Insight

The Regulatory Burdens of Implementing DOL's Overtime Pay Rule

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EXECUTIVE SUMMARY

The Department of Labor (DOL) proposed a rule that would expand the number of workers entitled to overtime pay. While most discussion of the rule has been focused on its labor market implications, there has been very little attention on the regulatory burden imposed from implementing the rule. Some have criticized the DOL for substantially understating this burden on employers. In this paper, American Action Forum (AAF) specifically examines the rule's implementation costs and what they could mean for workers. We find that the implementation costs of the overtime pay rule could be equivalent to:

· 11,083 to 690,945 full-time workers;

· $5.11 to $318.81 per every worker nationwide;

· And $126.59 to $7,891.93 per every worker who would become eligible for overtime pay because of the rule.

Given the wide range of implementation cost estimates, it is imperative that the regulatory burden of the DOL's overtime pay rule is examined.

INTRODUCTION

Earlier this year, the DOL unveiled a proposed rule to expand the number of workers eligible for overtime pay. In that rule, DOL plans to raise the threshold for exempting salaried workers from overtime pay from the current $455 per week to $970 per week, which DOL projects will be the 40th percentile of the distribution of weekly earnings for full-time salaried workers when the rule is implemented in 2016. This means that the salaried workers who are entitled to receive time-and-a-half pay for working over 40 hours per week will expand from those earning below $23,660 per year to those earning below $50,440 per year. After the DOL implements the rule, the salary level will then change each year so that it remains at the 40th percentile of full-time salaried workers.

Previous AAF research has taken a close look at how the DOL can expand overtime pay, the limitations of the proposed rule change, and its labor market consequences (see here, here, here, and here). But often overlooked is the significance of the regulatory burden imposed when implementing the rule. This burden includes the time it takes to learn about the rule, new paperwork hours, and new administrative compliance responsibilities. While the DOL provided estimates of the implementation costs, those figures have come under scrutiny by trade associations that argue they are far too small. In this brief paper, we use a range of cost estimates to demonstrate the magnitude of the overtime rule’s regulatory burden and what it could mean for employment and wages.

HOW THE DOL CAN CHANGE FEDERAL OVERTIME PAY REQUIREMENTS

Under the Fair Labor Standards Act (FLSA), all employees are required to earn time-and-a-half pay for working overtime, except certain categories of workers who are salaried and well compensated. Most workers who are exempt from overtime pay are categorized as either executive, administrative, or professional (EAP) workers. This is commonly referred to as the “white collar” exemption because it traditionally applies to highly paid skilled professionals and office managers. The DOL, meanwhile, has the authority to “define and delimit” the requirements for exempting a worker from overtime pay. Currently under DOL regulations, there are three primary requirements to exempt a worker from overtime pay: the worker must be salaried (the salary basis test), the salary must meet a minimum level (the salary level test), and the worker’s duties must align with the definition of EAP workers (the duties test).

Earlier this year the DOL proposed a new rule that would update the “white collar” exemption so fewer workers can be classified as exempt and more would be eligible to earn overtime pay for working over 40 hours per week. The DOL plans to expand overtime pay primarily by raising the salary level test from $455 per week to $970 per week, effective next year. The DOL specifically picked $970 per week so that the exemption threshold would match the projected 40th percentile of the distribution of weekly earnings of all full-time salaried workers in 2016. The DOL also proposed that going forward, as pay grows each year, the salary level test would rise with it so that it remains at the 40th percentile. Meanwhile, the DOL did not propose any changes to the duties test.

The DOL projected that as a result of the rule, about 5 million workers would no longer be exempt and would be eligible for overtime pay. According to the DOL, of those workers, only about 1 million actually work over 40 hours per week and would actually benefit from an increase in earnings.

IMPLEMENTATION COSTS

Many have raised serious concerns about the impact of the proposed rule on worker hourly earnings, hours worked, and employment. The DOL itself in the proposed rule acknowledged that hourly pay rates and weekly hours would likely fall among affected salaried workers. Often overlooked, however, are the costs from implementing the rule and the potential consequences for employment and pay. These burdens would include the costs to businesses to familiarize themselves with the rule, the cost of determining employee exemption status and adjusting firm overtime policies, and the cost of additional monitoring and supervision of employee schedules.

The DOL estimated that these factors combined would cost $592.7 million in the first year the rule is implemented. Starting in the second year, however, the DOL assumed that employers would become more knowledgeable of the rule and that familiarization costs would fall to $0. The DOL indicated that in the second year the rule would cost $188.8 million and in the tenth year it would cost $225.3 million. The DOL's estimates increase between the second year and tenth year because as the salary threshold increases each year, more workers would become eligible for overtime pay, causing adjustment and managerial costs to grow. Using this limited information, AAF previously inferred that the DOL estimated the rule would cost $2.46 billion over 10 years.

