment and possible adjustments arising from changes in that outcome. However, this metric must be interpreted carefully as it does not account for differences across industries in terms of risk-adjusted rates of return, nor does it reflect differences in the firm-level adjustment to profit impacts reflecting cross-industry variation in market structure. Costs and payroll increases as a percent of profits are highest in leisure and hospitality industry (although the information industry may be more affected because profits are negative). However, the magnitude of the relative shares is small, representing less than 0.8 percent of profits in each industry and 0.14 percent in aggregate. Similarly, costs and payroll increases as a percent of either payroll or revenue are highest in the leisure and hospitality industry.

Table 43: Year 1 Small Establishment Direct Costs and Payroll Increases, by Industry

Industry	Costs and Payroll Increases for All Small Establishments			
	Total (Millions) [a]	Percent of Annual Payroll	Percent of Estimated Revenues [b]	Percent of Profits [c]
Total	$899.9	0.04%	0.01%	0.14%
Industry				
Agriculture, forestry, fishing, & hunting	$1.4	0.01%	0.00%	0.02%

[309] Internal Revenue Service. (2012). Corporation Income Tax Returns. Available at: https://www.irs.gov/pub/irs-soi/12coccr.pdf.

[310] Table 5 of the IRS report provides information on total receipts and net income (less deficits) by size of business receipts, but is only available at a 2-digit NAICS level. The Department used the small business share of total revenues by industry from the 2012 SUSB data to approximate the appropriate business receipt sizes to include in the calculation of the profit ratio from the IRS data. The Department calculated the profit ratio as net income (less deficits) to receipts for small businesses in each industry. This ratio was then applied to revenue data to estimate profits.

Mining	$8.0	0.03%	0.00%	0.17%
Construction	$66.9	0.03%	0.01%	0.19%
Manufacturing	$89.7	0.02%	0.00%	0.09%
Wholesale & retail trade	$146.5	0.05%	0.00%	0.20%
Transportation & utilities	$18.7	0.02%	0.00%	0.16%
Information	$22.6	0.05%	0.01%	[d]
Financial activities	$80.8	0.05%	0.01%	0.06%
Professional & business services	$153.6	0.04%	0.02%	0.25%
Education & health services	$112.5	0.03%	0.01%	0.11%
Leisure & hospitality	$95.1	0.08%	0.02%	0.75%
Other services	$94.8	0.07%	0.02%	0.48%
Public administration	$9.4	0.03%	0.01%	[e]

Note: pooled data for FY2013-FY2015 projected to reflect FY2017.
[a] Total costs and payroll increases include regulatory familiarization costs to non-affected small establishments.
[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 2012 Census of Governments.
[c] Profit data based on corporations only. IRS data disaggregates net income data by business receipt size. Because the SBA standards for small businesses in some industries are based on number of employees, the Department had to estimate which receipt size categories to consider as small businesses.
[d] Profits in this industry were negative in the 2012 Corporation Income Tax Returns, Statistics of Income, IRS.
[e] Profit is not applicable for public administration.

vi. Projected Impacts 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 business for nine years after Year 1 of the rule. Projected employment and earnings were calculated using the same methodology described in Section VI.B.ii. Affected employees in small firms follow a similar pattern to affected workers in all establishments. The number decreases gradually in years without automatic updates, but the increases in years with automatic updates offset this fall and result in a net growth over time. There are 1.6 million affected workers in small establishments in Year 1 and 2.0 million in Year 10. Table 44 reports affected workers only in years when the salary level increases.

Table 44: Projected Number of Affected Workers in Small Establishments, by Industry

Industry	Affected Workers in Small Establishments (1,000s)			
	Year 1	Year 4	Year 7	Year 10
Total	1,567.5	1,711.1	1,838.2	1,955.3
Agriculture	[a]	[a]	[a]	2.4
Forest., log., fish., hunt., and trap.	[a]	[a]	[a]	[a]
Mining	11.8	14.0	14.8	16.2
Construction	83.1	90.2	98.3	106.1
Nonmetallic mineral prod. manuf.	3.9	4.8	4.7	5.5
Prim. metals and fab. metal prod.	18.1	18.9	18.6	19.4
Machinery manufacturing	17.4	17.7	17.8	17.1
Computer and elect. prod. manuf.	22.1	21.7	22.2	22.3
Electrical equip., appliance manuf.	[a]	[a]	[a]	[a]
Transportation equip. manuf.	14.0	14.2	14.1	13.7
Wood products	4.8	4.8	4.7	4.8
Furniture and fixtures manuf.	5.6	5.4	5.4	5.2
Misc. and not spec. manuf.	26.9	27.7	28.8	28.5
Food manufacturing	13.1	16.0	17.6	17.5
Beverage and tobacco products	2.8	2.8	3.5	3.4
Textile, app., and leather manuf.	10.4	11.6	11.6	11.8
Paper and printing	14.3	15.5	16.6	17.1
Petroleum and coal prod. manuf.	[a]	[a]	[a]	[a]
Chemical manufacturing	12.7	13.8	14.9	16.7
Plastics and rubber products	6.5	6.6	6.1	6.0
Wholesale trade	62.1	69.5	72.5	77.0
Retail trade	147.0	161.3	174.9	186.5
Transport. and warehousing	23.3	24.9	28.9	32.2

