

## DEPARTMENT OF LABOR

## Wage and Hour Division

## 29 CFR Part 541

RIN 1235-AA39

**Defining and Delimiting the Exemptions for Executive, Administrative, Professional, Outside Sales, and Computer Employees****AGENCY:** Wage and Hour Division, Department of Labor.**ACTION:** Notice of proposed rulemaking.

**SUMMARY:** In this proposal, the Department of Labor (Department) is updating and revising the regulations issued under the Fair Labor Standards Act implementing the exemptions from minimum wage and overtime pay requirements for executive, administrative, professional, outside sales, and computer employees. Significant proposed revisions include increasing the standard salary level to the 35th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (currently the South)—\$1,059 per week (\$55,068 annually for a full-year worker)—and increasing the highly compensated employee total annual compensation threshold to the annualized weekly earnings of the 85th percentile of full-time salaried workers nationally (\$143,988). The Department is also proposing to add to the regulations an automatic updating mechanism that would allow for the timely and efficient updating of all the earnings thresholds.

**DATES:** Interested persons are invited to submit written comments on this notice of proposed rulemaking (NPRM) on or before November 7, 2023.

**ADDRESSES:** You may submit comments, identified by Regulatory Information Number (RIN) 1235-AA39, by either of the following methods:

- **Electronic Comments:** Submit comments through the Federal eRulemaking Portal at <https://www.regulations.gov>. Follow the instructions for submitting comments.
- **Mail:** Address written submissions to: Division of Regulations, Legislation, and Interpretation, Wage and Hour Division, U.S. Department of Labor, Room S-3502, 200 Constitution Avenue NW, Washington, DC 20210.

**Instructions:** Response to this NPRM is voluntary. The Department requests that no business proprietary information, copyrighted information, or personally identifiable information be submitted in response to this NPRM. Commenters submitting file attachments

on <https://www.regulations.gov> are advised that uploading text-recognized documents—i.e., documents in a native file format or documents which have undergone optical character recognition (OCR)—enable staff at the Department to more easily search and retrieve specific content included in your comment for consideration.

Anyone who submits a comment (including duplicate comments) should understand and expect that the comment, including any personal information provided, will become a matter of public record and will be posted without change to <https://www.regulations.gov>. The Department posts comments gathered and submitted by a third-party organization as a group under a single document ID number on <https://www.regulations.gov>. All comments must be received by 11:59 p.m. ET on November 7, 2023, for consideration in this rulemaking; comments received after the comment period closes will not be considered.

The Department strongly recommends that commenters submit their comments electronically via <https://www.regulations.gov> to ensure timely receipt prior to the close of the comment period, as the Department continues to experience delays in the receipt of mail. Please submit only one copy of your comments by only one method.

**Docket:** For access to the docket to read background documents or comments, go to the Federal eRulemaking Portal at <https://www.regulations.gov>.

**FOR FURTHER INFORMATION CONTACT:**

Amy DeBisschop, Director, Division of Regulations, Legislation, and Interpretation, Wage and Hour Division, U.S. Department of Labor, Room S-3502, 200 Constitution Avenue NW, Washington, DC 20210; telephone: (202) 693-0406 (this is not a toll-free number). Alternative formats are available upon request by calling 1-866-487-9243. If you are deaf, hard of hearing, or have a speech disability, please dial 7-1-1 to access telecommunications relay services.

Questions of interpretation or enforcement of the agency's existing 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 <https://www.dol.gov/agencies/whd/contact/local-offices> for a nationwide listing of WHD district and area offices.

**SUPPLEMENTARY INFORMATION:****I. Executive Summary**

The Fair Labor Standards Act (FLSA or Act) requires covered employers to pay employees a minimum wage and, for employees who work more than 40 hours in a week, overtime premium pay of at least 1.5 times the employee's regular rate of pay. Section 13(a)(1) of the FLSA, which was included in the original Act in 1938, exempts from the minimum wage and overtime pay requirements "any employee employed in a bona fide executive, administrative, or professional capacity."<sup>1</sup> The exemption is commonly referred to as the "white-collar" or executive, administrative, or professional (EAP) exemption. The statute delegates to the Secretary of Labor (Secretary) the authority to define and delimit the terms of the exemption. Since 1940, the regulations implementing the EAP exemption have generally required that each of the following three tests must be met: (1) the employee must be paid a predetermined and fixed salary that is not subject to reduction because of variations in the quality or quantity of work performed (the salary basis test); (2) the amount of salary paid must meet a minimum specified amount (the salary level test); and (3) the employee's job duties must primarily involve executive, administrative, or professional duties as defined by the regulations (the duties test). The employer bears the burden of establishing the applicability of the exemption.<sup>2</sup> Job titles and job descriptions do not determine EAP exemption status, nor does merely paying an employee a salary.

Consistent with its broad authority under the statute, the Department is proposing compensation thresholds that will work effectively with the standard duties test and the highly compensated employee duties test to better identify who is employed in a bona fide EAP capacity. Specifically, the Department is proposing to set the standard salary level at the 35th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (\$1,059 per week or \$55,068 annually for a full-year worker)<sup>3</sup> and the highly

<sup>1</sup> 29 U.S.C. 213(a)(1).

<sup>2</sup> See, e.g., *Idaho Sheet Metal Works, Inc. v. Wirtz*, 383 U.S. 190, 209 (1966); *Walling v. Gen. Indus. Co.*, 330 U.S. 545, 547–48 (1947).

<sup>3</sup> In determining earnings percentiles in its part 541 rulemakings since 2004, the Department has consistently looked at nonhourly earnings for full-time workers from the Current Population Survey (CPS) Merged Outgoing Rotation Group (MORG) data collected by the Bureau of Labor Statistics (BLS). As explained in section VII.B.5, the Department considers data representing compensation paid to nonhourly workers to be an appropriate proxy for compensation paid to salaried workers, although for simplicity the Department

compensated employee total annual compensation threshold at the annualized weekly earnings of the 85th percentile of full-time salaried workers nationally (\$143,988). These proposed compensation thresholds are firmly grounded in the authority that the FLSA grants to the Secretary to define and delimit the EAP exemption, a power the Secretary has exercised for over 80 years.

The proposed increase in the standard salary level to the 35th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region better fulfills the Department's obligation under the statute to define and delimit who is employed in a bona fide EAP capacity. Upon reflection, the Department has determined that its rulemakings over the past 20 years, since the Department simplified the test for the EAP exemption in 2004 by replacing the historic two-test system for determining exemption status with the single standard test, have vacillated between two distinct approaches: One used in rules in 2004<sup>4</sup> and 2019,<sup>5</sup> that exempted lower-paid workers who historically had been entitled to overtime because they did not meet the more detailed duties requirements of the test that was in place from 1949 to 2004; and one used in a rule in 2016,<sup>6</sup> that restored overtime protection to lower-paid white-collar workers who performed significant amounts of nonexempt work but also removed from the exemption other lower-paid workers who historically were exempt under the prior test, an approach that received

unfavorable treatment in litigation.<sup>7</sup> Having grappled with these different approaches to setting the standard salary level, this proposal retains the simplified standard test, the benefits of which were recognized in the Department's 2004, 2016 and 2019 rulemakings,<sup>8</sup> while updating the standard salary level to account for earnings growth since the 2019 rule and adjusting the salary level methodology based on the lessons learned in recent rulemakings.

The Department's proposed standard salary level will, in combination with the standard duties test, better define and delimit which employees are employed in a bona fide EAP capacity. By setting a salary level above what the methodology used in 2004 and 2019 would produce using current data, the proposal would ensure that, consistent with the Department's historical approach to the exemption, fewer lower-paid white-collar employees who perform significant amounts of nonexempt work are included in the exemption. At the same time, by setting the salary level below the methodology used in 2016, the proposal would allow employers to continue to use the exemption for many lower-paid white-collar employees who were made exempt under the 2004 standard duties test. The combined effect would be a more effective test for determining who is employed in a bona fide EAP capacity.

The Department is also proposing to increase the salary levels in the U.S. territories, which have not been changed since 2004. Traditionally, the Department has set special salary levels only for territories that were not subject to the Federal minimum wage. In the 2004 rule, the Department ended the use of special salary levels for Puerto Rico and the U.S. Virgin Islands, as they had become subject to the Federal minimum wage since the Department last updated the part 541 salary levels, and set a special salary level only for American Samoa, which remained not subject to the Federal minimum wage.<sup>9</sup> In the 2019 rule, however, the Department elected to preserve the salary level set in 2004 (\$455 per week) for employees in Puerto Rico, Guam, the U.S. Virgin Islands, and the Commonwealth of the Northern Mariana Islands (CNMI) instead of applying the new standard

salary level of \$684 per week that applied to employees in the 50 states and the District of Columbia.<sup>10</sup> In doing so, the Department for the first time set a special salary level for employees in territories that were subject to the Federal minimum wage. In accordance with the Department's traditional practice, and in the interest of applying the FLSA uniformly to areas subject to the Federal minimum wage, the Department is proposing to apply the standard salary level to employees in all territories that are subject to the Federal minimum wage and to maintain a special salary level only for employees in American Samoa, because that territory remains subject to special minimum wage rates. The Department is also proposing to update the special base rate for employees in the motion picture industry.

The Department is also proposing to update the earnings threshold for the highly compensated employee (HCE) exemption, which was added to the regulations in 2004 and applies to certain highly compensated employees and combines a much higher annual compensation requirement with a minimal duties test. The HCE test's primary purpose is to serve as a streamlined alternative for very highly compensated employees because a very high level of compensation is a strong indicator of an employee's exempt status, thus eliminating the need for a detailed duties analysis.<sup>11</sup> In this rulemaking, the Department is proposing to increase the HCE total annual compensation threshold to the annualized weekly earnings amount of the 85th percentile of full-time salaried workers nationally (\$143,988). The proposed HCE threshold is high enough to exclude employees who are not "at the very top of [the] economic ladder"<sup>12</sup> and would guard against the unintended exemption of workers who are not bona fide EAP employees, including those in high-income regions and industries.

In each of its part 541 rulemakings since 2004, the Department recognized the need to regularly update the earnings thresholds to ensure that they remain effective in helping differentiate between exempt and nonexempt employees. As the Department observed in these rulemakings, even a well-calibrated salary level that is not kept up to date becomes obsolete as wages for nonexempt workers increase over

uses the terms salaried and nonhourly interchangeably in this proposal. The Department relied on CPS MORG data for calendar year 2022 to develop this NPRM, including to determine the proposed salary level. In the final rule, the Department will use the most recent data available, which will change the dollar figures. For example, if after consideration of comments received, the final rule were to adopt the proposed salary level of the 35th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census region (currently the South), in the fourth quarter of 2023 the Department projects that the salary threshold could be \$1,140 per week or \$59,285 for a full-year worker. To calculate this, the Department applied the Congressional Budget Office projections of the employment cost index for wages and salaries of workers in private industry growing by 4.5 percent in 2023 to the 35th percentile of weekly earnings of full-time salaried workers in the South from the fourth quarter of 2022, which was \$1,091 per week or \$56,732 for a full-year worker. As an additional example, in the first quarter of 2024, the Department projects that the salary threshold could be \$1,158 per week or \$60,209 for a full-year worker; the Department applied the 4.5 percent growth rate to the 35th percentile of weekly earnings of full-time salaried workers in the South from the first quarter of 2023, which was \$1,108 per week or \$57,616 for a full-year worker.

<sup>4</sup> 69 FR 22121 (April 23, 2004).

<sup>5</sup> 84 FR 51230 (Sept. 27, 2019).

<sup>6</sup> 81 FR 32391 (May 23, 2016).

<sup>7</sup> The Department never enforced the 2016 rule because it was invalidated by the U.S. District Court for the Eastern District of Texas. See *Nevada v. U.S. Department of Labor*, 275 F.Supp.3d 795 (E.D. Tex. 2017).

<sup>8</sup> See 84 FR 51243–45; 81 FR 32414, 32444–45; 69 FR 22126–28.

<sup>9</sup> 69 FR 22172.

<sup>10</sup> 84 FR 51246.

<sup>11</sup> See 69 FR 22173–74.

<sup>12</sup> *Id.* at 22174.

time.<sup>13</sup> Long intervals between rulemakings have resulted in eroded earnings thresholds based on outdated earnings data that were ill-equipped to help identify bona fide EAP employees.

To address this problem, in the 2004 and 2019 rules the Department expressed its commitment to regularly updating the salary levels.<sup>14</sup> In the 2016 rule, it included a regulatory provision to automatically update the salary levels.<sup>15</sup> Based on its long experience with updating the salary levels, the Department has determined that adopting a regulatory provision for automatically updating the salary levels, with an exception for pausing future updates under certain conditions, is the most viable and efficient way to ensure the EAP exemption earnings thresholds keep pace with changes in employee pay and thus remain effective in helping determine exemption status. The proposed automatic updating mechanism would allow for the timely, predictable, and efficient updating of the earnings thresholds.

The Department estimates that in Year 1, 3.4 million currently exempt employees who earn at least the current salary level of \$684 per week but less than the proposed standard salary level of \$1,059 per week would, absent the employer paying them at or above the new salary level, gain overtime protection. For more than half of these employees, this proposal would restore overtime protections that the employees would have been entitled to under every rule prior to the 2019 rule. The Department also estimates that 248,900 employees who are currently exempt under the HCE test would be affected by the proposed increase in the HCE total annual compensation level. Absent the employer paying these employees at or above the new HCE level, the exemption status of these employees would turn on the standard duties test (which these employees do not meet) rather than the minimal duties test that applies to employees earning at or above the HCE threshold. The economic analysis of the proposed rule quantifies the direct costs resulting from the rule: (1) regulatory familiarization costs; (2) adjustment costs; and (3) managerial costs. The Department estimates that total annualized direct employer costs over the first 10 years would be \$664 million with a 7 percent discount rate. This rulemaking will also give employees higher earnings in the form of transfers of income from employers to employees.

The Department estimates annualized transfers would be \$1.3 billion, with a 7 percent discount rate.

## II. Background

### A. The FLSA

The FLSA generally requires covered employers to pay 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 regular rate of pay for all hours worked over 40 in a workweek.<sup>16</sup> However, section 13(a)(1) of the FLSA, codified at 29 U.S.C. 213(a)(1), provides an exemption from both minimum wage and overtime pay for “any employee employed in a bona fide executive, administrative, or professional capacity . . . or in the capacity of [an] outside salesman (as such terms are defined and delimited from time to time by regulations of the Secretary [of Labor], subject to the provisions of [the Administrative Procedures Act] . . .).” The FLSA does not define the terms “executive,” “administrative,” “professional,” or “outside salesman,” but rather delegates that task to the Secretary. Pursuant to Congress’s grant of rulemaking authority, since 1938 the Department has issued regulations at 29 CFR part 541 to define and delimit the scope of the section 13(a)(1) exemption.<sup>17</sup> Because Congress explicitly delegated to the Secretary the authority to define and delimit the specific terms of the exemption, the regulations so issued have the binding effect of law.<sup>18</sup>

The exemption for executive, administrative, or professional employees (EAP exemption) was included in the original FLSA legislation passed in 1938.<sup>19</sup> It was modeled after similar provisions contained in the earlier National Industrial Recovery Act of 1933 (NIRA) and state law precedents.<sup>20</sup> As the Department has explained in prior rules, the EAP exemption is premised on two policy considerations. First, the type of work exempt employees perform is difficult to standardize to any time frame and cannot 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.<sup>21</sup> Second, exempted workers typically earn salaries well above the minimum wage and are presumed to enjoy other privileges to compensate them for their long hours of work. These include, for example, above-average fringe benefits and better opportunities for advancement, setting them apart from nonexempt workers entitled to overtime pay.<sup>22</sup>

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. 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.<sup>23</sup>

### B. Regulatory History

The Department’s part 541 regulations have consistently looked to the duties performed by the employee and the salary paid by the employer in determining whether an individual is employed in a bona fide executive, administrative, or professional capacity. Since 1940, the Department’s implementing regulations 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).

#### 1. The Part 541 Regulations From 1938 to 2004

The Department issued the first version of the part 541 regulations in October 1938.<sup>24</sup> The Department’s initial regulations included a \$30 per

<sup>16</sup> See 29 U.S.C. 206(a), 207(a).

<sup>17</sup> See *Helix Energy Solutions, Group Inc. v. Hewitt*, 143 S.Ct. 677, 682 (2023) (“Under [section 13(a)(1)], the Secretary sets out a standard for determining when an employee is a bona fide executive.”).

<sup>18</sup> See *Betterton v. Francis*, 432 U.S. 416, 425 n.9 (1977).

<sup>19</sup> See Fair Labor Standards Act of 1938, Public Law 75–718, 13(a)(1), 52 Stat. 1060, 1067 (June 25, 1938).

<sup>20</sup> See National Industrial Recovery Act, Public Law 73–67, ch. 90, title II, 206(2), 48 Stat 195, 204–5 (June 16, 1933).

<sup>21</sup> See Report of the Minimum Wage Study Commission, Volume IV, pp. 236 and 240 (June 1981).

<sup>22</sup> See *id.*

<sup>23</sup> See 29 U.S.C. 218(a).

<sup>24</sup> 3 FR 2518 (Oct. 20, 1938).

<sup>13</sup> 84 FR 51250–51; 81 FR 32430; see also 69 FR 22212, 22164.

<sup>14</sup> 69 FR 22171; 84 FR 51251–52.