These figures, however, have been criticized as being far too low. On behalf of the National Retail Federation, the economic advisory firm Oxford Economics estimated the overtime rule's 2016 implementation costs just for retailers. According to Oxford Economics, implementing the rule would cost retailers alone $745 million in 2016, substantially larger than DOL's cost estimate of $592.7 million for the entire economy. Retailers, meanwhile, only employ 13.2 percent of private sector workers.[1] For a rough calculation, if one assumes that the cost of the rule is distributed equally among workers, the Oxford Economics estimate suggests that the overtime rule would cost private sector employers $5.7 billion in 2016. Oxford Economics did not provide projected implementation costs for the years after 2016.

Even more dramatic are the estimates from the Chamber of Commerce, which put implementation costs at $ 36.95 billion in 2016. Moreover, the business trade association argued that since the salary threshold would increase every year, familiarization costs would not substantially fall after the initial year, which the DOL assumed in its cost estimate. The Chamber of Commerce estimated that starting in 2017, the rule would cost the economy $33.52 billion per year and cumulatively over 10 years the cost of the proposed overtime rule would amount to $338.5 billion.

IMPLICATIONS FOR EARNINGS AND EMPLOYMENT

Just like other regulations, the cost of implementing this rule has to come from somewhere. In a number of papers, AAF has shown the cost of excessive regulation results in fewer small businesses, fewer jobs, and lower pay. For instance, in a 2014 paper AAF found that for every $1 billion of regulatory costs imposed on an industry, that industry's employment generally declines 3.6 percent. To put that in perspective, consider that Oxford Economics estimated that implementing the overtime rule would cost the retail industry $745 million. Our research suggests that could result in a loss of roughly 410 thousand of the 15.3 million retail jobs in the country.

Another way to examine the potential labor market impact of the rule's implementation costs is to consider the actual number of workers and average per employee pay that these cost estimates are equivalent too. Let's just take a look at the initial year cost estimates, illustrated in the table below.

Labor Market Implications of Implementing the DOL Overtime Pay Rule				
Source	**Initial Year Cost Estimate** **($ millions)**	**FTE[2]**	**Annual Cost per Worker**	**Annual Cost per Newly Non-Exempt Worker**

Labor Market Implications of Implementing the DOL Overtime Pay Rule				
DOL	$592.7	11,083	$5.11	$126.59
Oxford Economics	$5,660	105,834	$48.83	$1,208.82
Chamber of Commerce	$36,950	690,945	$318.81	$7,891.93

The DOL's $592.7 million estimate translates to 11,083 full-time equivalent (FTE) workers. This means that if all of the costs of implementing the rule were directly passed on by cutting jobs, the number of work hours lost in the economy would be equivalent to losing 11,083 full-time jobs. When examining the higher cost estimates, the FTEs jump. For instance, the implementation cost derived from the Oxford Economics retail estimate translates to 105,834 FTEs. The Chamber of Commerce's cost estimate translates to 690,945 FTEs.

What if all of the costs were directly passed on to workers by lowering their pay? The DOL's estimate appears quite modest as it is only equivalent to $5.11 for every worker in the country in 2016. The larger cost estimates are equivalent to considerably higher pay. The Oxford Economics estimate is equivalent to $48.83 per worker and the Chamber of Commerce's estimate translates to $318.81 per worker.

Moreover, employers could directly pass these costs on to the pay of workers who specifically switch from exempt to non-exempt status because of the rule. According to the DOL, the rule would result in about 5 million newly non-exempt workers who would now be eligible for overtime pay.[3] But, if they face the entire cost of implementing the rule, the reduction in their pay would substantially offset any benefits intended by the rule. This is particularly true for the higher implementation cost estimates. While the DOL's cost estimate is equivalent to $126.59 per newly non-exempt worker, the Oxford Economics and Chamber of Commerce estimates are equivalent to $1,208.82 and $7,891.93, respectively.

CONCLUSION

The DOL proposed overtime pay rule would present a substantial new burden in federal labor requirements. While the White House hopes the new rule will result in substantially higher pay for a large number of workers, the DOL's own analysis demonstrates that the number of workers who would actually benefit from the rule is quite small and the actual income increase would be minimal. Meanwhile the regulatory costs could impose a substantial burden on employers, which AAF has frequently shown reduces employment and pay. Rather than another expensive regulation, perhaps it would be best to increase pay and employment by slowing down the excessive growth in federal regulations.

[1] Based on author's calculation of March data from the Quarterly Census of Employment and Wages, http://www.bls.gov/data/