Utilities	6.9	6.7	7.4	7.3
Publishing ind. (ex. internet)	14.7	15.2	17.4	17.7
Motion picture and sound recording	9.1	9.5	10.4	10.5
Broadcasting (except internet)	8.2	8.8	10.1	11.0
Internet publishing and broadcasting	[a]	[a]	[a]	[a]
Telecommunications	7.7	8.1	8.7	8.8
Internet serv. providers and data	[a]	[a]	3.1	3.2
Other information services	4.0	4.0	4.4	4.4
Finance	46.3	49.2	51.5	53.9
Insurance	48.3	50.9	56.4	59.5
Real estate	44.9	50.1	56.2	61.4
Rental and leasing services	5.1	5.6	5.7	5.8
Professional and technical services	256.8	278.6	296.8	314.0
Management of companies and enterprises	4.9	5.4	6.9	7.5
Admin. and support services	49.7	56.0	60.5	65.1
Waste manag. and remed. services	5.9	7.6	9.5	10.1
Educational services	44.0	46.9	51.2	56.0
Hospitals	13.2	15.4	15.8	17.2
Health care services, except hospitals	148.9	165.9	182.4	199.0
Social assistance	91.5	105.8	115.4	123.3
Arts, entertainment, and recreation	66.9	71.4	75.6	82.8
Accommodation	11.5	12.5	12.9	14.6
Food services and drinking places	26.1	29.1	31.5	33.1
Repair and maintenance	27.3	29.9	31.1	33.4
Personal and laundry services	16.3	17.4	19.4	20.2
Membership associations and organizations	84.5	93.2	96.6	101.8
Private households	[a]	[a]	[a]	[a]
Public administration	16.5	17.8	18.4	19.4

Note: Worker data are from CPS MORG using pooled data for FY2013-FY2015 projected to reflect FY2017 in Year 1.

[a] Data not displayed because sample size of affected workers in small establishments is less than 10.

Costs to small establishments decrease in the years following Year 1 because regulatory familiarization costs are zero in years without automatic updates, and adjustment costs are significantly smaller in years without automatic updating. However, both direct costs and

payroll increase over time as more workers become affected, leading to higher managerial costs and earnings for affected workers. Therefore, by Year 10 additional costs and payroll to small businesses have increased from $688.3 in Year 1 to $901.8 in Year 10 (Table 45). Despite this increase over the 10-year period, even in Year 10 costs and payroll increases are a relatively negligible 0.04 percent and 0.01 percent share of payroll and revenue respectively, assuming no growth in real firm payroll or revenues. 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 45: Projected Small Establishment Direct Costs and Payroll Increases, by Industry, Using All Employees in Establishment Affected Method

Industry	Costs and Payroll Increases for Small Affected Establishments, All Employees Affected (Millions)			
	Year 1	Year 4	Year 7	Year 10
Total	$688.3	$629.3	$749.3	$901.8
Agriculture	[a]	[a]	[a]	$3.9
Forest., log., fish., hunt., and trap.	[a]	[a]	[a]	[a]
Mining	$7.2	$12.8	$15.0	$17.6
Construction	$44.3	$34.5	$44.3	$51.9
Nonmetallic mineral prod. manuf.	$1.1	$1.5	$1.7	$2.8
Prim. metals and fab. metal prod.	$4.7	$4.3	$4.3	$5.1
Machinery manufacturing	$5.8	$4.3	$4.4	$4.4
Computer and elect. prod. manuf.	$10.8	$14.8	$18.0	$21.1
Electrical equip., appliance manuf.	[a]	[a]	[a]	[a]
Transportation equip. manuf.	$6.3	$6.3	$6.2	$6.1
Wood products	$3.5	$5.7	$5.9	$6.4
Furniture and fixtures manuf.	$1.1	$0.7	$0.7	$0.7
Misc. and not spec. manuf.	$15.5	$13.0	$15.1	$16.1
Food manufacturing	$11.4	$10.2	$12.1	$13.5
Beverage and tobacco products	$1.0	$0.6	$1.6	$1.6
Textile, app., and leather manuf.	$4.0	$3.3	$4.8	$5.0
Paper and printing	$8.3	$7.4	$9.1	$14.7
Petroleum and coal prod. manuf.	[a]	[a]	[a]	[a]
Chemical manufacturing	$3.9	$3.8	$3.9	$5.3
Plastics and rubber products	$2.8	$2.5	$3.0	$3.3

Wholesale trade	$28.6	$28.1	$34.1	$43.8
Retail trade	$82.2	$76.7	$99.1	$125.1
Transport. and warehousing	$11.2	$8.7	$10.5	$14.5
Utilities	$1.1	$0.7	$0.7	$0.9
Publishing ind. (ex. internet)	$4.6	$5.4	$5.8	$6.4
Motion picture and sound recording	$7.5	$6.9	$7.4	$7.8
Broadcasting (except internet)	$3.4	$3.4	$4.0	$4.3
Internet publishing and broadcasting	[a]	[a]	[a]	[a]
Telecommunications	$1.6	$1.1	$1.2	$1.4
Internet serv. providers and data	[a]	[a]	$0.9	$1.0
Other information services	$1.5	$1.0	$1.9	$1.1
Finance	$27.3	$28.5	$31.8	$34.9
Insurance	$12.0	$9.4	$10.6	$11.4
Real estate	$21.8	$16.0	$20.0	$21.9
Rental and leasing services	$1.6	$1.9	$1.9	$1.9
Professional and technical services	$89.0	$81.7	$92.2	$114.0
Management of companies and enterprises	$2.4	$1.9	$2.0	$2.2
Admin. and support services	$20.9	$20.1	$27.8	$35.3
Waste manag. and remed. services	$2.1	$5.9	$5.8	$9.1
Educational services	$11.6	$9.1	$10.6	$13.1
Hospitals	$4.6	$4.3	$5.2	$5.8
Health care services, except hospitals	$41.2	$34.0	$38.9	$46.8
Social assistance	$28.3	$22.6	$24.9	$28.3
Arts, entertainment, and recreation	$41.6	$36.9	$41.5	$47.6
Accommodation	$6.8	$8.3	$11.8	$17.4
Food services and drinking places	$24.0	$21.4	$27.6	$33.0
Repair and maintenance	$23.9	$21.3	$24.3	$28.6
Personal and laundry services	$8.2	$7.1	$8.3	$8.8
Membership associations and organizations	$38.9	$33.3	$39.9	$46.7
Private households	[a]	[a]	[a]	[a]
Public administration	$6.8	$6.1	$6.4	$8.6

Note: pooled data for FY2013-FY2015 projected to reflect FY2017 in Year 1.
[a] Data not displayed because sample size of affected workers in small establishments is less than 10.