<sup>15</sup> 81 FR 32430.

week compensation requirement for executive and administrative employees, as well as a duties test that prohibited employers from using the exemption for executive, administrative, and professional employees who performed “[a] substantial amount of work of the same nature as that performed by nonexempt employees of the employer.”<sup>25</sup>

The Department issued the first update to its part 541 regulations in October 1940,<sup>26</sup> following extensive public hearings.<sup>27</sup> Among other changes, the 1940 update added the salary basis requirement to the tests for executive, administrative, and professional employees; newly applied the salary level requirement to professional employees; and introduced a 20 percent cap on nonexempt work for executive and professional employees, replacing language which prohibited the performance of a “substantial amount” of nonexempt work.<sup>28</sup>

The Department conducted further hearings on the part 541 regulations in 1947,<sup>29</sup> and issued revised regulations in December 1949.<sup>30</sup> The 1949 rulemaking updated the salary levels set in 1940 and introduced a second, less stringent duties test for higher paid executive, administrative, and professional employees.<sup>31</sup> Thus, beginning in 1949, the part 541 regulations contained two tests for the EAP exemption. These tests became known as the “long” test and the “short” test. The long test paired a lower earnings threshold with a more rigorous duties test that generally limited the performance of nonexempt work to no more than 20 percent of an employee’s hours worked in a workweek. The short test paired a higher salary level and a less rigorous duties test, with no specified limit on the performance of nonexempt work. From 1958 until 2004, the regulations in place generally set the long test salary level to exclude from exemption approximately the lowest-paid 10 percent of salaried white-collar employees who performed EAP duties

in lower wage areas and industries and set the short test salary level significantly higher. The salary and duties components of each test complemented each other, and the two tests worked in combination to determine whether an individual was employed in a bona fide EAP capacity. Lower-paid employees who met the long test salary level but did not meet the higher short test salary level were subject to the long duties test which ensured that employees were, in fact, employed in a bona fide EAP capacity by limiting the amount of time they could spend on nonexempt work. Employees who met the higher short test salary level were considered to be more likely to meet the requirements of the long duties test and thus were subject to a short-cut duties test for determining exemption status.

Additional changes to the regulations, including salary level updates, were made in 1954,<sup>32</sup> 1958,<sup>33</sup> 1961,<sup>34</sup> 1963,<sup>35</sup> 1967,<sup>36</sup> 1970,<sup>37</sup> 1973,<sup>38</sup> and 1975.<sup>39</sup> The Department revised the part 541 regulations twice in 1992 but did not update the salary threshold at that time.<sup>40</sup> None of these updates changed the basic structure of the long and short tests.

The Department described the salary levels adopted in the 1975 rule as “interim rates,” intended to “be in effect for an interim period pending the completion of a study [of worker earnings] by the Bureau of Labor Statistics . . . in 1975.”<sup>41</sup> However, those salary levels remained in effect until 2004. The utility of the salary levels in helping to define the EAP exemption decreased as wages rose during this period. In 1991, the Federal minimum wage rose to \$4.25 per hour,<sup>42</sup> which for a 40-hour week exceeded the lower long test salary level of \$155 per week for executive and administrative employees and equaled the long test salary level of \$170 per week for professional employees. In 1997, the

Federal minimum wage rose to \$5.15 per hour,<sup>43</sup> which for a 40-hour week not only exceeded the long test salary levels, but also was close to the higher short test salary level of \$250 per week.

## 2. Part 541 Regulations From 2004 to 2019

The Department issued a final rule in April 2004 (the 2004 rule)<sup>44</sup> that updated the part 541 salary levels for the first time since 1975 and made several significant changes to the regulations. Most significantly, the Department eliminated the separate long and short tests and replaced them with a single standard test. The Department set the standard salary level at \$455 per week, which was equivalent to the 20th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (the South) and in the retail industry nationally. The Department paired the new standard salary level test with a new standard duties test for executive, administrative, and professional employees, respectively, which was substantially equivalent to the short duties test used in the two-test system.<sup>45</sup>

In the 2004 rule, the Department acknowledged that the switch from a two-test system to a one-test system was a significant change in the regulatory structure,<sup>46</sup> and noted that the shift to setting the salary level based on “the lowest 20 percent of salaried employees in the South, rather than the lowest 10 percent” of EAP employees was made, in part, “because of the proposed change from the ‘short’ and ‘long’ test structure.”<sup>47</sup> The Department asserted that elimination of the long duties test was warranted because “the relatively small number of employees currently earning from \$155 to \$250 per week, and thus tested for exemption under the ‘long’ duties test, will gain stronger protections under the increased minimum salary level which . . . guarantees overtime protection for all employees earning less than \$455 per week.”<sup>48</sup> The Department acknowledged, however, that the new standard salary level was comparable to the long test salary level used in the two-test system (*i.e.*, if the Department’s long test salary level methodology had been applied to contemporaneous

<sup>25</sup> *Id.*

<sup>26</sup> 5 FR 4077 (Oct. 15, 1940).

<sup>27</sup> See “Executive, Administrative, Professional . . . Outside Salesman” Redefined, Wage and Hour Division, U.S. Department of Labor, Report and Recommendations of the Presiding Officer [Harold Stein] at Hearings Preliminary to Redefinition (Oct. 10, 1940) (Stein Report).

<sup>28</sup> 5 FR 4077.

<sup>29</sup> See Report and Recommendations on Proposed Revisions of Regulations, Part 541, by Harry Weiss, Presiding Officer, Wage and Hour and Public Contracts Divisions, U.S. Department of Labor (June 30, 1949) (Weiss Report).

<sup>30</sup> See 14 FR 7705 (Dec. 24, 1949).

<sup>31</sup> *Id.* at 7706.

<sup>32</sup> 19 FR 4405 (July 17, 1954).

<sup>33</sup> 23 FR 8962 (Nov. 18, 1958).

<sup>34</sup> 26 FR 8635 (Sept. 15, 1961).

<sup>35</sup> 28 FR 9505 (Aug. 30, 1963).

<sup>36</sup> 32 FR 7823 (May 30, 1967).

<sup>37</sup> 35 FR 883 (Jan. 22, 1970).

<sup>38</sup> 38 FR 11390 (May 7, 1973).

<sup>39</sup> 40 FR 7091 (Feb. 19, 1975).

<sup>40</sup> The Department first created a limited exception from the salary basis test for public employees. 57 FR 37677 (Aug. 19, 1992). The Department also implemented a 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 Public Law 101–583, sec. 2, 104 Stat. 2871 (Nov. 15, 1990).

<sup>41</sup> 40 FR 7091.

<sup>42</sup> See Public Law 101–157, sec. 2, 103 Stat. 938 (Nov. 17, 1989).

<sup>43</sup> See Public Law 104–188, sec. 2104(b), 110 Stat. 1755 (Aug. 20, 1996).

<sup>44</sup> 69 FR 22122.

<sup>45</sup> See *id.* at 22192–93 (acknowledging “de minimis differences in the standard duties tests compared to the short duties tests”).

<sup>46</sup> See *id.* at 22126–28.

<sup>47</sup> *Id.* at 22167.

<sup>48</sup> *Id.* at 22126.

data).<sup>49</sup> Thus, employees who would have been subject to the more rigorous long duties test if the two-test system had been updated were subject to the equivalent of the short duties test under the new standard test. For example, under the 2004 rule's standard test, an employee who earned just over the rule's standard salary threshold of \$455 in weekly salary, and who met the standard duties test, was exempt even if they would not have met the previous long duties test because they spent substantial amounts of time performing nonexempt work. If the Department had instead retained the two-test system and updated the long test salary level to \$455, that same employee would have been nonexempt because they would have been subject to the more rigorous duties analysis due to their lower salary.

In the 2004 rule, the Department also created a new test for exemption for certain highly compensated employees.<sup>50</sup> The HCE test paired a minimal duties requirement—customarily and regularly performing at least one of the exempt duties or responsibilities of an EAP employee—with a high total annual compensation requirement of \$100,000, a threshold that exceeded the annual earnings of approximately 93.7 percent of salaried workers nationwide.<sup>51</sup> The Department also ended the use of special salary levels for Puerto Rico and the U.S. Virgin Islands, as they had become subject to the Federal minimum wage since the Department last updated the part 541 salary levels in 1975, and set a special salary level only for American Samoa, which remained not subject to the Federal minimum wage.<sup>52</sup> The Department expressed its intent “in the future to update the salary levels on a more regular basis, as it did prior to 1975.”<sup>53</sup>

In May 2016, the Department issued a final rule (the 2016 rule) that retained the single test system and the standard duties test but increased the standard

salary level and provided for regular updating. The 2016 rule (1) increased the standard salary level from the 2004 salary level of \$455 to \$913 per week, the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (the South);<sup>54</sup> (2) increased the HCE test total annual compensation amount from \$100,000 to \$134,004 per year;<sup>55</sup> (3) increased the special salary level for EAP workers in American Samoa;<sup>56</sup> (4) allowed employers, for the first time, to credit nondiscretionary bonuses, incentive payments, and commissions paid at least quarterly towards up to 10 percent of the standard salary level;<sup>57</sup> and (5) added a mechanism to automatically update the part 541 earnings thresholds every 3 years.<sup>58</sup> The standard salary level was set at the low end of the historical range of short test salary levels used in the pre-2004 two-test system.<sup>59</sup> The 2016 rule did not change any of the standard duties test criteria.<sup>60</sup> The 2016 rule was scheduled to take effect on December 1, 2016.

On November 22, 2016, the U.S. District Court for the Eastern District of Texas issued an order preliminarily enjoining the Department from implementing and enforcing the 2016 rule.<sup>61</sup> On August 31, 2017, the district court granted summary judgment to the plaintiff challengers, holding that the 2016 rule's salary level exceeded the Department's authority and invalidating the rule.<sup>62</sup> On October 30, 2017, the Department of Justice appealed to the U.S. Court of Appeals for the Fifth Circuit, which subsequently granted the Department's motion to hold that appeal in abeyance while the Department of Labor undertook further rulemaking. Following an NPRM published on March 22, 2019,<sup>63</sup> the Department published a final rule on September 27, 2019 (the 2019 rule),<sup>64</sup> which formally rescinded and replaced the 2016 rule.

The 2019 rule (1) raised the standard salary level from the 2004 salary level of \$455 to \$684 per week, the 20th percentile of weekly earnings of full-time salaried workers in the lowest-

wage Census Region (the South) and in the retail industry nationally; (2) increased the HCE total annual compensation threshold from \$100,000 to \$107,432; (3) allowed employers to credit nondiscretionary bonuses and incentive payments (including commissions) paid at least annually to satisfy up to 10 percent of the standard salary level; and (4) established special salary levels for all U.S. territories.<sup>65</sup> The 2019 rule did not make changes to the standard duties test.<sup>66</sup> While utilizing the same methodology used in the 2004 rule to set the salary threshold, the Department did not assert that this methodology constituted the outer limit for defining and delimiting the salary threshold. Rather, the Department reasoned the 2004 methodology was well-established, reasonable, would minimize uncertainty and potential legal challenge, and would address the concerns of the district court that the 2016 rule over-emphasized the salary level.<sup>67</sup> The Department acknowledged that the new salary level was below the long test salary level used in the pre-2004 two-test system.<sup>68</sup> As in its 2004 rule, the Department “reaffirm[ed] its intent to update the standard salary level and HCE total annual compensation threshold more regularly in the future using notice-and-comment rulemaking.”<sup>69</sup> The Department noted that large gaps between rulemakings did not serve employer or employee interests and diminished the usefulness of the salary level test, and that regular increases promoted predictable and incremental change.<sup>70</sup> The 2019 rule took effect on January 1, 2020.<sup>71</sup>

### C. Overview of Existing Regulatory Requirements

The part 541 regulations contain specific criteria that define each category of exemption provided for in section 13(a)(1) for bona fide executive, administrative, professional, and outside sales employees, as well as teachers and academic administrative personnel. The regulations also define exempt computer employees under

<sup>49</sup> *Id.* at 22169. The Department last set the long and short test salary levels in 1975. Throughout this proposal, when the Department refers to the relationship of salary levels set in 2004, 2016, and 2019 to equivalent long or short test salary levels, it is referring to salary levels based on current (at the relevant point in time) data that, in the case of the long test salary level, would exclude the lowest-paid 10 percent of exempt EAP employees in low-wage industries and areas and, in the case of the short test salary level, would be 149 percent of a contemporaneous long test salary level. The short test salary ratio of 149 percent is the simple average of the 15 historical ratios of the short test salary level to the long test salary level. *See* 81 FR 32467 & n.149.

<sup>50</sup> 69 FR 22169.

<sup>51</sup> *See id.* (Table 3).

<sup>52</sup> *Id.* at 22172.

<sup>53</sup> *Id.* at 22171.

<sup>54</sup> 81 FR 32550.

<sup>55</sup> *Id.*

<sup>56</sup> *Id.* at 32551.

<sup>57</sup> *See id.*

<sup>58</sup> *See id.* at 32550–51 (§ 541.602(a)(3)).

<sup>59</sup> *Id.* at 32405 (noting the historical range of short test salary levels was \$889 to \$1,231 based on an application of the short test methodology to contemporaneous data).

<sup>60</sup> *Id.* at 32444.

<sup>61</sup> *See Nevada v. U.S. Department of Labor*, 218 F. Supp. 3d 520 (E.D. Tex. 2016).

<sup>62</sup> *See Nevada*, 275 F.Supp.3d 795 (E.D. Tex. 2017).

<sup>63</sup> *See* 84 FR 10900 (Mar. 22, 2019).

<sup>64</sup> *See* 84 FR 51230.

<sup>65</sup> The Department established special salary levels of \$455 per week for Puerto Rico, Guam, the U.S. Virgin Islands, and the CNMI (effectively continuing the 2004 salary level); it also maintained the 2004 rule's \$380 per week special salary level for employees in American Samoa. 84 FR 51246.

<sup>66</sup> *See id.* at 51241–43.

<sup>67</sup> *See id.* at 51242.

<sup>68</sup> *Id.* at 51244.

<sup>69</sup> *Id.* at 51251.

<sup>70</sup> *See id.* at 51251–52.

<sup>71</sup> A lawsuit challenging the 2019 rule was filed in August 2022 and, at the time this proposal was drafted, remains pending in the U.S. District Court for the Western District of Texas. *Mayfield v. U.S. Department of Labor*, Case No. 1:22-cv-00792.

sections 13(a)(1) and 13(a)(17). The employer bears the burden of establishing the applicability of any exemption from the FLSA's pay requirements.<sup>72</sup> Job titles and job descriptions do not determine exemption status, nor does merely paying an employee a salary rather than an hourly rate.

To satisfy the EAP exemption, employees must meet certain tests regarding their job duties<sup>73</sup> and generally must be paid on a salary basis at least the amount specified in the regulations.<sup>74</sup> Some employees, such as doctors, lawyers, teachers, and outside sales employees, are not subject to salary tests.<sup>75</sup> Others, such as academic administrative personnel and computer employees, are subject to special, contingent earning thresholds.<sup>76</sup> The standard salary level for the EAP exemption is currently \$684 per week (equivalent to \$35,568 per year), and the total annual compensation level for highly compensated employees under the HCE test is currently \$107,432.<sup>77</sup> A special salary level of \$455 per week applies to employees in Puerto Rico, Guam, the U.S. Virgin Islands, and the CNMI;<sup>78</sup> a special salary level of \$380 per week applies to employees in American Samoa;<sup>79</sup> and employers can pay a special weekly "base rate" of \$1,043 per week to employees in the motion picture producing industry.<sup>80</sup> Nondiscretionary bonuses and incentive payments (including commissions) paid on an annual or more frequent basis may be used to satisfy up to 10 percent of the standard or special salary levels.<sup>81</sup>

Under the HCE test, employees who receive at least \$107,432 in total annual compensation 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.<sup>82</sup> The HCE test applies only to employees whose primary duty includes performing office or non-manual work.<sup>83</sup> Employees qualifying for exemption under the HCE test must receive at least the \$684 per week standard salary portion of their pay on a salary or fee basis without regard to the payment of nondiscretionary bonuses and incentive payments.<sup>84</sup>

### III. Need for Rulemaking

The goal of this rulemaking is to set effective earnings thresholds to help define and delimit the FLSA's EAP exemption. To this end, the Department is proposing to make appropriate increases to the standard salary level and the HCE test's total annual compensation requirement, apply the standard salary level to territories subject to the Federal minimum wage, and update the special salary levels for American Samoa and the motion picture industry. The Department is also proposing to maintain the effectiveness of these earnings thresholds by adding a provision to automatically update the standard salary level and the HCE annual compensation threshold every 3 years with current wage data (which would also have the effect of updating the levels in American Samoa and for the motion picture industry). The updating mechanism would also temporarily delay a scheduled automatic update if, and while, the Department engages in notice-and-comment rulemaking to change the salary level methodology and/or the updating mechanism.

The part 541 regulations have always included salary requirements. From the beginning, there has been "wide agreement" that the amount paid to an employee is "a valuable and easily applied index to the 'bona fide' character of the employment for which [the] exemption is claimed."<sup>85</sup> Because EAP employees "are denied the protection of the Act," they are "assumed [to] enjoy compensatory privileges" which distinguish them from nonexempt employees, including substantially higher pay.<sup>86</sup> The

Department has long recognized that the salary level test is a useful criterion for identifying bona fide EAP employees and providing a practical guide for employers and employees, thus tending to reduce litigation and ensuring nonexempt employees receive the overtime protection to which they are entitled.<sup>87</sup> The salary level test also facilitates application of the exemption by saving employees and employers from having to apply the more time-consuming duties analysis to a large group of employees who do not meet the duties test.<sup>88</sup> For these reasons, the salary level test has been a key part of how the Department defines and delimits the EAP exemption since the beginning of its rulemaking on the EAP exemption.<sup>89</sup> However, the Department has always recognized that any salary level will result in some employees who meet the duties test but do not earn enough to meet the salary level test, and thus are nonexempt and therefore eligible for overtime by virtue of their pay.<sup>90</sup> This is simply a feature of a salary level test; it does not undermine the efficacy of the salary level test but instead is taken into account in determining where the salary level is set.

The Department continues to believe that the amount paid to an employee is important evidence that they are employed in a bona fide EAP capacity, and that the salary level test "is a vital element in the regulations."<sup>91</sup> The salary level test benefits employees and employers alike, which is why—despite disagreement over the appropriate magnitude of the part 541 earnings thresholds—an "overwhelming majority" of stakeholders have supported the retention of such thresholds in prior part 541 rulemakings.<sup>92</sup>

The Department's authority to set a salary level is not without limits, and the salary test's role in defining and delimiting the scope of the EAP exemption must allow for additional examination of employee duties for employees whose salary exceeds the

compensatory benefits received by EAP employees, which set them apart from non-EAP employees.").

<sup>87</sup> See 84 FR 51237; Weiss Report at 8.

<sup>88</sup> Report and Recommendations on Proposed Revision of Regulations, Part 541, Under the Fair Labor Standards Act, by Harry S. Kantor, Assistant Administrator, Office of Regulations and Research, Wage and Hour and Public Contracts Divisions, U.S. Department of Labor (Mar. 3, 1958) (Kantor Report) at 2–3; 69 FR 22165; 84 FR 51280.

<sup>89</sup> See 84 FR 51237.