The Department projected costs and payroll increases per affected small establishment using the range for the estimated number of affected small establishments. Table 46 shows projected costs and payroll increases in Years 1, 4, 7, and 10 for the ten industries with the

highest costs and payroll increases in Year 1. Affected small establishments in the hospitals industry have the largest costs and payroll increases per establishment using the scenario where all workers employed by the establishment are affected. Using the scenario where one worker per establishment is affected, the costs and payroll increases per establishment are highest in Year 1 in the food services and drinking places industry.

Table 46: Projected Direct Costs and Payroll Increases per Small Establishment

Industry	Costs and Payroll Increases per Affected Small Establishments for Ten Industries with Highest Costs [a]			
	Year 1	Year 4	Year 7	Year 10
All Employees Affected at Small Establishment Affected				
Hospitals	$75,059	$69,034	$85,024	$93,262
Food manufacturing	$29,445	$26,410	$31,303	$34,962
Transportation equip. manuf.	$26,356	$26,656	$26,229	$25,653
Computer and elect. prod. manuf.	$24,715	$33,947	$41,226	$48,334
Misc. and not spec. manuf.	$16,154	$13,550	$15,740	$16,794
Chemical manufacturing	$15,522	$15,271	$15,543	$21,268
Wood products	$15,261	$24,826	$25,695	$27,934
Mining	$10,950	$19,532	$22,967	$26,945
Machinery manufacturing	$10,849	$7,921	$8,162	$8,231
Beverage and tobacco products	$10,227	$6,770	$17,102	$17,514
One Employee Affected at Each Small Establishment Affected				
Food services and drinking places	$949	$822	$1,059	$1,267
Repair and maintenance	$908	$783	$894	$1,051
Food manufacturing	$904	$782	$927	$1,035
Motion picture and sound recording	$856	$758	$814	$858
Wood products	$771	$1,201	$1,243	$1,351
Arts, entertainment, and recreation	$654	$553	$623	$714
Mining	$642	$1,086	$1,277	$1,497
Accommodation	$625	$721	$1,028	$1,517
Finance	$620	$619	$690	$757
Paper and printing	$610	$519	$638	$1,025

Note: pooled data for FY2013-FY2015 projected to reflect FY2017 in Year 1.
[a] Assuming no growth in number of establishments. Highest cost is based on cost in Year 1.

E. Description of the Compliance Requirements for Small Entities

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 for all hours worked and not less than one and one-half times their regular rates of pay for overtime hours worked. Every employer with covered employees 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. Thus, the recordkeeping requirements are not new requirements; however, employers would need to keep some additional records for additional affected employees (i.e., newly nonexempt workers). As indicated in this analysis, the Final Rule would expand minimum wage and overtime pay coverage to approximately 4.1 million affected EAP workers (excluding Type 4 workers who remain exempt) (section VI.D.vii.). This would 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 Final 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 significant 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 selecting the alternative adopted in the Final Rule and why other alternatives were rejected.

After considering the comments, the Department has made several changes from the proposed rule to the Final Rule. In particular, the Department has modified the standard salary level to more fully account for the salaries paid in low wage regions. In this Final Rule, the Department

sets the standard salary level equal to the 40th percentile of earnings of full-time salaried workers in the lowest-wage Census Region (currently the South). This results in a salary level of $913 per week, or $47,476 annually for a full-year worker, based on data from the fourth quarter of 2015.[311] The Department believes that a standard salary level set at the 40th percentile of full-time salaried employees in the lowest-wage Census Region 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 90th percentile of earnings of full-time salaried workers nationally ($134,004 annually based on the fourth quarter of 2015), as we proposed. This increase will bring the annual compensation requirement in line with the level established in 2004. The Department believes that this will avoid the unintended exemption of large numbers of employees in high-wage areas—such as secretaries in New York City or Los Angeles—who are clearly not performing EAP duties.

In order to prevent the salary and compensation levels from becoming outdated, the Department is including in the regulations a mechanism to automatically update the salary and compensation thresholds by maintaining the fixed percentiles of weekly earnings set in this Final Rule. In response to comments, however, the Final Rule provides for updates every three years rather than for annual updates as proposed. The first update will take effect on January 1, 2020. The Department believes that regularly updating the salary and compensation levels is the best

[311] The Bureau of Labor Statistics (BLS) estimated this value using Current Population Survey (CPS) data for earnings of full-time (defined as at least 35 hours per week) non-hourly paid employees. For the purpose of this rulemaking, the Department considers data representing compensation paid to non-hourly workers to be an appropriate proxy for compensation paid to salaried workers.

method to ensure that these tests continue to provide an effective means of distinguishing between overtime-eligible white collar employees and those who may be bona fide EAP employees. Based on historical wage growth in the South, at the time of the first update on January 1, 2020, the standard salary level is likely to be approximately $984 per week ($51,168 annually for a full-year worker) and the HCE total annual compensation requirement is likely to be approximately $147,524.

The Department also revises the regulations to permit employers for the first time 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 a quarterly or more frequent basis.

In setting the effective date of the rule, the Department responded to concerns raised about the amount of time required to evaluate and adjust to the new salary level. While the 2004 rule provided for 120 days, the final rule provides 180 days prior to the effective date.

Finally, the Department sought comments on modifications to the duties test in the proposed rule as a means to modernize overtime protections. In reviewing those comments including numerous responses from small entities, the Department decided to not make any changes to the duties tests in this Final Rule.

i. Differing Compliance and Reporting Requirements for Small Entities

This Final Rule provides no differing compliance requirements and reporting requirements for small entities. The Final Rule imposes no new reporting or recordkeeping requirements, although employers will be required to record and maintain records, as required by part 516, for additional workers if employees are reclassified from exempt to overtime-protected status. 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 inflating the 2004 standard salary level to FY2015 dollars using CPI-U (which would result in a standard salary level of $570 per week) and the most restrictive was updating the 1975 short test salary level for inflation based upon the CPI-U (which would result in a standard salary level of $1,100 per week). A lower salary level—or a degraded stagnant level over time—would result in a less effective bright-line test for separating potentially exempt workers from those nonexempt workers intended to be within the Act's protection. A low salary level will also increase the role of the duties test in determining whether an employee is exempt, which would 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. The Department found the most restrictive option to be overly burdensome on business in general, and specifically on small businesses. It was also inappropriately high given the fact that the long duties test (which was associated with a lower salary level) no longer exists.

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 to be unnecessary given the small annualized cost of the rule. The Year 1 cost of the Final Rule was estimated to be around $3,265 for a typical employer that qualifies as small, which is 0.87 percent of average annual payroll and 0.17 percent of average annual revenues. The Department makes available a variety of resources to employers for understanding their obligations and achieving compliance. Therefore the Final Rule does not provide differing compliance or reporting requirements for small businesses.

- The use of performance rather than design standards. Under the Final Rule, the employer may achieve compliance through a variety of means. The employer may elect to continue to claim the EAP exemption for affected employees by adjusting their salary level, hire additional workers or spread overtime hours to other employees, or compensate employees for overtime hours worked. The Department makes available to employers a variety of resources 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 1,500 employees (those defined as small businesses under SBA's size standards) is inconsistent with Congressional intent in the enactment of the FLSA, which applies to all employers that satisfy the enterprise coverage threshold or employ individually covered employees. See 29 U.S.C. 203(s).

F. 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), 2 U.S.C. 1501, requires agencies to prepare a written statement for rules for which a general notice of proposed 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 $156 million ($100 million in 1995 dollars adjusted for inflation) 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), 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]. . .)." 29 U.S.C. 213(a)(1). The requirements of the exemption provided by this section of the Act are contained in part 541 of the Department's regulations. Section 3(e) of the FLSA, 29 U.S.C. 203(e), 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, 29 U.S.C. 203(x), 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 UMRA, this rule includes a federal mandate that is expected to result in increased expenditures by the private sector of more than $156 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 $156 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 $115.1 million, of which $38.8 million are direct employer costs and $76.3 million are payroll increases (5). Additionally, the Final Rule will lead to $0.3 million in dead weight loss (DWL). In subsequent years, the Department estimated that state and local governments may experience payroll increases of as much as $85.4 million in a year when the salary level is automatically updated.

Costs to the private sector: The Department determined that the Final Rule will result in Year 1 costs to the private sector of approximately $1.8 billion, of which $637.7 million are direct employer costs and $1.2 billion are payroll increases. Additionally, the Final Rule will result in $6.0 million in DWL. In subsequent years, the Department estimated that the private sector may experience a payroll increase of as much as $1.5 billion per year.

Table 47: 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	4,228	3,765	452
Direct Employer Costs (Millions)			
Regulatory familiarization	$272.5	$268.9	$3.3

Adjustment	$191.4	$170.5	$20.5
Managerial	$214.0	$198.3	$15.1
Total direct costs	$677.9	$637.7	$38.8
Payroll Increases (Millions)			
From employers to workers	$1,285.2	$1,206.4	$76.3
Direct Employer Costs & Transfers (Millions)			
From employers	$1,963.1	$1,844.1	$115.1
DWL (Millions)			
DWL [b]	$6.4	$6.0	$0.3

[a] Includes only state, local, and tribal governments.
[b] DWL was estimated based on the aggregate impact of both the minimum wage and overtime pay provisions.

The largest estimated impact to workers is likely the transfer of income to workers from some combination of employers, end consumers, and other workers); but, to the extent that the utility derived by workers outweighs the disutility experienced by employers and other entities experiencing the negative side of transfers, there may be a societal welfare increase due to this transfer. The channels through which societal welfare may change , and other secondary benefits, transfers and costs may occur, include: decreased litigation costs due to fewer workers subject to the duties test, the multiplier effect of the transfer, changes in productivity, potentially reduced dependence on social assistance, and a potential increase in time off and its associated benefits to the social welfare of some workers (for instance, those who work so many hours that the overtime requirement renders their current combination of pay and hours worked non-compliant with the minimum wage). Additionally, because of the increased salary level, overtime protection will be strengthened for 5.7 million salaried white collar workers and 3.2 million salaried blue collar workers who do not meet the duties requirements for the EAP exemption, but who earn between the current minimum salary level of $455 per week and the updated salary level, because their right to minimum wage and overtime protection will be clear rather than depend upon an analysis of their duties.

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. 5 U.S.C. 1532(a)(4). However, OMB guidance on this requirement notes that such macro-economic effects tend to be measurable in nationwide econometric models only if the economic impact of the regulation reaches 0.25 percent to 0.5 percent of GDP, or in the range of $44.9 billion to $89.7 billion (using 2015 GDP). A regulation with smaller aggregate effect is not likely to have a measurable impact 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, payroll increases from employers to workers, and deadweight loss) of the Final Rule will be approximately $1.8 billion for private employers and $115.1 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 impact 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 0.03 percent of private sector payrolls nationwide.[312] Total private sector first-year costs compose 0.005 percent of national private sector revenues (revenues in FY2015 are projected to be $40.7 trillion).[313] The Department

[312] Private sector payroll costs nationwide are projected to be $5.7 trillion in FY2015. This projection is based on private sector payroll costs in 2012, which were $5.6 trillion using the 2012 Economic Census of the United States. This was inflated to FY2015 dollars using the CPI-U. Table EC0700A1: All sectors: Geographic Area Series: Economy-Wide Key Statistics: 2007.
[313] Private sector revenues in 2012 were $39.4 trillion using the 2012 Economic Census of the United States. This was inflated to FY2015 dollars using the CPI-U. Table EC0700A1: All sectors: Geographic Area Series: Economy-Wide Key Statistics: 2007.

concludes that impacts 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 approximately 0.01 percent of state and local government payrolls.[314] First-year state and local government costs compose 0.004 percent of state and local government revenues (projected FY2015 revenues were estimated to be $3.1 trillion).[315] Impacts of this magnitude will not result in significant disruptions to typical state and local governments. The $115.1 million in state and local government costs constitutes an average of approximately $1,277 for each of the approximately 90,106 state and local entities. The Department considers impacts 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 the Issuance of the NPRM