<sup>90</sup> See, e.g., Kantor Report at 5.

<sup>91</sup> Weiss Report at 9.

<sup>92</sup> 84 FR 51235; see also Stein Report at 5, 19; Weiss Report at 9.

<sup>72</sup> See, e.g., *Idaho Sheet Metal*, 383 U.S. at 209; *Walling*, 330 U.S. at 547–48.

<sup>73</sup> For a description of the duties that are required to be performed under the EAP exemption, see §§ 541.100 (executive employees); 541.200 (administrative employees); 541.300, 541.303–.304 (teachers and professional employees); 541.400 (computer employees); 541.500 (outside sales employees).

<sup>74</sup> Alternatively, administrative and professional employees may be paid on a fee basis for a single job regardless of the time required for its completion as long as the hourly rate for work performed (*i.e.*, the fee payment divided by the number of hours worked) would total at least the weekly amount specified in the regulation if the employee worked 40 hours. See § 541.605.

<sup>75</sup> See §§ 541.303(d); 541.304(d); 541.500(c); 541.600(e). Such employees are also not subject to a fee basis test.

<sup>76</sup> See § 541.600(c) and (d).

<sup>77</sup> See §§ 541.600(a); 541.601(a)(1).

<sup>78</sup> See §§ 541.100; 541.200; 541.300.

<sup>79</sup> See *id.*

<sup>80</sup> See § 541.709.

<sup>81</sup> § 541.602(a)(3).

<sup>82</sup> § 541.601.

<sup>83</sup> § 541.601(d).

<sup>84</sup> See § 541.601(b)(1); see also 84 FR 51249.

<sup>85</sup> Stein Report at 19.

<sup>86</sup> *Id.*; see also Report of the Minimum Wage Study Commission, Volume IV, p. 236 ("Higher base pay, greater fringe benefits, improved promotion potential and greater job security have traditionally been considered as normal

salary level.<sup>93</sup> Examination of duties for such employees is necessary in part because the salaries earned by employees who do and do not perform exempt job duties overlap. As explained in greater detail below, the proposed standard salary level set at the 35th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (\$1,059 per week, \$55,068 annually) would, in combination with the standard duties test, better identify which employees are employed in a bona fide EAP capacity in a one-test system. By setting a salary level above what would currently be the equivalent of the long test salary level (\$925 per week), the proposal would restore the right to overtime pay for salaried white-collar employees who prior to the 2019 rule were always considered nonexempt if they earned below the long test (or long test-equivalent) salary level and ensure that fewer white-collar employees who perform significant amounts of nonexempt work and earn between the long and short test salary levels are included in the exemption. At the same time, by setting the standard salary level well below what would currently be the equivalent of the short test salary level (\$1,378 per week),<sup>94</sup> the proposal would address the concerns that have been raised about excluding from the EAP exemption too many white-collar employees solely based on their salary level. As discussed in section IV.A.4 below, the duties test would continue to determine exemption status for almost three-quarters of all salaried white-collar employees subject to the part 541 regulations, allowing employers to continue to use the exemption for 24.5 million salaried white-collar workers who earn at least the proposed salary level and meet the standard duties test.<sup>95</sup> The proposed salary level would also reasonably distribute between employees and their employers what the Department now understands to be the impact of the shift from a two-test to a one-test system on employees earning

between the long and short test salary levels.

Since switching from a two-test to a one-test system for defining and delimiting the EAP exemption in 2004, the Department has followed different approaches to set the single standard salary level. In 2004, the Department set the new standard salary level roughly equivalent to the 20th percentile of weekly earnings of full-time salaried workers in the South and in the retail industry nationwide (\$455 per week).<sup>96</sup> This approach produced a salary level amount that was equivalent to the lower long test salary level under the two-test system.<sup>97</sup> Because it was equivalent to the long test salary level, employees who historically earned less than the long test salary level continued to be entitled to overtime compensation because they earned below the new standard salary level. However, because the new standard duties test was substantially equivalent to the less rigorous short duties test,<sup>98</sup> employees who were paid the equivalent of the lower long test salary level and who met the less rigorous short duties test also now met the standard duties test and were not entitled to overtime compensation. This approach broadened the EAP exemption because all employees between the long and short test salary levels who historically had not been considered bona fide EAP employees because they did not meet the long duties test became exempt. The Department followed this same methodology to set the standard salary level in 2019, although applying the 2004 rule's methodology resulted in a salary level that was a lower amount than what would have been the equivalent of the long test salary level.<sup>99</sup> This broadened the EAP exemption even further by, for the first time, setting a salary level that exempted a group of white-collar employees earning below the equivalent of the long test salary level (based on contemporaneous data). Both the 2004 and 2019 rules thus effectively placed the impact of the shift from a two-test to a one-test system on lower-salaried white-collar employees—both those who earned below the short test salary level and were traditionally protected by the more rigorous long duties test (*i.e.*, because they performed substantial amounts of nonexempt work), and, in the case of the 2019 rule, those who had previously been

protected by a salary level set at or equivalent to the long test salary.

To address the concern that the 2004 rule did not provide overtime compensation for lower-salaried white-collar employees performing large amounts of nonexempt work who historically were not considered bona fide EAP employees, in 2016 the Department set the standard salary level at the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (the South), which produced a salary level that was at the low end of the historical range of short test salary levels.<sup>100</sup> This approach restored overtime protection to white-collar employees who perform substantial amounts of nonexempt work and earned between the equivalent of the long test salary level and the short test salary level. However, this approach also made nonexempt some employees who had previously met the long duties test—employees who earned between the long test salary level and the low end of the short test salary range and performed only a limited amount of nonexempt work. Until 2004 employers could use the long test to exempt these employees, and under the 2004 rule these employees remained exempt under the one-test system. Thus, the impact of the 2016 rule was that employers could not use the exemption for certain white-collar employees who earned between the long and short test salary levels and would have met the more rigorous long duties test.<sup>101</sup> In the challenge to the 2016 rule, the district court expressed concern that the 2016 rule conferred overtime eligibility based on salary level alone to a substantial number of employees who would otherwise be exempt.<sup>102</sup>

Having grappled with the different approaches that it has used to set the standard salary level since switching to a one-test system in 2004, the Department's goal in this rulemaking is not only to update the single standard salary level to account for earnings growth since the 2019 rule, but also to build on the lessons learned in its most recent rulemakings to more effectively define and delimit employees employed in a bona fide EAP capacity. Consistent with its broad authority under the statute, the Department is proposing a standard salary level test that would work effectively with the standard duties test to help achieve these objectives and would also reasonably distribute the impact of the switch to a one-test system across white-collar

<sup>93</sup> 84 FR 51238 (noting salary's "useful, but limited, role").

<sup>94</sup> During the period from 1949 to 2004, the ratio of the short test salary level to the long test salary levels ranged from approximately 130 percent to 180 percent. See 81 FR 32403. The simple average of the 15 historical ratios of the short test salary level to the long test salary level is 149 and the Department calculates the short test salary level as 149 percent of the long test salary level. See *id.* at 32467 & n.149.

<sup>95</sup> This number does not include the additional 8.1 million workers employed in occupations that are not subject to the salary level test, such as doctors, lawyers, and teachers. Such employees are unaffected by this rulemaking because their exemption status is always determined by the duties test.

<sup>96</sup> See 69 FR 22168.

<sup>97</sup> See *id.* at 22168–69.

<sup>98</sup> *Id.* at 22214.

<sup>99</sup> See 84 FR 51260 (Table 4) (showing that the salary level derived from the Department's long test methodology would have been \$724 per week rather than the finalized \$684 per week amount).

<sup>100</sup> 81 FR 32405.

<sup>101</sup> See 84 FR 10908; 84 FR 51242.

<sup>102</sup> See *Nevada*, 275 F.Supp.3d. at 806.



employees earning between the long and short test salary levels and their employers. In 2004 and 2019, setting the salary level equivalent to or below the lower long test salary level resulted in the exemption of lower-salaried employees who perform large amounts of nonexempt work, in effect significantly broadening the exemption compared to under the two-test system. This approach included in the exemption lower-salaried employees whom the Department had long considered not to be employed in a bona fide EAP capacity because they performed substantial amounts of nonexempt work. Under the 2016 approach, setting the salary level equivalent to the low end of the higher short test salary range would have restored overtime protections to those employees who perform substantial amounts of nonexempt work and earned between the long test salary level and the low end of the short test salary levels. However, it also would have resulted in denying employers the use of the exemption for many lower-salaried employees who traditionally were exempt under the long test, which raised concerns that the Department was in effect narrowing the exemption compared to the two-test system.<sup>103</sup> In this rulemaking, the Department proposes setting a standard salary level that would better define and delimit the EAP exemption by more effectively accounting for the switch from a two-test to a one-test system, and reasonably distribute the impact of the shift by ensuring overtime protection for some lower-salaried employees without excluding from exemption too many white-collar employees solely based on their salary level.<sup>104</sup>

In addition, consistent with its previously stated intent, the Department is undertaking this rulemaking to keep the earnings thresholds up to date. Four years have passed since the 2019 rule, during which time salaried workers in the U.S. economy have experienced a rapid growth in their nominal wages, which lessens the effectiveness of the current salary level threshold. Reapplying the same methodology that was used to set the standard salary level in 2019 to recent earnings data would result in a new threshold of \$822 per week—a 20.2 percent increase over the current \$684 per week standard salary level.<sup>105</sup> Applying the long test salary methodology to current data would result in a salary threshold of \$925 per

week—a 35.2 percent increase over the current salary level.

The Department is also proposing to increase the HCE total annual compensation threshold to the annualized weekly earnings amount of the 85th percentile of full-time salaried workers nationally (\$143,988). Reapplying the 2019 methodology (annualized weekly earnings of the 80th percentile of full-time salaried workers nationally) to current earnings data results in a threshold of \$125,268 per year—a 16.6 percent increase over the current threshold of \$107,432. Other data further supports that the HCE test's current total annual compensation requirement has become outdated. When it was created in 2004, the HCE test featured a \$100,000 threshold that exceeded the annual earnings of approximately 93.7 percent of salaried workers nationwide.<sup>106</sup> More recently in the 2019 rule, the Department set the HCE test threshold so it would be equivalent to the annual earnings of the 80th percentile of full-time salaried workers nationwide. Today, however, the \$107,432 HCE threshold is approximately the 72nd percentile of annual earnings of full-time salaried workers nationwide. The Department's proposed increase from the 80th to the 85th percentile is high enough to exclude employees who are not "at the very top of [the] economic ladder"<sup>107</sup> and would ensure that this test for exemption continues to serve its intended function.

The salary levels applicable to the U.S. territories have not increased since 2004. In 2004, the Department ended the use of special salary levels in territories that had become subject to the Federal minimum wage since the salary levels were last set in 1975, and applied a special salary level of \$380 per week only to employees in American Samoa, who were subject to special minimum wage rates below the Federal minimum wage.<sup>108</sup> In 2019, however, the Department established a special salary level of \$455 per week for employees in Puerto Rico, Guam, the U.S. Virgin Islands, and the CNMI, for the first time setting a special salary level in territories that were subject to the Federal minimum wage.<sup>109</sup> The Department also maintained the special salary level for American Samoa at \$380 per week, the level set in 2004. There is thus a compelling need to increase the salary levels applicable to employees in U.S. territories,

particularly employees in those territories that are subject to the Federal minimum wage.

Finally, the Department proposes to adopt a mechanism to automatically update the earnings thresholds in the part 541 regulations in future years. In its three most recent part 541 rulemakings, the Department has expressed its commitment to keeping the salary level tests up to date. In its 2004 rule, the Department conveyed its intent "in the future to update the salary levels on a more regular basis."<sup>110</sup> In its 2016 rule, the Department adopted a mechanism to automatically update the salary level on a triennial basis. In 2019, after initially proposing to codify its commitment to updating the threshold every 4 years through rulemaking, the Department affirmed in its final rule that it "intends to update these thresholds more regularly in the future."<sup>111</sup> As noted above, however, the history of the part 541 regulations shows multiple, significant gaps during which the salary levels were not updated and their effectiveness in helping to define the EAP exemption decreased as wages increased. While the Department increased its part 541 earnings thresholds every 5 to 9 years in the 37 years between 1938 and 1975, more recent decades have included long periods without raising the salary level, resulting in significant erosion of the real value of the threshold levels followed by unpredictable increases. As explained in greater detail in section IV.D, employees and employers alike would benefit from the certainty and stability of regularly scheduled updates.

#### IV. Discussion of Proposed Rule

Consistent with its statutory duty to define and delimit the EAP exemption, the Department is proposing increases to the earnings thresholds provided in the part 541 regulations. As explained in greater detail below, the Department proposes to increase the standard salary level to the 35th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (currently the South). The Department also proposes to apply this updated standard salary level to the four U.S. territories that are subject to the Federal minimum wage—Puerto Rico, Guam, the U.S. Virgin Islands, and the CNMI—and to update the special salary levels for American Samoa and the motion picture industry in relation to the new standard salary level. The Department additionally proposes raising the HCE test's total annual compensation

<sup>103</sup> See 84 FR 51242.

<sup>104</sup> See section IV.A.3.

<sup>105</sup> See section VII.C.5 (applying CPS MORG data from calendar year 2022).

<sup>106</sup> See 69 FR 22169 (Table 3).

<sup>107</sup> *Id.* at 22174.

<sup>108</sup> See *id.* at 22172.

<sup>109</sup> See 84 FR 51246.

<sup>110</sup> 69 FR 22171.

<sup>111</sup> 84 FR 51251–52.



requirement to the annual equivalent of the 85th percentile of weekly earnings of full-time salaried workers nationally (\$143,988). Finally, the Department proposes a new mechanism to automatically update the standard salary level and the HCE total annual compensation threshold every 3 years to ensure that they remain effective tests for exemption.

While the primary regulatory changes proposed are in §§ 541.600, 541.601, 541.709, and newly-added § 541.607, additional conforming changes are proposed to update references to the salary level throughout part 541. The Department is not proposing any changes to the salary basis or duties test requirements in this rulemaking. The Department welcomes comments on all aspects of this proposal.

#### A. Standard Salary Level

The salary level test is grounded in the text of section 13(a)(1). The Secretary's expressly-delegated authority to "define[]" and "delimit[]" the terms of the EAP exemption includes the authority to use a salary level test as one criterion for identifying employees who are employed in a "bona fide executive, administrative, or professional capacity." The Department has used a salary level test since the first part 541 regulations in 1938. From the FLSA's earliest days, stakeholders have generally favored the use of a salary test,<sup>112</sup> and the Department's authority to use a salary test has been repeatedly upheld.<sup>113</sup>

Despite numerous amendments to the FLSA over the past 85 years, Congress has not restricted the Department's use of the salary level tests. Significant regulatory changes involving the salary requirements since 1938 include adding a separate salary level for professional employees in 1940, adopting a two-test system with separate short and long test salary levels in 1949, and creating a single standard salary level test and establishing a new HCE exemption test in 2004. These changes were all made through regulations issued pursuant to the Secretary's authority to define and delimit the exemption. Despite having amended the FLSA numerous times over the years, Congress has not amended section 13(a)(1) to alter these regulatory salary requirements.

The FLSA delegates to the Secretary the power to "define[]" and "delimit[]" the terms "bona fide executive,

administrative, or professional capacity" through regulation. Congress thus "provided that employees should be exempt who fell within certain general classifications"—those employed in a bona fide executive, administrative, or professional capacity—and authorized the Secretary "to define and delimit those classifications by reasonable and rational specific criteria."<sup>114</sup> Therefore, the Department "is responsible not only for determining which employees are entitled to the exemption, but also for drawing the line beyond which the exemption is not applicable."<sup>115</sup>

As the Department stated in its 2019 rule, an employee's salary level "is a helpful indicator of the capacity in which an employee is employed, especially among lower-paid employees."<sup>116</sup> The amount an employee is paid is also a "valuable and easily applied index to the 'bona fide' character of employment for which exemption is claimed," as well as the "principal[]" "delimiting requirement" "prevent[ing] abuse" of the exemption.<sup>117</sup> As the Department has explained, if an employee "is of sufficient importance . . . to be classified as a bona fide" executive employee, for example, and "thereby exempt from the protection of the [A]ct, the best single test of the employer's good faith in attributing importance to the employee's services is the amount [it] pays for them."<sup>118</sup> Employee compensation is a relevant indicator of exemption status given that the EAP exemption is premised on the understanding that individuals who are employed in a bona fide executive, administrative, or professional capacity typically earn higher salaries and enjoy other privileges to compensate them for their long hours of work, setting them apart from nonexempt employees entitled to overtime pay.<sup>119</sup>

<sup>114</sup> *Walling*, 140 F.2d at 831–32; see *Ellis v. J.R.'s Country Stores, Inc.*, 779 F.3d 1184, 1199 (10th Cir. 2015) (approvingly quoting *Walling*); see also *Auer v. Robins*, 519 U.S. 452, 456 (1997) ("The FLSA grants the Secretary broad authority to 'defin[e] and delimit[t]' the scope of the exemption for executive, administrative, and professional employees.").

<sup>115</sup> Stein Report at 2.

<sup>116</sup> 84 FR 51239 (internal quotation marks omitted).

<sup>117</sup> Stein Report at 19, 24; see also 81 FR 32422.

<sup>118</sup> Stein Report at 19, 24; see also *id.* at 26 ("[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 is properly describable as an employee employed in a bona fide administrative capacity.").

<sup>119</sup> See Report of the Minimum Wage Study Commission, Vol. IV, at 236, 240; see also, e.g., Stein Report at 19 (explaining that the "term 'executive' implies a certain prestige, status, and

Consistent with the Department's longstanding approach, the proposed rule ensures that the salary level test and duties test continue to complement each other to define and delimit the EAP exemption and that the salary level does not play an outsized role in determining whether an individual is employed in a bona fide EAP capacity.<sup>120</sup> In part because of the overlap in the salaries earned by employees who do and do not perform exempt job duties, the salary level must allow for appropriate examination of duties. As discussed in section IV.A.4, under the Department's proposed standard salary level, the duties test will determine the exemption status for most white-collar employees.