Prior to issuing the NPRM, the Department embarked on an extensive outreach program, conducting listening sessions in Washington, D.C., and several other locations, as well as by conference call. As part of this outreach program, the Department conducted stakeholder listening sessions with representatives of state, local, and tribal governments. In these sessions the Department asked stakeholders to address, among other issues, three questions: (1) what is the appropriate salary level for exemption; (2) what, if any, changes should be made to the duties

[314] Projected FY2015 payroll costs are estimated to be $878.5 billion. This projection is based on state and local payroll costs in 2012, which were reported in the Census of Governments data as $852 billion. This was inflated to FY2015 dollars using the CPI-U. 2012 Census of Governments: Employment Summary Report. Available at: http://www2.census.gov/govs/apes/2012_summary_report.pdf.

[315] State and local revenues in 2012 were reported by the Census as $3.0 trillion. This was inflated to FY2015 dollars using the CPI-U. U.S. Department of Commerce. (2014). 2012 Census of Governments: Finance— State and Local Government Summary Report. Available at: http://www2.census.gov/govs/local/summary_report.pdf.

tests; and (3) how can the regulations be simplified. The discussions in the listening sessions informed the development of the NPRM.

ii. Comments Received in Response to the NPRM

In the NPRM, the Department specifically sought comments from state, local, and tribal governments concerning the ability of these entities to absorb the costs related to the proposed revisions. The Department received multiple comments on this and other issues from state, local, and tribal governments. Many of these commenters raised concerns about the Department's proposal to increase the salary level. Several commenters writing on behalf of state or local governments asserted that public employers would respond to the proposed salary level increase by cutting vital services or increasing taxes. See, e.g., Charlotte County, Florida; Pennsylvania State Association of Township Supervisors; Rockingham County, Virginia. Several commenters writing on behalf of tribal governments similarly asserted that tribes would be forced to respond to the proposed salary level increase by reducing services to tribal communities. See, e.g., Ho-Chunk, Inc. (a company wholly owned by the Winnebago Tribe of Nebraska); Native American Finance Officers Association. The Jamestown S'Kallam Tribe stated that "requiring Tribal business to 'transfer income' to employees takes money not only out of tribal governments, but to the economy of the surrounding communities as tribes provide enormous employment opportunities to the non-native communities." Given these concerns, some commenters writing on behalf of state, local, or tribal governments requested that the Department adopt a lower standard salary threshold than we proposed and/or a phase-in period for raising the salary, while other commenters requested a special salary level or an exemption from the salary level or the FLSA's requirements for state, local, and tribal governments. See, e.g., Georgia Department of Administrative Services; Isle of Wight County,

Virginia; Mississippi State Personnel Board; Pennsylvania State Association of Township Supervisors; New Mexico State Personnel Board. In addition to their concerns about the salary level, some commenters, for example the New Mexico State Personnel Board and the Mississippi State Personnel Board, also expressed concern about the Department's proposal to update the salary level annually, and some requested that the Department not make any changes to the duties test.

As discussed in this Final Rule, the Department has modified the proposed rule by setting the salary level equal to the 40th percentile weekly earnings of full-time salaried workers in the lowest-wage Census Region (currently the South). We believe that this adjustment will provide relief for state, local, and tribal government employers, as it does for employers in low-wage areas and industries. Furthermore, the Department has decided to automatically update the salary level every three years rather than annually, and the Final Rule does not make any changes to the duties test. The Department notes that we expect employers to respond in a variety of ways to changes in salary level, and the manner in which an employer responds will affect how the employer (and its employees) is impacted. In response to comments suggesting the implementation of a special salary threshold or an exemption for state, local, or tribal government employers, the Department did not propose any different treatment for employees of state, local, or tribal government employers or ask any questions in the NPRM about such a change; therefore, we believe the special provisions sought are beyond the scope of this rulemaking.

Some state, local, and tribal governments expressed concern with our automatic updating proposal. Several commenters stressed the burdens this change would impose on public sector employers. For example, the California State Association of Counties stated that the "volatility

of the [salary level] changes" resulting from annual automatic updating would "make planning and budgeting very challenging," while the Charlotte County Board of County Commissioners asked the Department to "strongly consider the increased administrative and financial burdens" that annual updating "would place on county governments." See also City of Galax. Similarly, the New Mexico State Personnel Board stated that "in the public sector, an automatic annual increase would become an unbudgeted mandate placed on the Executive and the Legislature, which would require the State to respond both fiscally and administratively," and that this change could negatively impact employee morale and productively, the State's budgeting process, and "may cause budgets to be diverted from other areas such as health, safety, and security, possibly impacting services to citizens." While most tribal government commenters did not specifically address this aspect of the Department's proposal, the Chitimacha Tribe of Louisiana stated that annual automatic updating could negatively impact employee morale, increase burdens on tribal businesses (including its casino hotel), make it harder to estimate year-to-year costs, and "would be tantamount to Chitimacha being required to give its government and business enterprise salaried employees a raise every year or be forced to reclassify the worker as an hourly employee."

Some state and local government commenters specifically addressed the automatic updating alternatives discussed in the Department's proposal. The New Mexico State Personnel Board opposed both updating methods, stating that "the CPI-U measures purchasing power . . . [and not] the supply and demand of labor," and that the fixed percentile approach would "result in an accelerated upward movement of the [salary] threshold, as previously salaried workers are reclassified to hourly, or as they have their incomes increased to be over the new" threshold.

Other commenters appeared more receptive to automatic updating, provided the Department make certain changes from our proposal. The Georgia Department of Administrative Services and the Mississippi State Personnel Board stated that a wage index (rather than a price index) provided a more appropriate basis for automatic updates, although both commenters favored other changes including updating only every five years and, rather than a nationwide effective date, permitting employers to determine when updated salary levels would apply to their organizations. The Commonwealth of Virginia's Department of Human Resource Management (which supported a lower salary level) favored updating using "a measure such as the Employment Cost Index," while some state, local, and tribal governments that opposed aspects of the Department's rulemaking did not specifically address our automatic updating proposal. See, e.g., City of Seward, Alaska; Elk Valley Rancheria Indian Tribe; Indiana Association of Cities and Towns; National League of Cities.