The Department's proposed standard salary level will, in combination with the standard duties test, better define and delimit which employees are employed in a bona fide EAP capacity in a one-test system. By setting a salary level above the equivalent of the long test salary level, the proposal would (unlike the 2004 and 2019 rules) ensure that not all lower-paid white-collar employees who perform significant amounts of nonexempt work, and were historically considered by the Department not to be employed in a bona fide EAP capacity because they failed the long duties test, are included in the exemption. At the same time, by setting it well below the equivalent of the short test salary level, the proposal would address potential concerns that the salary level test should not be determinative of EAP exemption status for too many white-collar employees. The combined effect would be a more effective test for exemption. The proposed salary level would also reasonably distribute between employees and their employers what the Department now understands to be the impact of the 2004 shift from a two-test to a one-test system on employees earning between the long and short test salary levels.

#### 1. History of the Salary Level

The first version of the part 541 regulations, issued in 1938, set a minimum compensation requirement of \$30 per week for executive and administrative employees.<sup>121</sup> Since then, the Department has increased the

importance" denoted by pay "substantially higher than" the Federal minimum wage).

<sup>120</sup> The Department has consistently stated that salary alone cannot define who is a bona fide EAP employee. See 84 FR 51239; 81 FR 32429; 69 FR 22173.

<sup>121</sup> 3 FR 2518.

<sup>112</sup> See Stein Report at 5, 19.

<sup>113</sup> See, e.g., *Wirtz v. Miss. Publishers Corp.*, 364 F.2d 603, 608 (5th Cir. 1966); *Fanelli v. U.S. Gypsum Co.*, 141 F.2d 216, 218 (2d Cir. 1944); *Walling v. Yeakley*, 140 F.2d 830, 832–33 (10th Cir. 1944).

salary levels eight times—in 1940, 1949, 1958, 1963, 1970, 1975, 2004, and 2019.

In 1940, the Department maintained the \$30 per week salary level for executive employees but established a higher \$200 per month salary level test for administrative and professional employees. In selecting these thresholds, the Department used salary surveys from Federal and State Government agencies, experience gained under NIRA, and Federal Government salaries to determine the salary level that was a reasonable “dividing line” between employees performing exempt and nonexempt work.<sup>122</sup>

In 1949, 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” to protect small businesses.<sup>123</sup> In 1949, the Department also established a short test for exemption, which paired a higher salary level with a less rigorous duties test. The justification for this short test was that employees who met the higher salary level were more likely to meet all the requirements of the exemption (including the 20 percent limit on nonexempt work), and thus a “short-cut test of exemption . . . would facilitate the administration of the regulations without defeating the purposes of section 13(a)(1).”<sup>124</sup> Employees who met only the lower long test salary level, and not the higher short test salary level, were still required to satisfy the long duties test, which included a limit on the amount of nonexempt work that an exempt employee could perform. The two-test system remained part of the Department’s regulations until 2004.

In 1958, the Department reiterated that salary is a “mark of [the] status” of an exempt employee and reinforced the importance of salary as an enforcement tool, adding that the Department had “found no satisfactory substitute for the salary tests.”<sup>125</sup> To set the salary levels, 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 in place at the

time) and set the salary levels at \$80 per week for executives and \$95 per week for administrative and professional employees.<sup>126</sup> The Department set the long test salary levels so that only a limited number of employees performing EAP duties (about 10 percent) in the lowest-wage regions and industries would fail to meet the new salary level and therefore become entitled to overtime pay.<sup>127</sup> In laying out this methodology, often referred to as the “Kantor” methodology and generally referenced in this NPRM as the “long test” methodology, the Department echoed its prior comments stating that the salary tests “simplify enforcement by providing a ready method of screening out the obviously nonexempt employees.”<sup>128</sup>

The Department followed a similar methodology when determining the appropriate long test salary level in 1963, using data regarding salaries paid to exempt workers collected in a 1961 WHD survey.<sup>129</sup> The salary level for executive and administrative employees was increased to \$100 per week, and the professional exemption salary level was increased to \$115 per week.<sup>130</sup> The Department noted that these salary levels approximated the methodology used in 1958 to set the long test salary levels.<sup>131</sup>

The Department continued to use a similar methodology when it updated the 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,<sup>132</sup> the Department increased the long test salary level for executive and administrative employees to \$125 per week and increased the long test salary level for professional employees to \$140 per week.<sup>133</sup>

In 1975, instead of following the previous long test methodology, the Department set the long test salary levels “slightly below” the amount suggested by adjusting the 1970 salary levels for inflation based on increases in the Consumer Price Index (CPI).<sup>134</sup> The long test salary level for executive and administrative employees was set at \$155, while the professional level was set at \$170. The salary levels adopted

were intended to be 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.<sup>135</sup> The envisioned process was never completed, however, and the “interim” salary levels remained unchanged for the next 29 years.

The short test salary level increased in tandem with the long test level throughout the various rulemakings between 1949 and 2004. Because the short test was designed to capture only those white-collar employees whose salary was high enough to indicate a stronger likelihood of being employed in a bona fide EAP capacity and thus warrant a less stringent duties requirement, the short test salary level was always set significantly higher than the long test salary level.

When the Department updated the part 541 regulations in 2004, it opted to create a single standard test for exemption instead of retaining the two-test system from prior rulemakings. The Department set the new standard salary level at \$455 per week and paired it with a duties test that was substantially equivalent to the less rigorous short duties test. In setting the new standard salary level, the Department looked at nonhourly earnings from the CPS MORG data collected by BLS.<sup>136</sup> The Department set a salary level that would exclude from exemption roughly the bottom 20 percent of full-time salaried employees in each of two subpopulations: (1) the South and (2) the retail industry nationally. In setting the salary level the Department looked to earnings data for all white-collar workers—exempt and nonexempt—and looked to a higher percentile than the long test methodology (10th percentile of exempt workers in low-wage industries and areas). The Department acknowledged, however, that the salary arrived at by this method was, at the time, equivalent to the salary derived from the long test method using current data.<sup>137</sup>

In the 2016 rule, the Department again used CPS MORG data but set the standard salary level equal to the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (the South),

<sup>126</sup> *Id.* at 6, 9.

<sup>127</sup> *Id.* at 6–7.

<sup>128</sup> *Id.* at 2–3; see Weiss Report at 8.

<sup>129</sup> 28 FR 7002 (July 9, 1963).

<sup>130</sup> *Id.* at 7004.

<sup>131</sup> *Id.*

<sup>132</sup> See 34 FR 9934, 9935 (June 24, 1969).

<sup>133</sup> 35 FR 885.

<sup>134</sup> 40 FR 7091.

<sup>135</sup> *Id.* at 7091–92.

<sup>136</sup> See 69 FR 22166–67.

<sup>137</sup> *Id.* at 22168. The 2004 methodology used the 20th percentile of a data set of all full-time salaried workers and the long test methodology looked to the lowest-paid 10 percent of exempt salaried workers. The two methodologies resulted in equivalent salary levels because exempt salaried workers generally have higher earnings than nonexempt salaried workers.

<sup>122</sup> See Stein Report at 20–21, 31–32.

<sup>123</sup> Weiss Report at 8, 14.

<sup>124</sup> *Id.* at 22–23.

<sup>125</sup> Kantor Report at 2–3.

resulting in a standard salary level of \$913 per week, which was at the low end of the historic range of short test salary levels. The Department explained that the increase in the standard salary level was needed because the 2004 rule exempted lower-salaried employees performing large amounts of nonexempt work who should be covered by the overtime compensation requirement.<sup>138</sup> Since the standard duties test was equivalent to the short duties test, the Department asserted that a salary level in the short test salary range was necessary to address this effect of the 2004 rule. As explained earlier, the U.S. District Court for the Eastern District of Texas held the 2016 rule invalid.

In updating the standard salary level in 2019, the Department reapplied the methodology from the 2004 rule, setting the salary level equal to the 20th percentile of weekly earnings of full-time salaried workers in the South and in the retail sector nationwide.<sup>139</sup> This methodology addressed concerns that had been raised that the 2016 methodology excluded too many employees from the exemption based on their salary alone. Unlike in 2004, however, where the 20th percentile of weekly earnings of full-time salaried workers in the South and retail nationally was essentially the same as the long test, this methodology now produced a salary level amount that was lower than the equivalent of the long test salary level using contemporaneous data. This methodology produced the current standard salary level of \$684 per week (equivalent to \$35,568 per year).<sup>140</sup>

## 2. Salary Level Test Function and Effects

Since 1940, the Department's regulations have consistently looked at both the duties performed by the employee and the salary paid by the employer in defining and delimiting who is a bona fide executive, administrative, or professional employee exempt from the FLSA's minimum wage and overtime protections. From 1949 to 2004, the Department determined EAP exemption status using a two-test system comprised of a long test (a lower salary level paired with a more rigorous duties test that limited performance of nonexempt work to no more than 20 percent for most employees) and a short test (a higher salary level paired with a less rigorous duties test that looked to the employee's primary duties and did

not have a numerical limit on the amount of nonexempt work). The two-test system facilitated the determination of whether white-collar workers across the income spectrum were employed in a bona fide EAP capacity, and employees who met either test could be classified as EAP exempt.

In a two-test system, the long test salary level screens from the exemption the lowest-paid white-collar employees, thereby ensuring their right to overtime compensation. The Department has often referred to many of the employees who are screened from the exemption by virtue of their earning below the lower long test salary level as "obviously nonexempt employees[.]"<sup>141</sup> The long test salary level helped distinguish employees who were not employed in a bona fide EAP capacity because the Department found that employees who were screened from exemption by the long test salary level generally did not meet the other requirements for exemption.<sup>142</sup> Since 1958, the long test salary level was generally set to exclude from exemption approximately the lowest-paid 10 percent of salaried white-collar employees who performed EAP duties in the lowest-wage regions and industries.<sup>143</sup> The long test salary level also served as a line delimiting the population of white-collar employees for whom the duties test determined their exemption status. In the two-test system, this duties analysis included an examination of the amount of nonexempt work performed, which ensured that employees earning lower salary levels were, in fact, employed in a bona fide EAP capacity by limiting the amount of time they could spend on nonexempt work. Thus, the Department long recognized that lower salaried workers should be subject to a test that placed significant limits on the amount of nonexempt work they perform. The duties and salary level tests worked in tandem to properly define and delimit the exemption: lower-paid workers had to satisfy a more rigorous duties test with strict limits on nonexempt work; higher paid employees were subject to a less rigorous duties test because they were more likely to satisfy all the requirements of the exemption (including the limit on nonexempt work).<sup>144</sup>

<sup>141</sup> See *id.* at 51237 (quoting Kantor Report at 2–3).

<sup>142</sup> See Kantor Report at 2–3; Weiss Report at 8 ("In an overwhelming majority of cases, it has been found by careful inspection that personnel who did not meet the salary requirements would also not qualify under other sections of the regulations[.]").

<sup>143</sup> See 84 FR 51236.

<sup>144</sup> Weiss Report at 22–23.

Because employees who met the short test salary level were paid well above the long test salary level, the short test salary level did not perform the same function as the long salary level of screening obviously nonexempt employees. Instead, the short test salary level was used to determine whether the full duties test or the short-cut duties test would be applied to determine EAP exemption status. The exemption status of employees paid more than the long and less than the short test salary levels was determined by applying the more rigorous long duties test that ensured overtime protections for employees who performed substantial amounts of nonexempt work. The exemption status of employees paid at or above the higher short test salary level was determined by the less rigorous short duties test that looked to the employee's primary duty and did not cap the amount of nonexempt work an employee could perform. The short test thus provided a faster and more efficient duties test based on the Department's experience that employees paid at the higher short test salary level "almost invariably" met the more rigorous long duties test, including its 20 percent limit on nonexempt work, and therefore a shortened analysis of duties was a more efficient test for exemption status.<sup>145</sup>

In 2004, rather than update the two-test system, the Department chose to establish a new single-test system for determining exemption status. The new single standard test for exemption used a duties test that was substantially equivalent to the less rigorous short duties test in the two-test system.<sup>146</sup> Since the creation of the standard test, the Department has taken two different approaches to set the standard salary level that pairs with the standard duties test.

In 2004, as noted above, the Department set the new salary level roughly equivalent to the 20th percentile of weekly earnings of full-time salaried workers in the South and in the retail industry nationwide.<sup>147</sup> The Department acknowledged that the salary level (\$455 per week) was, in fact, equivalent to the lower long test salary level amount under the two-test system using contemporaneous data.<sup>148</sup> Because it was equivalent to the long test salary level, the standard salary test continued to perform the same initial screening function as the long test salary level and employees who historically were entitled to overtime compensation

<sup>145</sup> *Id.*

<sup>146</sup> 69 FR 22214.

<sup>147</sup> See *id.* at 22168–69.

<sup>148</sup> See *id.*

<sup>138</sup> 81 FR 32405.

<sup>139</sup> See 84 FR 51260 (Table 4).

<sup>140</sup> *Id.* at 51238.

because they earned below the long test salary level remained nonexempt under the new standard test. Without a higher salary short test, however, all employees who met the standard salary level were subject to the same duties test. The single standard duties test was equivalent to the short duties test, and so some employees who previously did not meet the long duties test met the standard duties test. As a result, the shift from a two-test to a one-test system significantly broadened the EAP exemption because employees who historically had not been considered bona fide EAP employees—in particular, those lower-paid employees who did not meet the long duties test because they performed substantial amounts of nonexempt work—were now defined as falling within the exemption and would not be eligible for overtime compensation.

This broadening specifically impacted lower-paid, salaried white-collar employees who earned between the long and short test salary levels and performed substantial amounts of nonexempt work. Under the two-test system, these employees had been entitled to overtime compensation if their nonexempt duties exceeded the long test's strict limit on such work. Under the 2004 standard test, these employees became exempt because they met both the low standard salary level and the less rigorous standard duties test. The Department's discussion of the elimination of the long duties test in 2004 focused primarily on the minimal role played by the long test at that time due to the erosion of the long salary level, and on the difficulties employers would face if they were again required to track time spent on nonexempt work when the dormancy of the long duties test meant that they had generally not been performing such tracking for many years.<sup>149</sup> While asserting that employees who were then subject to the long test would be better protected under the higher salary level of the new standard test, the Department did not compare the protection lower salaried employees would receive under the standard test with the protection they would have received under an updated long test with a salary level based on contemporary data and the existing long duties test.

To address the concern that lower-salaried employees performing large amounts of nonexempt work historically were not considered bona fide EAP employees and thus should be entitled to overtime compensation, in 2016 the Department set the standard salary level

at the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (the South). This methodology produced a salary level (\$913 per week) that was at the low end of the historical range of short test salary levels.<sup>150</sup> This approach restored overtime protection for employees performing substantial amounts of nonexempt work who earned between the long and short test salary levels, as they failed the new salary level test. However, this approach generated potential concerns that the salary level test should not be determinative of exemption status for too many individuals.

Due to the 2016 rule's narrowing of the exemption, employers were unable to use the exemption for employees who earned between the long test salary level and the low end of the short test salary range and would have met the more rigorous long duties test. Prior to 2004 employers could use the long test to exempt these employees, and under the 2004 rule these employees remained exempt under the one-test system. Thus, while the 2016 rule accounted for the absence of the long duties test by restoring overtime protections to employees earning between the long test salary level and the low end of the short test salary range who perform significant amounts of nonexempt work, it also made a group of employees who had been exempt under the two-test system newly nonexempt under the one-test system: employees earning between the long test level and the short test salary range who perform only limited nonexempt work.

In its 2019 rule, the Department determined that the 2016 rule had not sufficiently considered the impact of the increased standard salary level on employers' ability to use the exemption for this group of employees.<sup>151</sup> The Department emphasized that “[f]or most . . . employees the exemption should turn on an analysis of their actual functions, not their salaries,” and that the 2016 rule's effect of making nonexempt all lower-paid, white-collar employees who traditionally were exempt under the long test “deviated from the Department's longstanding policy of setting a salary level that does not ‘disqualify[] any substantial number of’ bona fide executive, administrative, and professional employees from exemption.”<sup>152</sup> To address these concerns, the Department simply returned to the 2004 rule's methodology for setting the salary threshold. In

responding to comments that the proposed salary level did not account for the absence of the more rigorous long duties test, the 2019 rule reiterated the statements made in the 2004 rule and asserted that the 2016 rule did not adequately account for the absence of the lower long test salary level.<sup>153</sup> Applying the 2004 method to the earnings data available in 2019 produced a standard salary level of \$684 per week, which was even below the equivalent of what the long test salary level would have been using contemporaneous data (\$724 per week).<sup>154</sup>

The 2019 rule thus had the same impact as the 2004 rule of exempting all employees who earned between the long and short test salary levels and who performed too much nonexempt work to meet the long duties test, but passed the short duties test. The 2019 rule also for the first time permitted the exemption of a group of low-paid white-collar employees (those earning between \$684 and \$724 per week) who had always been protected by the salary level test's initial screening function—either under the long test, or under the 2004 rule salary level that was equivalent to the long test salary level. The Department stated that the standard salary level's “fairly small difference” from the long test level did not justify using the long test methodology to set the salary level, and emphasized that its approach preserved the salary level's principal function as a tool for screening from exemption obviously nonexempt employees.<sup>155</sup> In response to commenter concerns about the rule exempting employees who traditionally earned between the long and short test salary levels and received overtime compensation because they did not meet the long duties test, the Department cited the legal risks posed by the 2016 methodology (as evidenced by the district court's decisions) and explained that such employees were already exempt in the years leading up to 2004 because the Department's outdated salary levels had rendered the long test with its more rigorous duties requirement largely dormant.<sup>156</sup> As in the 2004 rule, the Department did not address the protection lower salaried employees would have received under the long test with an updated salary level based on contemporary data.

The Department's experience with a one-test system shows that it is less nuanced than the two-test system,

<sup>149</sup> See 69 FR 22126–27.

<sup>150</sup> 81 FR 32405.

<sup>151</sup> 84 FR 10908.

<sup>152</sup> *Id.* (quoting Kantor Report at 5).

<sup>153</sup> See 84 FR 51243.

<sup>154</sup> *Id.* at 51260.

<sup>155</sup> *Id.* at 51244.

<sup>156</sup> *Id.* at 51243.

which allowed for finer calibration in defining and delimiting the EAP exemption. In a two-test system, there are four variables (two salary levels and two duties tests) that can be adjusted to define and delimit the exemption. In a one-test system, there are only two variables (one salary level and one duties test) that can be adjusted, necessarily yielding less nuanced results. The loss in precision does not impact the lowest-paid white-collar employees, who were screened from exemption by the long test salary level, because they maintain their right to overtime pay so long as the standard salary level is set at least equivalent to the lower long test salary level—a condition that was met by the 2004 rule's salary level but not by the 2019 rule's salary level. Instead, the Department's experience shows that the shift from a two-test system to a one-test system impacts employees earning between the long and short test salary levels and, in turn, employers' ability to use the exemption for these employees.

In the two-test system, employees who earned between the long and short test salary levels and performed large amounts of nonexempt work were protected by the long duties test, while bona fide EAP employees who performed only limited amounts of nonexempt work in that earnings range were exempt. Meanwhile, the short test provided a time-saving short-cut test for higher-earning employees who would almost invariably pass the more rigorous, and thus more time consuming, long duties test. But the more rigorous long duties test, with its limitation on the amount of nonexempt work that could be performed, was always core to the two-test system, with the higher short test salary level and less rigorous short duties test serving as a time-saving mechanism for employees who would likely have met the more rigorous long duties test.

Upon reflection and based on its rulemakings over the past 20 years, the Department has determined that a one-test system that uses the standard duties test, without its limitations on the amount of nonexempt work, must use a salary level above the long test salary level in order to ensure that it is effectively identifying bona fide EAP employees. A single test system cannot fully replicate both the two-test system's heightened protection for employees performing substantial amounts of nonexempt work and its increased efficiency for determining exemption status for employees who are highly likely to perform EAP duties. One way in a one-test system to protect lower-salaried employees earning between the

long and short test salary levels who were historically entitled to overtime compensation under the long test would be to reinstate the long duties test with its limitation on nonexempt work. A one-test system with a more rigorous duties test would appropriately emphasize the important role of duties in determining exemption status. However, for the reasons discussed in this section, the Department is not proposing in this rulemaking to replace the standard duties test with the long duties test or to return to a two-test system with the long duties test. The Department has not had a one-test system with a limit on nonexempt work other than from 1940 to 1949,<sup>157</sup> when the Department replaced this approach with its two-test system, and returning to it would eliminate the benefits of the current duties test, including having a single test with which employers and employees are familiar.

In light of these considerations, the Department's goal in this rulemaking is not only to update the single standard salary level to account for earnings growth since the 2019 rule, but also to build on the lessons learned in its most recent rulemakings to more effectively define and delimit employees working in a bona fide EAP capacity. Consistent with its broad authority under section 13(a)(1), the Department is proposing a single salary level test that will work effectively with the standard duties test to better define who is employed in a bona fide EAP capacity and will both perform the initial screening function that the salary level has always played and also adjust the salary level to account for the change to a single test system.

### 3. Salary Level Methodology

The Department's extensive regulatory history shows that the two-test system for defining the EAP exemption is an effective method of determining the exemption status of white-collar employees at both lower and higher salary levels. With this system, the salary and duties components of each test balance each other and the two tests work in combination to efficiently identify exempt employees while protecting employees who should receive overtime compensation. Although the two-test system's effectiveness diminished in its later years, this was a consequence of the Department's failure to update the salary level tests after 1975, not a flaw with the two-test structure itself. Not updating the salary levels in a two-test system is particularly problematic

because the real value of the higher short test salary level will inevitably decrease, expanding the exemption to lower-paid white-collar employees who previously were not considered bona fide EAP employees because they did not meet the long duties test and earned below the short test salary level, and rendering the lower long test salary level, with its more rigorous duties requirements, less effective in differentiating between exempt and nonexempt employees.

The Department has considered returning to the two-test system as a way to define and delimit the EAP exemption without incurring the precision-related challenges inherent in a one-test system. However, the Department believes that a one-test system, with a single duties test, benefits both employers and employees in terms of the increased efficiency and simplicity in application. As the Department explained in 2004, a two-test system, with the more rigorous long duties test determining exemption status for many employees, would make exemption status determinations more complex and less efficient than retaining a single-test system with the existing duties test.<sup>158</sup> The Department also continues to be mindful of the post-1991 regulatory landscape, which remains highly relevant given that the two-test system effectively became a one-test system in 1991 when the Federal minimum wage equaled or surpassed the long test salary levels.<sup>159</sup>

The Department has also considered whether to propose changing the standard duties test in this rulemaking. A test requiring closer scrutiny of employee duties would be consistent with the statutory text, and a credible way to define the exemption.<sup>160</sup> Indeed, a more rigorous duties test, which limited the amount of nonexempt work—the long duties test—was traditionally the core of the EAP exemption in the two-test system. Experience under the two-test system shows that a more rigorous duties test helps to ensure that exempt employees are in fact performing EAP duties and

<sup>158</sup> See 69 FR 22126–27; see also 81 FR 32444–45 (discussing widespread employer and employee stakeholder opposition to reinstating a two-test system).

<sup>159</sup> 84 FR 51243.

<sup>160</sup> See 81 FR 32446 (“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.”); see also Stein Report at 17 (noting that “it would be inconsistent with the purposes of the [FLSA]” to exempt employees like working foremen). In the 2004 rule, the Department explained that eliminating the salary level test entirely would require significant changes to the duties test. See 69 FR 22172.

<sup>157</sup> See 5 FR 4077.

are therefore employed in a bona fide EAP capacity.<sup>161</sup> In this respect, the duties test allows for finer calibration than the salary level test when determining who is employed in a bona fide EAP capacity, with a rigorous duties test that limits the amount of nonexempt work that can be performed ensuring that employees are actually performing EAP work and not simply performing nonexempt work without receiving overtime compensation. Were the Department to lessen the salary level test's role by adopting a more rigorous duties test, the number of employees who are nonexempt based on their salary alone would decrease, helping alleviate concerns about the salary level "supplanting an analysis of an employee's job duties" in too many instances.<sup>162</sup> The Department could, for instance, return to a duties test that explicitly limited the amount of nonexempt work that could be performed. As discussed above, a limitation on nonexempt work was an integral part of the long duties test that was, for a long time, a critical component of the test for EAP exemption.

The Department has ultimately decided, however, not to propose any changes to the duties test, consistent with its decisions in the 2016 and 2019 rules. This decision was also informed by the Department's experience when it established the single-test system in 2004. In that rulemaking, the Department initially considered substantive changes to the duties test,<sup>163</sup> but ultimately declined to go through with most of the proposed changes, stating that the final standard duties test was substantially the same as the short duties test.<sup>164</sup> The Department also considered changing the duties test in both the 2016 and 2019 rulemakings,

but ultimately chose not to propose any such changes.<sup>165</sup>

At this time, the Department favors keeping the current duties test and concludes that, paired with an appropriate salary level requirement, the test can appropriately distinguish bona fide EAP employees from nonexempt workers. While comments received in previous rulemakings and during listening sessions show that the standard duties test is not universally popular, it is well known to employers, employees, and the courts, making it easier and more efficient for employers to implement and for workers to understand. Substantive changes to the duties test are a possible way to revise the regulatory test but they would take more time for employers and employees to adjust to than an increase in the salary level, requiring employers to reassess their current exemption determinations.

#### i. Fully Restoring the Salary Level's Screening Function

To determine the appropriate salary level, the Department first considers whether the present methodology adequately performs the historical screening function of the long test salary level and next, the extent to which the salary level must be increased above the long test salary level to account for the switch to a one-test system in 2004.

The Department first focused on the salary level's historic function of screening obviously nonexempt employees from the exemption, a "principle [that] has been at the heart of the Department's interpretation of the EAP exemption for over 75 years."<sup>166</sup> Under the two-test system, the lower long test salary level provided "a ready method of screening out the obviously nonexempt employees, making an analysis of duties in such cases unnecessary."<sup>167</sup> When the Department updated the long test in 1958, it reaffirmed the long test salary's function as a screening tool.<sup>168</sup>

When the Department moved to a one-test system, the standard salary test had to perform the initial screening function that the long test salary level performed in the two-test system. In the 2004 rule, the Department reaffirmed its historical statements emphasizing the salary level's critical screening function.<sup>169</sup> Most significantly, the Department used the long test

methodology to validate its new salary level of \$455 per week. Even though the 2004 rule made certain changes from that methodology (most significantly, setting the salary level equivalent to the "lowest 20% of *all* salaried employees" instead of the "lowest 10% of *exempt* salaried employees"), the Department stressed that both "approaches are capable of reaching exactly the same endpoint" and demonstrated that the new method and the long test method produced equivalent salary levels at the time.<sup>170</sup> By setting a salary level equivalent to the long test level, the Department ensured that employees earning at levels whereby they were entitled to overtime compensation under the two-test system because they earned below the long test salary level remained screened from the exemption by the new standard salary test, regardless of whether they met the less rigorous standard duties test. In the 2004 rule, the Department rejected requests from commenters who supported a salary level that was \$30 to \$95 lower than the level the Department ultimately adopted,<sup>171</sup> thus maintaining the historic screening function by declining to set a salary level lower than the long test level.

In its 2019 rule, the Department reemphasized the salary level's screening function.<sup>172</sup> The Department distinguished the 2016 rule, which the Department explained was invalidated because it "'untethered the salary level test from its historical justification' of '[s]etting a dividing line between nonexempt and potentially exempt employees' by screening out only those employees who, based on their compensation level, are unlikely to be bona fide executive, administrative, or professional employees."<sup>173</sup> In contrast, the Department explained, reapplying the 2004 methodology to current data was likely to pass muster because the district court that invalidated the 2016 rule "endorsed the Department's historical approach to setting the salary level" and "explained that setting 'the minimum salary level as a floor to screen[ ] out the obviously nonexempt

<sup>161</sup> The importance of a rigorous duties test was illustrated by the Department's *Burger King* litigation in the early 1980s, 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. 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 not exempt and therefore entitled to overtime compensation because they did not meet the more rigorous long duties test.

<sup>162</sup> 275 F. Supp. 3d at 806.

<sup>163</sup> See 68 FR 15564–68.

<sup>164</sup> 69 FR 22126, 22192–94.

<sup>165</sup> 84 FR 10904; 82 FR 34618 (July 26, 2017); 80 FR 38543 (July 6, 2015).

<sup>166</sup> See 84 FR 51241.

<sup>167</sup> Weiss Report at 8.

<sup>168</sup> Kantor Report at 2–3.

<sup>169</sup> 69 FR 22165.

<sup>170</sup> See *id.* at 22167–71 (showing that for all full-time salaried employees, \$455 in weekly earnings corresponded to just over the 20th percentile in the South and the 20th percentile in retail, and that for employees performing EAP duties, \$455 in weekly earnings corresponded to just over the 8th percentile in the South and the 10th percentile in retail).

<sup>171</sup> See *id.* at 22164.

<sup>172</sup> 84 FR 51237 (internal quotation marks omitted).

<sup>173</sup> *Id.* at 51231 (quoting 84 FR 10901).

employees' is 'consistent with Congress's intent.'"<sup>174</sup>

The Department's position remains that a core function of the salary level test is to screen from the EAP exemption employees who, based on their low pay, should receive the FLSA's overtime protections. For decades under the Department's two-test system, the long test salary level performed this screening function. In the 2004 rule, the Department used a different approach—setting a single salary level test that was equivalent to, and thus set the same line of demarcation as, the long test salary level (although it combined that salary level with a duties test that was equivalent to the less rigorous short duties test). The Department deviated from this approach in 2019, setting a salary level that was \$40 per week below the level produced using the long test methodology.<sup>175</sup> In doing so, the Department for the first time expanded the exemption to include employees who were paid below the long test salary level. As an initial step, the proposed salary level methodology must fully restore the salary level's screening function by ensuring that employees who were nonexempt because they earned less than the long test salary are also nonexempt under the standard test. Simply restoring the historic screening function would require a standard salary level amount that is at least equal to the long test level (which is \$925 per week using current data). Such a salary level would not, however, account for the shift to a one-test system in 2004.

Increasing the standard salary level to at least the long test level would ensure that the salary level, at a minimum, performs the historical screening function it would have performed in a two-test system. From 1938 to 2019, all salaried white-collar employees paid below the long test salary level were entitled to the FLSA's protections, regardless of the duties they performed. This was true from 1938 to 1949 under the salary level test that became the long test,<sup>176</sup> from 1949 to 2004 under the long test, and from 2004 to 2019 under the standard salary level test that was set equivalent to the long test level. Setting the salary level below the long test level as was done in the 2019 rule—because the 2004 methodology no longer matched the long test salary level based on contemporaneous data—departed from this history by enlarging the exemption to newly include

employees who earned less than the long test salary level.

In the 2019 rule, the Department expressly declined to use the long test methodology to set the salary level test.<sup>177</sup> Because the Department is not using the long test methodology to set the salary level in this proposal, but is instead using it to inform its selection of a new salary level methodology, the concerns expressed by the Department in 2019 do not apply. The Department was in part worried that the long test method is "complex to model and thus is less accessible and transparent."<sup>178</sup> This concern does not arise here because the Department's proposed methodology uses a publicly available data set of all full-time nonhourly workers in the South to set the salary level, as opposed to the long test methodology data set (which only included exempt workers).<sup>179</sup> In 2019, the Department also expressed concern that the long test methodology presents a "circularity problem" because this approach "would determine the population of exempt salaried employees, while being determined by the make-up of that population."<sup>180</sup> This concern is similarly not implicated here because, consistent with its practice since 2004, the Department is setting the salary level using a data set of all full-time nonhourly workers, not just exempt workers.

#### ii. Selecting the Proposed Salary Level Methodology

Section 13(a)(1)'s broad grant of statutory authority for the Department to define and delimit the EAP exemption provides the Department a degree of latitude in determining an appropriate salary level for identifying individuals who are employed in a bona fide EAP capacity. The Department believes that the long and short test salary levels provide useful parameters informed by its historical rulemaking for determining how to update the salary level test in this rulemaking. As previously discussed, the long and short test salary levels have served as the foundation for nearly all of the Department's prior

rulemakings, either directly under the two-test system, or indirectly as a means of evaluating the Department's salary level methodology under a one-test system. Based on 2022 data, applying the long test methodology produces a salary level of \$925 per week (\$48,100 per year) and the short test methodology produces a salary level of \$1,378 per week (\$71,656 per year).

The long and short test salary levels reflected longstanding understandings of how an individual's salary level informs the question of whether an individual is employed in a bona fide EAP capacity. As noted above, the long test salary level helped distinguish employees who were not employed in a bona fide EAP capacity and the Department found that employees who were screened from exemption by the long test salary level generally did not meet the other requirements for exemption.<sup>181</sup> The justification for the short test, on the other hand, was that employees who met the higher salary level were more likely to meet all the requirements of the exemption (including the long test's 20 percent limit on nonexempt work).<sup>182</sup> Moreover, because the Department's rulemakings since 2004 have, to varying extents, used the long and short tests as guideposts for setting the salary level in a one-test system, maintaining the same orientation in this rulemaking would enable the Department to calibrate its methodology to better define and delimit bona fide EAP employees, and evaluate how it impacts employees who historically have been entitled to overtime compensation and the ability of employers to use the exemption to exclude from overtime protection employees who have historically been exempt.

In its almost 20 years of experience with the one-test system, the Department has never set a standard salary level that falls between the long test salary level and the short test range. As explained more fully above, the Department set the standard salary at (or below) the long test salary level in the 2004 and 2019 rules and set it at the low end of the historic range of short test salary levels in the 2016 rule. Setting the salary level at either the long test salary level or equivalent to a short test salary level in a one-test system with the standard duties test, however, results in either denying overtime protection to lower-paid employees who are performing large amounts of nonexempt work, and thus, were exempt under the Department's historical view of the EAP

<sup>174</sup> *Id.* at 51241 (quoting 275 F. Supp.3d at 806).

<sup>175</sup> *Id.* at 51244.

<sup>176</sup> During this period the Department used a one-test system that paired a lower salary level with a more rigorous duties test. *See, e.g.*, 5 FR 4077.

<sup>177</sup> 84 FR 51244, 51260.

<sup>178</sup> *Id.* at 51244.

<sup>179</sup> For the same reason, the Department's approach does not implicate concerns that applying the long test method "requires 'uncertain assumptions'" to compile a dataset set that represents exempt EAP employees. *Id.* (quoting 69 FR 22167). Moreover, while it is true that the Department must apply its probability codes to determine the group of salaried employees who pass the duties test, the Department has consistently applied these codes since the 2004 rule. *See generally* section VII.B.5 (discussing probability codes).

<sup>180</sup> 84 FR 51244 (quoting 69 FR 22167).

<sup>181</sup> *See* Kantor Report at 2–3.

<sup>182</sup> Weiss Report at 22–23.



exemption, or in raising concerns that the salary level is determining the status of too many employees. An appropriately calibrated salary level between the long and short test salary levels would better define and delimit which employees are employed in a bona fide EAP capacity, and thus better fulfill the Department's duty to define and delimit the EAP exemption.

Traditionally, the Department considered employees earning between the long and short test salary levels to be employed in a bona fide EAP capacity only if they were not performing substantial amounts of nonexempt work. With the adoption of a duties test based on the less rigorous short duties test, the shift to a single-test system eliminated the inquiry into the amount of nonexempt work employees performed. Following this shift, the Department has taken two approaches to setting the salary level to pair with the standard duties test. The approach taken in the 2004 rule permitted the exemption of all employees earning above the long test salary level who met the standard duties test—including many employees who performed substantial amounts of nonexempt work and were protected by the long duties test. The approach taken in the 2016 rule was challenged and criticized as making nonexempt employees earning between the long test salary level and the low end of the short test salary range—including some employees who may have performed very little nonexempt work and would have been exempt under the long test. Inevitably, any attempt to pair a single salary level with the current duties test will result in some employees who perform substantial amounts of nonexempt work being exempt, and some employees who perform almost exclusively exempt work being nonexempt.<sup>183</sup> But such a result is inherent in setting any salary level in a one test system—some employees will have EAP status turn on salary level. The proposed salary level would better identify which employees are employed in a bona fide EAP capacity—particularly by restoring overtime eligibility for individuals who perform substantial amounts of nonexempt work and historically would have been protected by the long duties test—while at the same time addressing potential concerns that the salary level test should not be determinative of

exemption status for too many individuals.<sup>184</sup>

In setting the salary level, the Department continues to believe that it is important to use a methodology that is transparent and easily understood. As in its prior rulemakings, the Department proposes to set the salary level using a lower-salary regional data set (as opposed to nationwide data) to accommodate businesses for which salaries generally are lower due to geographic or industry-specific reasons.<sup>185</sup> Specifically, the Department proposes to set the salary level using the data set of full-time nonhourly<sup>186</sup> workers in the lowest-wage Census Region (the South). Like the Department's 2004, 2016, and 2019 rules, this approach would promote transparency because BLS routinely compiles this data. It would also promote regulatory simplification because the data set is not limited to exempt EAP employees and thus does not require the Department to model which employees pass the duties test.<sup>187</sup>

For similar reasons, the Department is not proposing to add nationwide earnings data from specific industries (such as retail) to the CPS earnings data from the lowest-wage Census Region. The Department's 2019 rule included such data to faithfully replicate the 2004 methodology which considered earnings of full-time nonhourly workers in the lowest-wage Census Region and the retail industry nationally.<sup>188</sup> The Department's approach nonetheless would yield a salary level that would be appropriate in low-wage industries because using earnings data from the lowest-wage Census Region would capture differences across regional labor markets without attempting to adjust to specific industry conditions.<sup>189</sup>

Based on 2022 data, applying the long test methodology produces a salary level of \$925 per week (\$48,100 per year),

<sup>184</sup> The Department has repeatedly recognized that increasing salary level tends to correlate with the performance of bona fide EAP duties. See section IV.A.2 (discussing role of long test and short test salary levels); section IV.C (discussing the role of the HCE total annual compensation threshold). Thus, increasing overtime protection specifically for workers earning at the lower end of the range between the long test salary level and short test salary level—but not those earning at the higher end of that range—is an especially appropriate approach to balancing these concerns.