The Department concludes that the concerns raised by state, local, and tribal governments do not provide a basis for declining to institute automatic updating. We recognize that in some instances public sector employers may face different employment environments than their private sector counterparts. However, the Department believes that any unique burdens that automatic updating may pose for government employers are adequately mitigated by the Department's decision to automatically update the salary level every three years (instead of annually) and to increase from 60 to 150 days the notice before automatically updated salary levels take effect. Additionally, between updates all employers can access BLS data to estimate the likely size of the next updated salary level. These changes should provide government employers sufficient time and predictability to allow adaptation to, and compliance with, new salary levels. We also reiterate, as discussed in sections IV.E.ii.-iii, that nothing in this

rulemaking requires employers to convert newly nonexempt employees to hourly status or reward underperforming employees with a raise. As to what method the Department should use to automatically update the salary level, commenters from State, local, and tribal governments generally raised the same points as non-government commenters. For the reasons already discussed at length, we conclude that automatic updating using the fixed percentile method will best ensure that the salary level continues to serve, in tandem with the duties test, as an effective dividing line between potentially exempt and nonexempt workers.

Some of commenters suggested that the Department failed to adequately consult with state, local, and tribal governments in developing the rule. For example, the State of Maine Department of Labor asserted that "USDOL did not reach out to all states to discuss the impacts this proposed rule change would have on the states." The Elk Valley Rancheria Indian Tribe asserted that "there has been no tribal consultation on this rule-making," and the Ute Mountain Ute Tribe stated that "the proposed rule will have a substantial and direct effect on the Tribe and is subject to consultation under Executive Order 13175." See also. e.g., Gila River Indian Community; Confederated Tribes of the Umatilla Indian Reservation; Poarch Band of Creek Indians. Finally, some commenters, such as the Isle of Wight County, Virginia, urged the Department "to delay implementation" of the rule "until further analysis is done on the increased financial and administrative burdens it would place on county governments." The Department disagrees that there has been little or no tribal consultation or consultation with state and local governments on this rulemaking. As discussed above, the Department conducted an extensive outreach program, including several listening sessions that were specific to state, local, and tribal governments. Representatives from multiple states, local governments, and tribal governments participated in these listening sessions. In addition, the Department engaged associations

representing governmental organizations such as: Interstate Labor Standards Association, National Association of Counties, National Association of Latino Elected and Appointed Officials, National Association of State Workforce Agencies, National Black Caucus of State Legislators, National Conference of State Legislatures, National Congress of American Indians, National Governors Association, National League of Cities, Progressive States Network, and the U.S. Conference of Mayors.

D. Least Burdensome Option or Explanation Required

The Department's consideration of various options has been described throughout the preamble and economic impact analysis (section VI). The Department believes that it has chosen the least burdensome but still cost-effective mechanism to update the salary level and index future levels that is also consistent with the Department's statutory obligation. Although some alternative options considered, such as inflating the 2004 standard salary level to FY2015 dollars resulting in a salary level of $570 per week, would have set the standard salary level at a rate lower than the updated salary level, which might impose lower direct payroll costs on employers, that outcome would not necessarily be the most cost-effective or least burdensome alternative for employers. A lower salary level—or a degraded stagnant level over time—would result in a less effective bright-line test for separating workers who may be exempt from those nonexempt workers intended to be within the Act's protection. A low salary level will also increase the role of the duties test in determining whether an employee is exempt, which would 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 impacts 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 has determined that setting the standard salary level at the 40th percentile of earnings of full-time salaried workers in the lowest-wage Census Region (currently the South) and automatically updating this level every three years best balances the risks and costs of misclassification of exempt status.

IX. Executive Order 13132 (Federalism)

The Department has reviewed this Final Rule in accordance with Executive Order 13132 regarding federalism, and determined that it does not have federalism implications. The Final Rule will not have substantial direct effects on the States, on the relationship between the national government and the States, or on the distribution of power and responsibilities among the various levels of government.

X. Executive Order 13175, Indian Tribal Governments

The Department has reviewed this Final Rule under the terms of Executive Order 13175 and determined that it does not have "tribal implications." The Final Rule does 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." As a result, no tribal summary impact statement has been

prepared.

XI. Effects on Families

The undersigned hereby certifies that this Final Rule will not adversely affect the well-being of families, as discussed under section 654 of the Treasury and General Government Appropriations Act, 1999.

XII. Executive Order 13045, Protection of Children

Executive Order 13045 applies to any rule that (1) is determined to be "economically significant" as defined in Executive Order 12866, and (2) concerns an environmental health or safety risk that the promulgating agency has reason to believe may have a disproportionate effect on children. This Final Rule is not subject to Executive Order 13045 because it has no environmental health or safety risks that may disproportionately affect children.

XIII. Environmental Impact Assessment

A review of this Final Rule in accordance with the requirements of the National Environmental Policy Act of 1969 (NEPA), 42 U.S.C. 4321 et seq.; the regulations of the Council on Environmental Quality, 40 CFR 1500 et seq.; and the Departmental NEPA procedures, 29 CFR part 11, indicates that the Final Rule will not have a significant impact on the quality of the human environment. As a result, there is no corresponding environmental assessment or an environmental impact statement.

XIV. Executive Order 13211, Energy Supply

This Final Rule is not subject to Executive Order 13211. It will not have a significant adverse effect on the supply, distribution, or use of energy.

XV. Executive Order 12630, Constitutionally Protected Property Rights

This Final Rule is not subject to Executive Order 12630, because it does not involve

implementation of a policy "that has takings implications" or that could impose limitations on private property use.