<sup>185</sup> See 84 FR 51238; 81 FR 32404.

<sup>186</sup> Consistent with recent rulemakings, in determining earnings percentiles the Department looked at nonhourly earnings for full-time workers from the CPS MORG data collected by BLS.

<sup>187</sup> As discussed in the economic analysis, see section VII.B.5, this modeling is done using the Department's probability codes. See 84 FR 51244; 69 FR 22167.

<sup>188</sup> See 84 FR 51244 (citing 69 FR 22167).

<sup>189</sup> See 81 FR 32410.

which equates to between the 26th and 27th percentiles of weekly earnings of full-time, nonhourly workers in the lowest-wage Census Region (the South).<sup>190</sup> This figure provides what the Department believes should be the lowest boundary of a salary level methodology because it would at least restore the historical screening function that had operated under a two-test system.

The Department is not proposing to set the salary level equivalent to the long test level in part because doing so would perpetuate the problem that has become evident under the 2004 and 2019 rules: that setting the single salary level no higher than the long test level enables employers to exempt employees who were traditionally not considered bona fide EAP employees because they performed substantial amounts of nonexempt work and did not meet the long duties test under the two-test system. Like these earlier rules, this approach would impact white-collar employees earning between the long and short test salary levels who perform substantial amounts of nonexempt work—and thus were entitled to overtime protection under the two-test system—but meet the less rigorous standard duties test.

As discussed above, the Department could address this issue by changing the duties test to reinstate the long test's limit on nonexempt work. Doing so would restore the relationship between the salary level and duties tests that existed under the two-test system whereby the Department paired a lower salary level with a more rigorous duties test. Paired with a long test-equivalent salary level, a stronger duties test would ensure that lower-paid employees who perform large amounts of nonexempt work receive overtime protection, while permitting employers to continue using the exemption for lower-paid employees performing EAP duties. However, for the reasons previously discussed, the Department proposes to restore the relationship between the salary level and duties test by keeping the duties test unchanged at this time and instead increasing the salary level moderately above the long test level. This increase in the salary level is necessary for the Department to effectively fulfill its role of defining and delimiting the EAP exemption because, without it, the employees who were not considered bona fide EAPs historically—those earnings between the long and short test

<sup>190</sup> The 26th percentile in this data set corresponds to a salary level of \$918 per week and the 27th percentile corresponds to a salary level of \$933 per week.

<sup>183</sup> See Stein Report at 6 (“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 benefits of the act.”).

salary levels who did not meet the historical long duties test—would remain exempt from overtime. In other words, the Department's proposed salary level methodology will better help limit the exemption of lower-paid employees who historically were not considered bona fide EAP employees because they perform substantial amounts of nonexempt work, but who are not receiving overtime protection under the one-test system.

Although the “regulations cannot have the precision of a mathematical formula[.]”<sup>191</sup> with only two variables to adjust in a one-test system, and with the Department deciding to leave one of those variables (the duties test) unchanged in this rulemaking, the Department wanted to look more precisely at methods for updating the salary level test. The Department has therefore looked to employee earnings ventiles rather than only deciles as it has historically done.<sup>192</sup> The earnings ventiles between the long test salary level (approximately the 26th or 27th percentile) and short test salary level (approximately the 53rd percentile) are the 30th, 35th, 40th, 45th, and 50th percentiles of weekly earnings of full-time salaried workers in the lowest-wage Census Region. The Department examined these earnings ventiles with the goal of more effectively defining and delimiting the exemption while maintaining the one-test system.

Setting the salary level at the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region would reduce the impact of a one-test system on lower-paid white-collar employees who perform significant amounts of nonexempt work. This percentile is midway between the 30th and 50th percentiles and would produce a salary level (\$1,145 per week) that is roughly the midpoint between the long and short test salary levels. Of the approximately 10.3 million salaried white-collar employees who earn between the long and short test salary levels, approximately 47 percent earn between the long test salary level and

\$1,145 and would receive overtime protection by virtue of their salary, while approximately 53 percent earn between \$1,145 and the short test salary level and would have their exemption status turn on whether they meet the duties test.

The Department remains concerned, however, that courts could find this approach makes the salary level test determinative of overtime eligibility for too many employees (*i.e.*, 47 percent of those earning between the long and short test levels). Setting the salary level equal to the 45th or 50th percentile of weekly earnings would further amplify this concern. In contrast, setting the salary level based on a lower percentile of earnings will (compared to such higher levels) increase the number of employees for whom duties is determinative of exemption status, and in turn the ability of employers to use the exemption for more lower-paid employees who meet the EAP duties requirements. This outcome is consistent with the important role of the duties test in identifying bona fide EAP employees and recognizes that the 2016 rule (which set the salary level equal to the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region) was held invalid by the U.S. District Court for the Eastern District of Texas for making too many employees eligible for overtime based on salary alone.<sup>193</sup>

The Department is also responding to concerns that setting the salary level equal to the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region would foreclose employers from exempting any white-collar employees who earn less than \$1,145 per week and perform EAP duties, including those who were exempt under the long test and remained exempt when the Department established the one-test system in 2004 and set the salary level equivalent to the long test level.<sup>194</sup> Litigants challenging the 2016 rule also emphasized this consequence of setting a salary level above the long test in a one-test system, and those arguments have contributed to the Department more fully attempting to account for the impact of the shift from a two-test to a one-test system on the scope of the exemption. Although some stakeholders have urged the Department to follow the methodology from the 2016 rule or set an even higher threshold, the Department has chosen a salary level that is appreciably lower than the midpoint between the short and long test salary levels—an approach

that it believes is an appropriate method for identifying bona fide EAP employees. This approach would also reasonably balance the goal of ensuring that employees earning above the long test salary level but performing substantial amounts of nonexempt work are not exempt with the goal of enabling employers to use the exemption for employees who do not perform substantial amounts of nonexempt work.

The Department also examined the 30th and 35th percentiles of weekly earnings of full-time salaried workers in the lowest-wage Census Region. The Department did not consider setting the salary level at the 25th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (\$901 per week or \$46,852 per year) because it is lower than the long test salary level (\$925 per week or \$48,100 per year, which is approximately the 26th or 27th percentile). Setting the standard salary level at the 30th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region would result in a salary level of \$975 per week (\$50,700 per year). This salary level is roughly the midpoint between the 2004 methodology (the 20th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census region and in retail nationally, currently \$822 per week or \$42,744 per year), and the 2016 methodology (the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region, currently \$1,145 per week or \$59,540 per year). While setting the salary level equal to the 30th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region would produce a salary level that is above the long test salary level, it is very close to the long test salary level, and the Department is concerned it would not sufficiently address the problem inherent in the 2004 methodology of including in the exemption employees who perform significant amounts of nonexempt work, including those earning salaries closer to the long test salary level, and historically were not considered bona fide EAP employees under the two-test system. Additionally, only 11 percent of white-collar employees who earn between the long and short test salary levels earn below the 30th percentile. As noted above, the Department believes that the standard salary must fulfill the historical screening function of the long test salary level and account for the shift to a one-test system, and the

<sup>191</sup> Weiss Report at 9.

<sup>192</sup> Historically, the Department set the long test salary level to exclude from exemption approximately the lowest-paid 10 percent of exempt salaried employees in the lowest-wage regions and industries. In 2004 and 2019, the Department set the standard salary level test equivalent to the 20th percentile of weekly earnings of full-time salaried workers in the South Census Region and in the retail industry nationally. In the 2016 rule, the Department set the salary level equal to the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (the South). See 84 FR 51236–37 (describing prior methodologies).

<sup>193</sup> See *Nevada*, 275 F.Supp.3d at 806–07.

<sup>194</sup> See 84 FR 51242.

Department is concerned that this salary level would not fulfill both objectives.

After careful consideration, the Department concludes that setting the salary level equal to the 35th percentile—which produces a salary level of \$1,059 per week—will effectively define and delimit the scope of the EAP exemption. Consistent with the Department’s responsibility to “not only . . . determin[e] which employees are entitled to the exemption, but also [to] draw[] the line beyond which the exemption is not applicable[.]”<sup>195</sup> the Department’s proposed standard salary level will, in combination with the standard duties test, effectively calibrate the scope of the exemption to ensure the exemption of bona fide EAP employees, and do so in a way that distributes across the population of white-collar employees earning between the long and short test salary levels the impact of the shift to a one-test system.

The Department stated in the 2019 rule that the primary and modest purpose of the salary level is to identify potentially exempt employees by screening out obviously nonexempt employees.<sup>196</sup> While this initial screening function is the primary effect of the salary level, as noted above, each update to the salary level has also had a secondary effect: it defines the group of white-collar employees for whom the duties test is determinative of their exemption status. Setting the salary level equal to the 35th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region produces a salary level high enough above the long test level to ensure overtime protection for some lower-paid employees who were traditionally entitled to overtime compensation under the two-test system by virtue of their performing large amounts of nonexempt work. The salary level is also low enough, as compared with higher salary levels, to significantly shrink the group of employees performing EAP duties who are excluded from the exemption by virtue of their salary alone. Of the 10.3 million salaried white-collar employees earning between the equivalent of the long and short test salary levels, approximately 31 percent earn between \$925 (the equivalent of the long test salary level) and \$1,059 (the proposed salary level) and would receive overtime protection by virtue of their salary, while approximately 69 percent earn between \$1,059 and \$1,378 (the equivalent of the short test salary level) and would have their exemption status

turn on whether they meet the duties test.

Comparing the impact of the new salary level on white-collar employees earning between the long and short test salary levels and their employers reinforces the reasonableness of the Department’s proposed salary level. Whereas the 2004 and 2019 rules permitted the exemption of such employees even if they performed significant amounts of nonexempt work, and the 2016 rule prevented employers from using the exemption for such employees earnings below the short test salary range even if they performed EAP duties, the proposed methodology falls between these two methodologies and therefore reasonably balances the effect of the switch to a one-test system in a way that better differentiates between those who are and are not employed in a bona fide EAP capacity. Even though the Department’s decision to select a salary level below the midpoint between the long and short tests means that the effect of the salary level on these employees and employers is not equal, a higher salary level could disrupt reliance interests of employers who (due in part to the Department’s failure to update the salary level tests between 1975 and 2004), have been able to use a lower salary level and more lenient duties test to determine exemption status since 1991. However, a significantly lower salary level akin to the long test salary level would avoid disrupting such reliance interests only by continuing to place the burden of the move to a one-test system entirely on employees who historically were entitled to the FLSA’s overtime protections because they perform substantial amounts of nonexempt work. The Department believes that employer reliance interests should inform where the salary level is set between the long and short test levels, and that its approach strikes a workable equilibrium that reasonably balances, between employees’ right to receive overtime compensation and employers’ ability to use the exemption, the impact of a one-test system.

Such reasonable balancing is fully in line with the Department’s authority under the FLSA to “mak[e] certain by specific definition and delimitation” the “general phrases” “bona fide executive, administrative, and professional employee.”<sup>197</sup> This grant of authority confers discretion upon the Department to reasonably determine the boundaries of these general categories; any such line-drawing, as courts have recognized, will “necessarily” leave out some

employees “who might fall within” these categories.<sup>198</sup>

The Department recognizes that it stated in its 2016 rule that the current duties test could not be effectively paired with a salary level below the short test salary range, and for this reason expressly rejected setting the salary level at the 35th percentile of weekly earnings of full-time salaried workers in the South.<sup>199</sup> But that rule, which would have prevented employers from using the EAP exemption for some employees who were considered exempt under the prior two-test system, was challenged in court, and a return to it would result in significant legal uncertainty for both workers and the regulated community. In the 2019 rule, the Department expressly rejected setting the salary level equal to the long test or higher.<sup>200</sup> However, as noted above, the Department did not fully address in that rule the implications of the switch from a two-test to a single-test system. Having now grappled with those implications, particularly in light of the Department’s experience in the litigation challenging its 2016 rule, the Department has concluded that not only can it pair the current duties test with a salary between the long and short test salary levels, but that doing so appropriately recalibrates the salary level in a one-test system to ensure that it effectively identifies bona fide EAP employees.

The Department is not proposing any changes to how bonuses are counted toward the salary level requirement. Consistent with the current regulations, if the salary level is finalized as proposed, employers could satisfy up to 10 percent of the salary level (\$105.90 per week under this proposed rule) through the payment of nondiscretionary bonuses and incentive pay (including commissions) paid annually or more frequently.<sup>201</sup>

#### 4. Assessing the Impact of the Proposed Salary Level

As stated above, the Department believes that the salary level test should fulfill a “useful, but limited, role” in defining and delimiting the EAP exemption.<sup>202</sup> In proposing to update the standard salary level, the Department seeks to: preserve the primary role of an analysis of employee duties in determining EAP exemption status, fully restore the initial screening function of the salary level, and more

<sup>195</sup> Stein Report at 2.

<sup>196</sup> 84 FR 51238.

<sup>197</sup> *Walling*, 140 F.2d at 831.

<sup>198</sup> *Id.*

<sup>199</sup> 81 FR 32410.

<sup>200</sup> See 84 FR 51244.

<sup>201</sup> § 541.602(a)(3).

<sup>202</sup> 84 FR 51238.

effectively identify in a one-test system who is employed in a bona fide EAP capacity in a manner that reasonably distributes among employees earning between the long and short test salary levels and their employers the impact of the Department's move from a two-test to a one-test system. A closer look at the expected impact of the proposed salary level shows that it meets these objectives.

The Department intentionally chose a salary level methodology that, if finalized, would ensure that the EAP exemption status of the great majority of white-collar employees would continue to depend on their duties. To evaluate whether the proposed methodology meets this objective, the Department first considered its effect on the population of all salaried white-collar employees—the universe of employees who could potentially be impacted by a change in the standard salary level. This analysis confirmed that the number of white-collar employees who would be

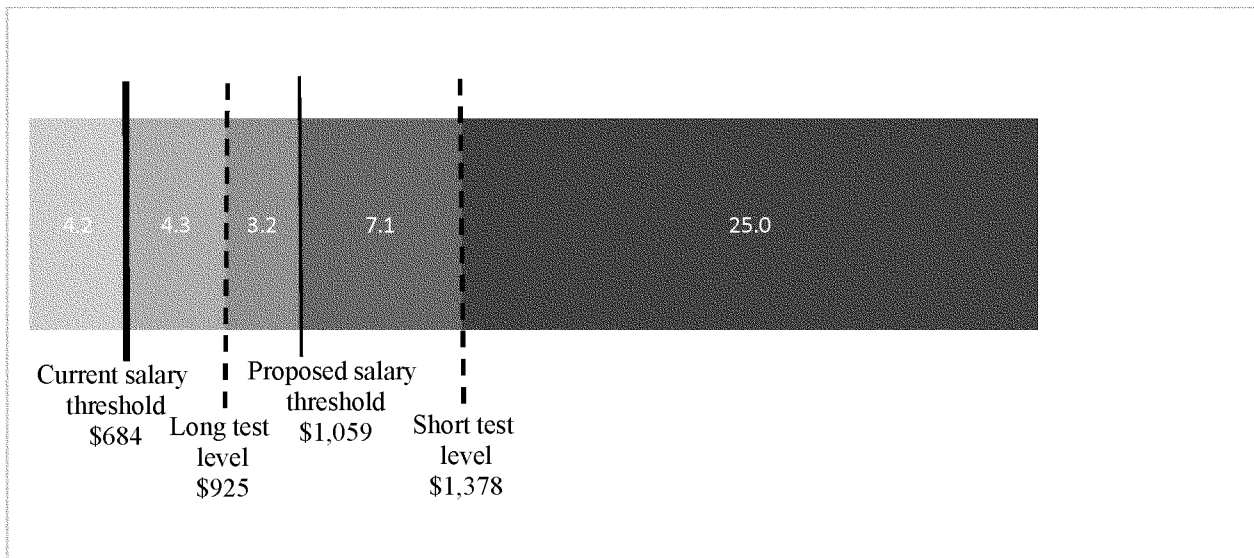
excluded from the EAP exemption as a result of the Department's proposed standard salary level is greatly exceeded by the far-larger population of white-collar employees for whom duties would continue to determine their exemption status.

As illustrated in Figure A below, of the approximately 43.8 million salaried white-collar employees in the United States subject to the FLSA,<sup>203</sup> about 11.7 million earn below the Department's proposed standard salary level of \$1,059 per week and about 32.1 million earn above the Department's proposed salary level.<sup>204</sup> Thus, approximately 27 percent of salaried white-collar employees (most of whom, as discussed below, do not perform EAP duties) earn below the proposed salary level, whereas approximately 73 percent of salaried white-collar employees earn above the salary level and would have their exemption status turn on their job duties.<sup>205</sup>

Scrutinizing these figures more closely reinforces the continued

importance of the duties test under the Department's proposal. Of the approximately 11.7 million salaried white-collar employees who earn below the Department's proposed standard salary level of \$1,059 per week, about 8.5 million earn below the long test salary level of \$925 per week. As explained above, with the exception of the 2019 rule, when the Department set the salary level slightly lower, the Department has always set salary levels that screened from exemption employees earning below the long test salary level. The number of salaried white-collar employees for whom salary would be determinative of their nonexempt status and who earn at least the long test salary level—3.2 million—is nearly ten times smaller than the number of salaried white-collar employees for whom job duties would continue to be determinative of their exemption status because they earn at least the proposed standard salary level—32.1 million.<sup>206</sup>

Figure A: Distribution of Salaried White-Collar Employees by Weekly Earnings



Note: Numbers are in millions of employees.

Note: The long test level is the salary threshold that, based on current data, would exclude the lowest-paid 10 percent of exempt EAP employees in low-wage industries and areas. The short test level is equal to 149 percent of the long test level. The 149 percent ratio is the simple average of the fifteen historical ratios of the short test salary level to the long test salary level.

<sup>203</sup> Excluded from this number are workers in named occupations and those exempt under another non-EAP overtime exemption. The exemption status of these groups will not be impacted by a change in the standard salary level.

<sup>204</sup> As discussed further below, *see, e.g.*, section VII.B.5, the Department used data representing compensation paid to nonhourly white-collar

workers to estimate compensation paid to salaried white-collar employees.

<sup>205</sup> Even this estimate is conservative, as it excludes 8.1 million white-collar employees employed as teachers, attorneys, and physicians, for whom there is no salary level requirement under the part 541 regulations and whose exemption status is therefore always determined by their duties. If these employees in "named occupations"

are included, the percentage of white-collar employees for whom exemption status would depend on duties, rather than salary, increases to 77 percent. *See* §§ 541.303–304.

<sup>206</sup> As noted above, *see supra* note 205, these figures do not include the additional 8.1 million white-collar employees in occupations for which there is no salary level requirement and so duties is always determinative of exemption status.

In analyzing how the Department's proposed salary level would impact all salaried white-collar employees, the Department also considered the extent to which salaried white-collar employees across the income distribution perform EAP duties. As noted above, the salary level has historically served as "a helpful indicator of the capacity in which an employee is employed, especially among lower-paid employees;"<sup>207</sup> however, it should not eclipse the duties test.<sup>208</sup> The Department's proposed standard salary level meets this standard because, according to probability codes the Department has

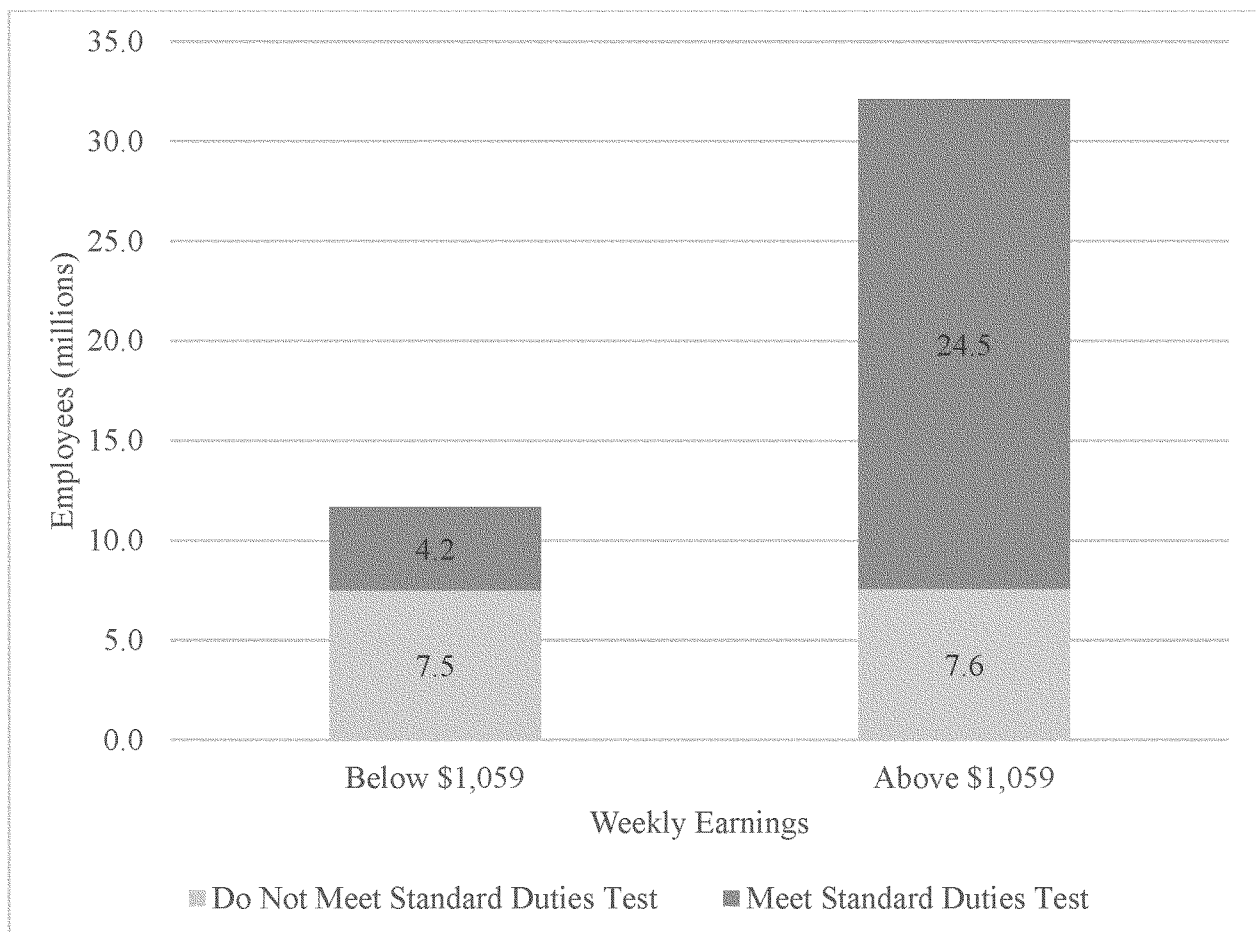
used in all of its recent part 541 rules,<sup>209</sup> most salaried white-collar employees paid less than the proposed standard salary level do not meet the duties test, whereas a substantial majority of salaried white-collar employees earning above the proposed standard salary level meet the duties test.

As illustrated in Figure B, of the 11.7 million salaried white-collar employees who earn less than the proposed standard salary level of \$1,059 per week, the Department estimates that only 36 percent—about 4.2 million employees—meet the standard duties test. In contrast, of the 32.1 million salaried white-collar employees who earn at least \$1,059 per week, 76

percent—about 24.5 million employees—meet the standard duties test.<sup>210</sup> The number of salaried white-collar workers who meet the standard duties test and earn below the proposed standard salary level is thus nearly six times smaller than the number of salaried white-collar workers who meet the standard duties test and earn at least the proposed standard salary amount. And 85 percent of all salaried white-collar workers who meet the standard duties test—24.5 million out of a total of approximately 28.7 million—earn at least the Department's proposed standard salary level.<sup>211</sup>

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Figure B: Salaried White-Collar Employees Earnings Above and Below the Proposed Standard Salary Level Who Meet or Do Not Meet the Standard Duties Test



The Department next evaluated its proposed salary level methodology by

looking at salaried white-collar employees who earn between the long

and short test salary levels. As discussed in section IV.A.3.ii, the long

<sup>207</sup> 84 FR 51239 (quoting 84 FR 10907).

<sup>208</sup> See *id.* at 51245.

<sup>209</sup> See section VII.B.5.

<sup>210</sup> As noted above, see *supra* note 205, these figures exclude salaried white-collar workers who are not subject to the part 541 salary criteria.

<sup>211</sup> Note that these numbers refer only to salaried white-collar employees at all salary levels who meet

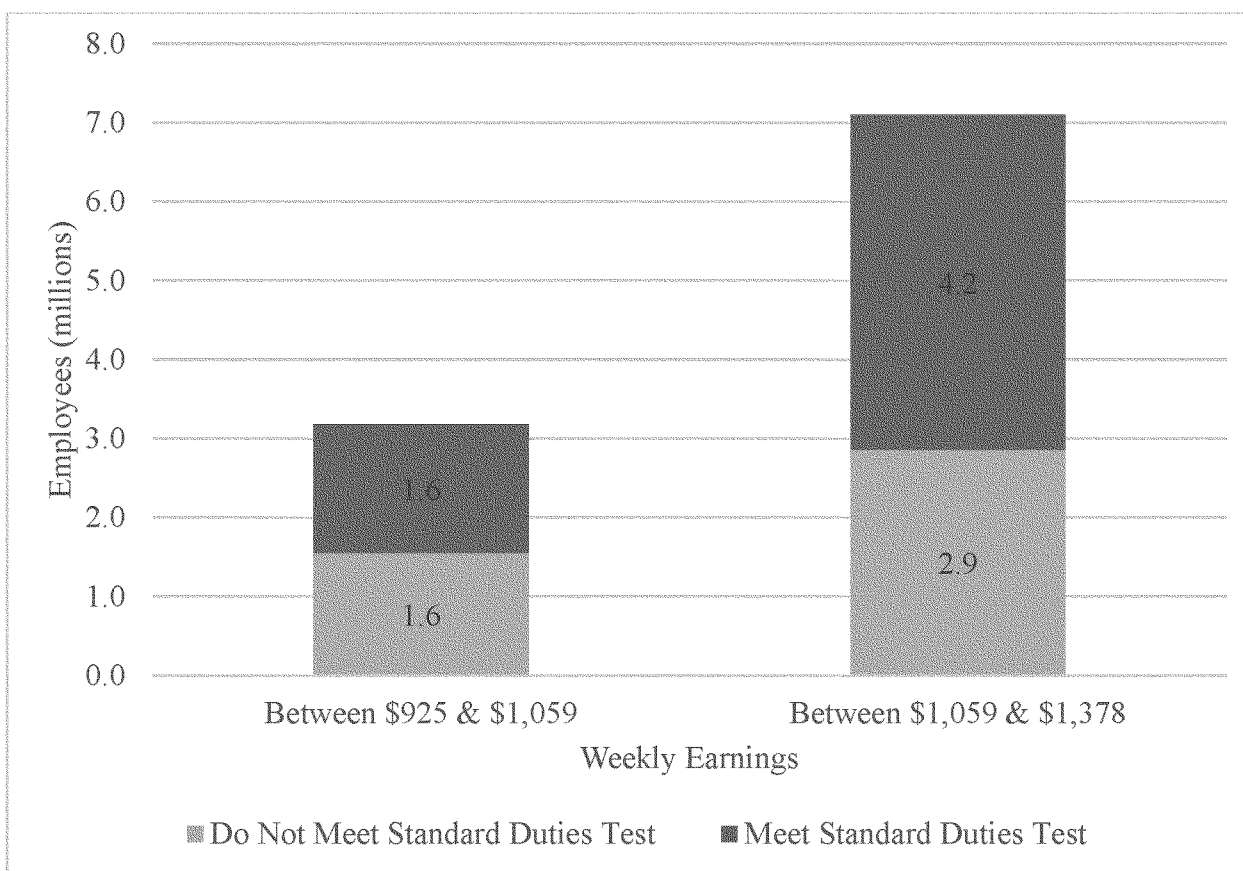
the standard duties test, including employees who are nonexempt because they earn below the current standard salary level.

and short test salary levels provide appropriate parameters for determining how to update the salary level test. Under the Department's proposal, duties would continue to be determinative of exemption status for a significant majority of white-collar employees earning between these thresholds.

As illustrated in Figure C, of the approximately 10.3 million salaried white-collar employees who earn between the long test salary level of \$925 per week and the short test salary level of \$1,378 per week, about 31 percent (3.2 million) earn below the Department's proposed standard salary

level, and about 69 percent (7.1 million) earn at or above the Department's proposed standard salary level. Moreover, of the 3.2 million employees earning between the long test and the proposed standard salary level, approximately half do not meet the standard duties test.<sup>212</sup>

Figure C: Salaried White-Collar Employees Between Long and Short Test Salary Levels Who Meet or Do Not Meet the Standard Duties Test



#### BILLING CODE 4510-27-C

Finally, the Department also looked at the impact of the proposed salary level on currently exempt EAP employees—those salaried white-collar employees who meet the standard duties test and earn at least \$684 per week. As with every prior rulemaking to increase the part 541 salary levels, a relatively small percentage of currently exempt employees would become nonexempt if this proposal were finalized. Of the

approximately 43.8 million salaried white-collar employees in the United States, approximately 27.9 million currently qualify for the EAP exemption.<sup>213</sup> Of these 27.9 million presently-exempt employees, just 3.4 million earn at or above the current \$684 per week standard salary level but less than \$1,059 per week and would, without some intervening action by their employers, become entitled to

overtime protection as a result of the Department increasing the standard salary level to \$1,059 per week. A test for exemption that includes a salary level component will necessarily result in a number of employees who earned at or above the prior salary level and pass the duties test becoming nonexempt when the salary level is updated. This is a feature, and not a flaw, of a salary level test, and as the

<sup>212</sup> As discussed further below, about 1.6 million of the approximately 3.2 million salaried white-collar employees who earn between the long test salary threshold and the Department's proposed salary level (about 49 percent of these employees) do not meet the standard duties test. Thus, in effect, only 16 percent of salaried white-collar employees who earn between the long and short test salary

levels—1.6 million out of a total of 10.3 million—have their exemption status determined solely by the proposed standard salary level.

<sup>213</sup> Note that the 27.9 million employee figure only refers to employees who meet the standard EAP exemption and thus differs from the population of currently exempt EAP workers

identified in the economic analysis (28.4 million), which includes workers who qualify only for the HCE exemption. As noted above, this is a conservative estimate because there are also 8.1 million employees in the “named occupations” who, under the Department's regulations, are exempt based on their duties alone.

Department has consistently found since 1938, salary is an important indicator of whether an individual is employed in a bona fide EAP capacity and therefore a key element in defining the exemption.

The Department's proposed standard salary level would impact the exemption status of two distinct and important, but relatively small, groups of lower-paid EAP employees. First, the Department's proposal would restore overtime protections to 1.8 million currently exempt employees who meet the standard duties test but earn less than the equivalent of the long test salary level (\$925). As previously explained, such employees were always excluded from the EAP exemption prior to 2019, either by the long test salary level itself, or under the 2004 rule salary level, which was equivalent to the long test salary level. Fully restoring the salary level's initial screening function requires a salary level that would ensure all employees who earn below the long test level would be excluded from the exemption.

Second, the proposed standard salary level would result in overtime protections for an additional 1.6 million currently exempt employees who meet the standard duties test and earn between the long test salary level (\$925 per week) and the Department's proposed standard salary level. As explained earlier, the Department believes it is necessary to set the standard salary level above the long test level to reasonably distribute the impact of the switch from a two-test system to a one-test system. The Department's proposal would limit the number of affected employees by setting a standard salary level towards the lower end of the range between the long and short test salary levels and by using earnings data from the lowest-wage Census region (the South).

Even among the 3.4 million affected employees, the fact that a majority of these employees earn below the long test level underscores the modest role of the Department's proposed standard salary level. Beyond these 1.8 million employees earning less than the long test salary level—to whom this proposal would simply restore overtime protections that they had under every rule prior to 2019—the Department's proposed increase in the standard salary level would only affect the exemption status of 1.6 million employees. This group makes up less than six percent of all currently exempt, salaried white-collar employees and less than four percent of all salaried white-collar

employees.<sup>214</sup> That this group is so small reinforces the conclusion that the Department's proposed salary level methodology would maintain the “useful, but limited, role” of the salary level in defining and delimiting the EAP exemption.<sup>215</sup>

#### 5. Salary Level Alternatives

In determining which methodology to use to update standard salary level, the Department considered several alternatives to its proposed methodology of the 35th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region. As discussed, the Department believes that the long and short test salary levels provide appropriate boundaries for assessing potential salary levels,<sup>216</sup> though it also considered the methodology used in the 2019 rule, which set the standard salary level below the long test level.<sup>217</sup> The Department also looked at earnings ventiles for full-time salaried workers falling between the long and short test salary levels. The Department analyzed four alternative salary levels—two methodologies that would produce a higher salary level than the proposed methodology, and two that would produce a lower salary level.<sup>218</sup>

The Department first considered setting the standard salary level at the historical average short test salary level (\$1,378 per week or \$71,656 per year).<sup>219</sup> This would ensure that all employees who earn between the long and short test salary levels and perform substantial amounts of nonexempt work would be entitled to overtime compensation. However, by making exemption status for all employees who earn between the long and short test levels depend entirely on the salary paid by the employer, this approach would also prevent employers from being able to use the EAP exemption for employees earning between these salary levels who do not perform substantial amounts of nonexempt work and thus were historically exempt under the long test. For this reason, among others, the Department has chosen not to propose the salary level generated by this methodology.

<sup>214</sup> The 3.4 million employees affected by the Department's proposed standard salary level represent only 12 percent of the 27.9 million salaried white-collar employees who currently qualify for the standard EAP exemption.

<sup>215</sup> 84 FR 51238.

<sup>216</sup> See section IV.A.3.ii.

<sup>217</sup> See 84 FR 51260.

<sup>218</sup> The potential impact of these four alternatives is discussed in greater detail below. See section VII.C.8.

<sup>219</sup> See section IV.A.3.ii.

The Department also considered setting the standard salary level at the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (\$1,145 per week or \$59,540 per year). This salary level is roughly the midpoint between the long and short test salary level alternatives (\$925 per week and \$1,378 per week, respectively). However, as discussed above, the Department is concerned that this approach could be seen by courts as making salary determinative of exemption status for too large a portion of employees, as this salary level would make the salary paid by the employer determinative of exemption status for roughly half (47 percent) of white-collar employees who earn between the long and short test salary levels.<sup>220</sup> The Department is also concerned that this approach would generate the same concerns that led to the district court decision invalidating the 2016 rule (which adopted the same methodology).<sup>221</sup>

The Department also considered using the 2004 methodology (the 20th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census region and in retail nationally), which is currently \$822 per week (\$42,744 per year). This is also the methodology that the Department used in the 2019 rule.<sup>222</sup> However, the salary level produced by the 2004 methodology is below the equivalent of the long test salary level (\$925 per week). As discussed, the Department considers the long test to be the lower boundary for an appropriate salary level since, except for the 2019 rule, employees who earn below the long test salary level have consistently been excluded from the EAP exemption by the initial screening function of the salary level.<sup>223</sup> Accordingly, the Department believes that a standard salary level produced using the 2004 methodology would be too low to fully effectuate the salary level's role in defining the EAP exemption.