XVI. Executive Order 12988, Civil Justice Reform Analysis

This Final Rule was drafted and reviewed in accordance with Executive Order 12988 and will not unduly burden the federal court system. The Final Rule was: (1) reviewed to eliminate drafting errors and ambiguities; (2) written to minimize litigation; and (3) written to provide a clear legal standard for affected conduct and to promote burden reduction.

List of Subjects in 29 CFR part 541

Labor, Minimum wages, Overtime pay, Salaries, Teachers, Wages.

David Weil,

Administrator, Wage and Hour Division

PART 541--DEFINING AND DELIMITING THE EXEMPTIONS FOR EXECUTIVE, ADMINISTRATIVE, PROFESSIONAL, COMPUTER AND OUTSIDE SALES EMPLOYEES

1. The authority citation for part 541 is revised 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 per week of not less than the 40th percentile of weekly earnings of full-time nonhourly workers in the lowest-wage Census Region (or 84 percent of that amount per week, if employed in American Samoa by employers other than the Federal government), exclusive of board, lodging or other facilities. Beginning January 1, 2020, and every three years thereafter, the Secretary shall update the required salary amount pursuant to § 541.607;

* * * * *

3. In § 541.200, revise paragraph (a)(1) to read as follows:

<u>§ 541.200 General rule for administrative employees.</u>

(a) * * *

(1) Compensated on a salary or fee basis pursuant to § 541.600 at a rate per week of not less than the 40th percentile of weekly earnings of full-time nonhourly workers in the lowest-wage Census Region (or 84 percent of that amount per week, if employed in American Samoa by employers other than the Federal government), exclusive of board, lodging or other facilities. Beginning January 1, 2020, and every three years thereafter, the Secretary shall update the required salary amount pursuant to § 541.607;

* * * * *

4. In § 541.204, revise paragraph (a)(1) to read as follows:

<u>§ 541.204 Educational establishments.</u>

(a) * * *

(1) Compensated on a salary or fee basis pursuant to § 541.600 at a rate per week of not less than the 40th percentile of weekly earnings of full-time nonhourly workers in the lowest-

wage Census Region (or 84 percent of that amount 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. Beginning January 1, 2020, and every three years thereafter, the Secretary shall update the required salary amount pursuant to § 541.607; 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 per week of not less than the 40th percentile of weekly earnings of full-time nonhourly workers in the lowest-wage Census Region (or 84 percent of that amount per week, if employed in American Samoa by employers other than the Federal government), exclusive of board, lodging or other facilities. Beginning January 1, 2020, and every three years thereafter, the Secretary shall update the required salary amount pursuant to § 541.607; and

* * * * *

6. In § 541.400, remove the first sentence in paragraph (b) introductory text and add three sentences in its place.

The additions 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 pursuant to § 541.600 at a rate per week of not less than the

40th percentile of weekly earnings of full-time nonhourly workers in the lowest-wage Census Region (or 84 percent of that amount per week, if employed in American Samoa by employers other than the Federal government), exclusive of board, lodging or other facilities. Beginning January 1, 2020, and every three years thereafter, the Secretary shall update the required salary amount pursuant to § 541.607. The section 13(a)(17) exemption applies to any computer employee compensated on an hourly basis at a rate of not less than $27.63 an hour. * * *

* * * * *

7. Amend § 541.600 by removing the first sentence of paragraph (a) and adding three sentences in its place and revising paragraph (b).

The revisions and additions read as follows:

<u>§ 541.600 Amount of salary required.</u>

(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 per week of not less than the 40th percentile of weekly earnings of full-time nonhourly workers in the lowest-wage Census Region. As of December 1, 2016, and until a new rate is published in the Federal Register by the Secretary, such an employee must be compensated on a salary basis at a rate per week of not less than $913 (or $767 per week, if employed in American Samoa by employers other than the Federal government), exclusive of board, lodging or other facilities. Beginning January 1, 2020, and every three years thereafter, the Secretary shall update the required salary amount pursuant to § 541.607. * * *

(b) The required amount of compensation per week may be translated into equivalent amounts for periods longer than one week. The requirement will be met if the employee is compensated biweekly on a salary basis of $1,826, semimonthly on a salary basis of $1,978, or

monthly on a salary basis of $3,956. However, the shortest period of payment that will meet this compensation requirement is one week. Beginning January 1, 2020, and every three years thereafter, the Secretary shall update the required salary amount pursuant to § 541.607 and the updated salary amount may be paid weekly, biweekly, semimonthly, or monthly on a salaried basis.

* * * * *

8. Amend § 541.601 by:

a. Revising paragraph (a);

b. Adding introductory text to paragraph (b);

c. Revising the first sentence of paragraph (b)(1); and

d. Revising paragraph (b)(2).

The revisions and additions read as follows:

<u>§ 541.601 Highly compensated employees.</u>

(a) An employee shall be exempt under section 13(a)(1) of the Act if:

(1) The employee receives total annual compensation of at least the annualized earnings amount of the 90th percentile of full-time nonhourly workers nationally; and

(2) The employee customarily and regularly performs any one or more of the exempt duties or responsibilities of an executive, administrative or professional employee identified in subpart B, C, or D of this part.

(b) As of December 1, 2016, and until a new amount is published in the Federal Register by the Secretary and becomes effective, such an employee must receive total annual compensation of at least $134,004. Beginning January 1, 2020, and every three years thereafter, the Secretary shall update the required total annual compensation amount pursuant to § 541.607.

(1) "Total annual compensation" must include at least a weekly amount equal to the required salary amount required by § 541.600(a) 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. * * *

(2) If an employee's total annual compensation does not total at least the minimum amount established in paragraph (a) of this section 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, if the current annual salary level for a highly compensated employee is $134,004, an employee may earn $100,000 in base salary, and the employer may anticipate based upon past sales that the employee also will earn $35,000 in commissions. However, due to poor sales in the final quarter of the year, the employee actually only earns $10,000 in commissions. In this situation, the employer may within one month after the end of the year make a payment of at least $24,004 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) to read as follows:

(a) General rule. An employee will be considered to be paid on a "salary basis" within the meaning of this part if the employee regularly receives each pay period on a weekly, or less frequent basis, a predetermined amount constituting all or part of the employee's compensation,

which amount is not subject to reduction because of variations in the quality or quantity of the work performed.

(1) Subject to the exceptions provided in paragraph (b) of this section, an exempt employee must receive the full salary for any week in which the employee performs any work without regard to the number of days or hours worked. Exempt employees need not be paid for any workweek in which they perform no work.

(2) An employee is not paid on a salary basis if deductions from the employee's predetermined compensation are made for absences occasioned by the employer or by the operating requirements of the business. If the employee is ready, willing and able to work, deductions may not be made for time when work is not available.

(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 quarterly or more frequently. If by the last pay period of the quarter the sum of the employee's weekly salary plus nondiscretionary bonus, incentive, and commission payments received does not equal 13 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 quarter. Any such final payment made after the end of the 13-week period may count only toward the prior quarter's salary amount and not toward the salary amount in the quarter it was paid. This provision does not apply to highly compensated employees under § 541.601.

* * * * *

10. Revise § 541.604 to read as follows:

<u>§ 541.604 Minimum guarantee plus extras.</u>

(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, if the current weekly salary level is $913, an exempt employee guaranteed at least $913 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 $913 each week paid on a salary basis. Similarly, the exemption is not lost if an exempt employee who is guaranteed at least $913 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, if the weekly salary level is $913, an exempt employee guaranteed compensation of at least $1,000 for any week in which the employee performs any work, and who normally works four or five shifts each week, may be paid $300 per shift without violating the 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, if the salary level were $913, an artist paid $500 for a picture that took 20 hours to complete meets the minimum salary requirement for exemption since earnings at this rate would yield the artist $1000 if 40 hours were worked.

12. Add § 541.607 to read as follows:

§ 541.607 Automatic updates to amounts of salary and compensation required.

(a) Standard salary level. The amount required to be paid to an exempt employee on a salary or fee basis, as applicable, pursuant to §§ 541.100(a)(1), 541.200(a)(1), 541.204(a)(1), 541.300(a)(1), 541.400(b), 541.600(a)-(b), 541.601(b)(1), 541.604(a), and 541.605(b), is:

(1) $913 per week as of December 1, 2016; and

(2) Beginning on January 1, 2020, and every three years thereafter, updated to equal the 40th percentile of weekly earnings of full-time nonhourly workers in the lowest-wage Census

Region in the second quarter of the year preceding the update as published by the Bureau of Labor Statistics.

(b) American Samoa. The amount required to be paid to an exempt employee employed in American Samoa, on a salary or fee basis, pursuant to §§ 541.100(a)(1), 541.200(a)(1), 541.204(a)(1), 541.300(a)(1), 541.400(b), and 541.600(a), is:

(1) $767 per week as of December 1, 2016; and

(2) Beginning on January 1, 2020, and every three years thereafter:

(i) Updated to correspond to 84 percent of the updated salary set in paragraph (a)(2) of this section; and

(ii) Rounded to the nearest multiple of $1.00;

(3) Provided that when the highest industry minimum wage for American Samoa equals the minimum wage under 29 U.S.C. 206(a)(1), exempt employees employed in all industries in American Samoa shall be paid the rate specified in paragraph (a) of this section.

(c) Motion picture producing industry. The amount required to be paid to an exempt motion picture producing employee pursuant to § 541.709 is:

(1) $1,397 per week as of December 1, 2016; and

(2) Beginning on January 1, 2020, and every three years thereafter:

(i) Updated from the previously applicable base rate, adjusted by the same percentage as the updated salary set in paragraph (a)(2) of this section; and

(ii) Rounded to the nearest multiple of $1.00.

(d) The amount required in total annual compensation for an exempt highly compensated employee pursuant to § 541.601, is:

(1) $134,004 per year as of December 1, 2016; and

(2) Beginning on January 1, 2020, and every three years thereafter, updated to correspond to the annualized earnings amount of the 90th percentile of full-time nonhourly workers nationally in the second quarter of the year preceding the update as published by the Bureau of Labor Statistics.

(e) The Secretary will determine the lowest-wage Census Region for paragraphs (a) and (b) of this section using the 40th percentile of weekly earnings of full-time nonhourly workers in the Census Regions based on data from the Current Population Survey as published by the Bureau of Labor Statistics.

(f) The Secretary will use the 90th percentile of weekly earnings data of full-time nonhourly workers nationally based on data from the Current Population Survey as published by the Bureau of Labor Statistics for paragraph (d) of this section.

(g) Not less than 150 days before the January 1st effective date of the updated earnings requirements for this section, the Secretary will publish a notice in the Federal Register stating the updated amounts for paragraphs (a) through (d) of this section.

(h) The Wage and Hour Division will publish and maintain on its website the applicable earnings requirements for employees paid pursuant to this part.

13. Revise § 541.709 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, as of December 1, 2016, at a base rate of at least $1,397 per week (exclusive of board, lodging, or other facilities); and beginning on January 1, 2020, and every three years thereafter, is compensated at a base rate of at least the previously applicable base rate adjusted by the same ratio as the preceding standard salary level

is increased (exclusive of board, lodging, or other facilities). Thus, an employee in this industry who is otherwise exempt under subparts B, C, or D of this part, and who is employed at a base rate of at least the applicable current minimum amount a week is exempt if paid a proportionate amount (based on a week of not more than 6 days) for any week in which the employee does not work a full workweek for any reason. Moreover, an otherwise exempt employee in this industry qualifies for exemption if the employee is employed at a daily rate under the following circumstances:

(a) The employee is in a job category for which a weekly base rate is not provided and the daily base rate would yield at least the minimum weekly amount if 6 days were worked; or

(b) The employee is in a job category having the minimum weekly base rate and the daily base rate is at least one-sixth of such weekly base rate.

BILLING CODE 4510-27-P

[FR Doc. 2016-11754 Filed: 5/18/2016 8:45 am; Publication Date: 5/23/2016]