The Department also considered setting the standard salary level at the long test level (\$925 per week or \$48,100 per year). Doing so would ensure the initial screening function of the salary level by restoring overtime protections to those employees who were consistently excluded from the EAP exemption prior to 2019, either by the long test salary level itself, or under the 2004 rule salary level, which was set equivalent to the long test salary

<sup>220</sup> See *id.*

<sup>221</sup> See *id.*

<sup>222</sup> 84 FR 51260.

<sup>223</sup> See section IV.A.2; section IV.A.4.



level.<sup>224</sup> However, as explained above, setting the standard salary level at the long test level would perpetuate the problem that has become evident under the 2004 and 2019 rules. Specifically, this approach would unduly deny overtime protections to all employees whose entitlement to overtime compensation was protected by the more rigorous long duties test.<sup>225</sup> As noted above, however, the Department believes that in a one-test system with the current duties test it must set the salary level above the long test salary level in order to better define and delimit which employees are employed in a bona fide EAP capacity.

While, for the reasons discussed herein, none of these alternatives were used as a method to establish the proposed salary test level, they confirm that the proposed salary level of the 35th percentile of weekly earnings of all full-time salaried employees in the lowest-wage Census Region (the South) is an appropriate salary level. The Department's proposed salary level appropriately would account for the shift from a two-test to a one-test system for determining exemption status, protecting lower-paid white-collar employees who traditionally have been entitled to overtime protection, while allowing employers to use the exemption for EAP employees earning less than the short test salary level.

The Department welcomes comments on its proposed increase to the standard salary level. The Department also invites comments on alternate salary methodologies and specifically how such alternative methodologies would better define and delimit bona fide EAP employees than the Department's proposed methodology.

## *B. Special Salary Levels—U.S. Territories and Motion Picture Industry*

### *1. United States Territories*

The FLSA's overtime requirements and the EAP exemption apply to employees in U.S. territories.<sup>226</sup> Historically, the Department generally applied special, lower salary levels to employees in U.S. territories that were not subject to the Federal minimum wage in section 6(a)(1) of the FLSA. Consistent with this principle, as the Department explained in the 2004 rule, the Department applied lower salary levels to employees in Puerto Rico, the U.S. Virgin Islands, and American Samoa because, until 1989, the FLSA permitted the establishment of special minimum wage rates below the Federal

minimum wage in these territories.<sup>227</sup> The Department did not set a special salary level for employees in Guam, where the Federal minimum wage has applied since at least 1957,<sup>228</sup> or the CNMI.<sup>229</sup>

In 1989, Congress amended the FLSA to apply the Federal minimum wage to the U.S. Virgin Islands beginning that same year and to Puerto Rico beginning in 1996, while maintaining special minimum wage rates for American Samoa.<sup>230</sup> When the Department next updated the salary level tests in 2004, it applied the same salary level to employees in Puerto Rico and the U.S. Virgin Islands that it applied to employees in the 50 states and the District of Columbia (\$455 per week), explaining that because these territories were "now subject to the same minimum wage as the U.S. mainland, there was no longer a basis for a special salary level test[.]"<sup>231</sup> The Department maintained a special salary level for employees in American Samoa equal to approximately 84 percent of the standard level (\$380 per week), since American Samoa was not subject to the Federal minimum wage. This was roughly the same ratio to the U.S. mainland salary level that existed prior to 2004.<sup>232</sup> The Department also continued to apply the same salary level to employees in Guam and the CNMI that it applied to employees in the U.S. mainland.

The Department followed the same approach in the 2016 rule. Like the 2004 rule, the 2016 rule would have continued to apply the standard salary level to employees in all the U.S. territories except for American

Samoa.<sup>233</sup> It also would have maintained a special salary level for employees in American Samoa, keeping it at 84 percent of the standard salary level, since American Samoa was still subject to special minimum wage rates below the Federal minimum wage.

In the 2019 rule, the Department elected to preserve the 2004 standard salary level for employees in Puerto Rico, Guam, the U.S. Virgin Islands, and the CNMI (\$455 per week) instead of applying the \$684 per week salary level that applied to employees in the 50 states and the District of Columbia;<sup>234</sup> in effect, establishing a special salary level for employees in territories that were subject to the Federal minimum wage for the first time. In support of this approach, the Department pointed to the economic climate in Puerto Rico; stated that Guam, the U.S. Virgin Islands, and the CNMI, as U.S. territories, also faced their own economic challenges; and expressed a desire to promote salary level consistency across the U.S. territories.<sup>235</sup> The Department also maintained the 2004 special salary level for employees in American Samoa (\$380 per week).<sup>236</sup> The Department determined that a special salary level lower than the other four territories was warranted for American Samoa because, like in 2004 and 2016, the territory was subject to special minimum wage rates below the Federal minimum wage.<sup>237</sup>

In § 541.600, the Department proposes to return to its longstanding pre-2019 approach of only setting special salary levels for employees in those U.S. territories that are not subject to the Federal minimum wage. Accordingly, the Department proposes to apply the

<sup>227</sup> 69 FR 22172.

<sup>228</sup> See Sarah A. Donovan, Cong. Rsch. Serv., R42713, *The Fair Labor Standards Act (FLSA): An Overview*, 6 (Mar. 8, 2023). In 1957, Congress amended section 13 of the FLSA to clarify that the Act's minimum wage and overtime requirements apply to Guam. Public Law 85–231, 71 Stat. 514 (Aug. 30, 1957) (codified at 29 U.S.C. 213(f)).

<sup>229</sup> The CNMI was exempted from the FLSA's minimum wage requirements, but not its overtime requirements, under the 1976 Covenant of Association with the United States, which established the CNMI as a Commonwealth. Public Law 94–241, sec. 503(c), 90 Stat. 263, 268 (Mar. 24, 1976). Congress applied the FLSA's minimum wage requirements to the CNMI for the first time in the Fair Minimum Wage Act of 2007, which was subsequently amended in 2015; pursuant to this legislation, the minimum wage in the CNMI gradually increased until it reached the full section 6(a)(1) minimum wage in 2018. See Public Law 110–28, sec. 8103, 121 Stat. 112, 188 (May 25, 2007); Public Law 114–61, sec. 1, 129 Stat. 545 (Oct. 7, 2015); Minimum Wage in the Northern Mariana Islands, WHD, available at: <https://www.dol.gov/sites/dolgov/files/WHd/legacy/files/cnmi.pdf>.

<sup>230</sup> See Public Law 101–157, sec. 4, 103 Stat. 938, 939–941 (Nov. 17, 1989).

<sup>231</sup> 69 FR 22172.

<sup>232</sup> *Id.*

<sup>233</sup> See 81 FR 32444. After the Department published the 2016 rule, Congress passed the Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA), Public Law 114–187, which prevented the rule from taking effect in Puerto Rico until the Comptroller General of the United States produced a report on the impact of applying the rule to Puerto Rico and the Secretary of Labor determined, based on the report, that applying the rule to Puerto Rico would not have a negative impact on its economy. The Comptroller General published its report in June 2018. See U.S. Gov't Accountability Off., GAO–18–483, *Puerto Rico: Limited Federal Data Hinder Analysis of Economic Condition and DOL's 2016 Overtime Rule* (June 29, 2018). The 2016 rule was invalidated and so the Department did not have occasion to further address this issue.

<sup>234</sup> 84 FR 51246.

<sup>235</sup> *Id.* In the 2019 rule, the Department explained that while PROMESA did not apply to rulemakings other than the 2016 rule, the considerations that motivated PROMESA's adoption supported setting a special salary level in Puerto Rico. See *id.* As in 2019, the Department continues to believe that PROMESA does not constrain the Department's authority to set a salary level for Puerto Rico in this rulemaking.

<sup>236</sup> *Id.*

<sup>237</sup> *Id.*

<sup>224</sup> See section IV.A.1.

<sup>225</sup> See section IV.A.2.

<sup>226</sup> 29 U.S.C. 213(f).

standard salary level (\$1,059 per week) to employees in Puerto Rico, where the Federal minimum wage has applied since 1996; Guam, where the Federal minimum wage has applied since at least 1957; the U.S. Virgin Islands, where the Federal minimum wage has applied since 1989; and the CNMI, where the Federal minimum wage has applied since 2018. The Department proposes to set a special salary level for employees in American Samoa equal to 84 percent of the standard salary level (\$890 per week, based on a proposed standard salary level of \$1,059 per month), since American Samoa remains subject to special minimum wage rates below the Federal minimum wage.<sup>238</sup> This is the same ratio to the standard salary level that the Department used in the 2004 and 2016 rules, as well as the same ratio to the salary level in the other four U.S. territories that the Department used in the 2019 rule.<sup>239</sup>

Pursuant to the Fair Minimum Wage Act of 2007, as amended, industry-specific special minimum wage rates in American Samoa are scheduled to be gradually eliminated. Under this legislation, barring further Congressional action, special wage rates in American Samoa will increase by \$0.40 on September 30, 2024 and every 3 years thereafter until they equal the Federal minimum wage.<sup>240</sup> As such, the Department also proposes that 90 days after the highest industry minimum wage for American Samoa equals the Federal minimum wage, the full standard salary level will apply for all EAP employees in all industries in American Samoa.

The Department recognizes that the salary levels for the U.S. territories have not changed since 2004, and it understands that U.S. territories face their own economic challenges. However, the FLSA's EAP exemption should apply equally to employees subject to the Federal minimum wage in

section 6(a)(1) of the FLSA—including in the U.S. territories, to which this provision explicitly applies—absent a special minimum wage for the territory, which the Department has interpreted as an indication of Congressional intent to treat employees in the territory differently. As noted above, except for the 2019 rule, the Department has taken the position that a special, lower salary level should only be set for employees in those U.S. territories that are not subject to the Federal minimum wage, a group which is currently limited to employees in American Samoa.<sup>241</sup> This approach provides a clear and objective standard by which to determine whether to apply the standard salary level or a special, lower salary level. Thus, in accordance with the Department's longstanding practice, and in the interest of applying the FLSA uniformly to all employees subject to the Federal minimum wage, the Department proposes to apply the standard salary level to employees in Puerto Rico, Guam, the U.S. Virgin Islands, and the CNMI, and to maintain a special salary level for employees in American Samoa equal to 84 percent of the standard salary level until the highest industry minimum wage rate applicable in the territory equals the Federal minimum wage.<sup>242</sup>

The Department seeks comments on the proposed salary levels for the U.S. territories.

<sup>241</sup> Three U.S. territories have a local minimum wage higher than the Federal minimum wage. The local minimum wage in Puerto Rico is currently \$9.50 per hour; the local minimum wage in Guam is currently \$9.25 per hour; and the local minimum wage in the U.S. Virgin Islands is currently \$10.50 per hour. See State Minimum Wage Laws, WHD, available at: <https://www.dol.gov/agencies/whd/minimum-wage/state>.

<sup>242</sup> It is the Department's intent that the proposal to apply the standard salary level to employees in territories that are subject to the Federal minimum wage is severable from the proposal to raise the standard salary level from the current amount (\$684 per week) to the 35th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (\$1,059 per week using current data). The Department also intends that the proposal to set the special salary level for employees in American Samoa equal to 84 percent of the standard salary level, and to eliminate the special salary level for American Samoa when the highest industry minimum wage equals the Federal minimum wage, be severable from the proposal to raise the standard salary level. The Department has an interest in the uniform application of the EAP exemption to all employees subject to the Federal minimum wage and in adopting a clear and objective standard by which to determine whether to apply a special salary level to any U.S. territory. Accordingly, the Department's intent is to apply the standard salary level to employees in those territories that are subject to the Federal minimum wage and set a special salary for American Samoa equal to 84 percent of the standard salary level until the highest minimum wage in the territory reaches the Federal minimum wage even if the standard salary level amount proposed in this rule does not take effect.

## 2. Motion Picture Producing Industry

The Department permits employers to classify as exempt employees in the motion picture producing industry who are paid a specified base rate per week (or a proportionate amount based on the number of days worked), so long as they meet the duties tests for the EAP exemption.<sup>243</sup> This exception from the salary basis requirement was created in 1953 to address the “peculiar employment conditions existing in the [motion picture producing] industry,” and applies, for example, when a motion picture producing industry employee works less than a full workweek and is paid a daily base rate that would yield the weekly base rate if 6 days were worked.<sup>244</sup> Consistent with its practice since the 2004 rule, the Department proposes in § 541.709 to increase the required base rate in proportion to the Department's proposed increase in the standard salary level test, resulting in a proposed base rate of \$1,617 per week (or a proportionate amount based on the number of days worked).<sup>245</sup>

The Department seeks comments on the proposed base rate for the motion picture industry.

### C. Highly Compensated Employees

In the 2004 rule, the Department created the HCE test for certain highly compensated employees. Combining a much higher compensation requirement with a minimal duties test, the HCE test is based on the rationale that employees who earn at least a certain amount annually—an amount substantially higher than the annual equivalent of the weekly standard salary level—will almost invariably pass the standard duties test.<sup>246</sup> The HCE test's primary purpose is thus to serve as a streamlined alternative for very highly compensated employees because a very high level of compensation is a strong indicator of an employee's exempt status, thus eliminating the need for a detailed duties analysis.<sup>247</sup>

As outlined in § 541.601, to be exempt under the HCE test, an employee must

<sup>243</sup> § 541.709.

<sup>244</sup> 18 FR 2881 (May 19, 1953).

<sup>245</sup> The Department calculated this figure by dividing the proposed standard salary level (\$1,059 per week) by the current standard salary level (\$684 per week), and then multiplying this result (rounded to the nearest hundredth) by the base rate set in the 2019 rule (\$1,043 per week). This produces a new base rate of \$1,617 (per week), when rounded to the nearest whole dollar.

<sup>246</sup> 84 FR 51249; see also § 541.601(c) (“A high level of compensation is a strong indicator of an employee's exempt status, thus eliminating the need for a detailed analysis of the employee's job duties.”).

<sup>247</sup> See 69 FR 22173–74.

<sup>238</sup> Special wage rates by industry in American Samoa currently range from \$5.38 per hour to \$6.79 per hour. See Federal Minimum Wage in American Samoa, available at: <https://www.dol.gov/sites/dolgov/files/WHd/legacy/files/ASminwagePoster.pdf>.

<sup>239</sup> As noted above, the Department set the special salary level for American Samoa in the 2004 rule at \$380 per week, which is approximately 84 percent of the standard salary level of \$455 per week. 69 FR 22172. The 2016 rule would have set the special salary level for American Samoa at \$767 per week, which is 84 percent of the standard salary level of \$913 per week. 81 FR 32444. The 2019 rule preserved the 2004 salary level of \$455 per week for employees in Puerto Rico, Guam, the U.S. Virgin Islands, and the CNMI, as well as the 2004 salary level of \$380 per week (approximately 84 percent of \$455) for employees in American Samoa. 84 FR 51246.

<sup>240</sup> See Public Law 114–61, sec. 1, 129 Stat. 545 (Oct. 7, 2015).

earn at least the amount specified in the regulations in total annual compensation, of which at least the standard salary amount per week must be paid on a salary or fee basis,<sup>248</sup> and must customarily and regularly perform any one or more of the exempt duties or responsibilities of an executive, administrative, or professional employee. The HCE test applies only to employees whose primary duty includes performing office or non-manual work. Employees qualifying for exemption under the HCE test must receive at least the standard salary level per week on a salary or fee basis, while the remainder of the employee's total annual compensation may include commissions, nondiscretionary bonuses, and other nondiscretionary compensation.<sup>249</sup> Total annual compensation does not include board, lodging, or other facilities, and does not include payments for medical insurance, life insurance, retirement plans, or other fringe benefits. An employer is permitted to make a final "catch-up" payment during the last pay period or within one month after the end of the 52-week period to bring an employee's compensation up to the required level.

The 2004 rule set the HCE total annual compensation amount at \$100,000,<sup>250</sup> which exceeded the annual earnings of approximately 93.7 percent of salaried workers.<sup>251</sup> In the 2016 rule, the Department set the total annual compensation requirement for the HCE test at the annualized weekly earnings of the 90th percentile of full-time salaried workers nationally, which was \$134,004.<sup>252</sup> As previously noted, however, the 2016 rule was enjoined before its effective date and was subsequently invalidated in litigation.<sup>253</sup> In 2019, the Department set the HCE total annual compensation

threshold at the 80th percentile of full-time salaried worker earnings nationwide, resulting in a HCE threshold of \$107,432 per year.<sup>254</sup>

The Department continues to believe that the HCE test is a useful alternative to the standard salary level and duties tests for highly compensated employees. However, as with the standard salary level, the HCE total annual compensation level must be updated to ensure that it remains a meaningful and appropriate standard to pair with the minimal HCE duties test. To maintain the HCE test's role as a streamlined alternative for those employees most likely to qualify as EAPs, the HCE total annual compensation level must be high enough to exclude all but those employees "at the very top of [the] economic ladder."<sup>255</sup>

Accordingly, the Department proposes to update the HCE test by setting the total compensation amount equal to the annualized weekly earnings of the 85th percentile of full-time salaried workers nationwide. Consistent with its prior rules, the Department is setting the HCE test level using nationwide data, rather than a regional data set. This approach results in a HCE threshold of \$143,988, of which at least \$1,059 per week (the proposed standard salary level) must be paid on a salary or fee basis.<sup>256</sup>

The Department considered updating the current HCE threshold (the 80th percentile) with current data (which would result in a compensation level of \$125,268), but is concerned that repeating the 2019 rule's methodology now would not produce a threshold high enough to reserve the HCE test for employees at the top of today's economic ladder and could risk the unintended exemption of large numbers of employees in high-wage regions.<sup>257</sup> The Department also considered setting the HCE threshold at the 90th percentile, like in its 2016 rule. However, the Department is concerned that the resulting compensation level (\$172,796) could unduly restrict the use of the HCE exemption for employers in

lower-wage regions and industries.<sup>258</sup> In contrast, setting the HCE compensation level at the 85th percentile would be a reasonable increase, particularly in comparison to the HCE threshold initially adopted in 2004, which covered 93.7 percent of all full-time salaried workers.<sup>259</sup> The Department believes that setting the HCE threshold at the annualized weekly earnings of the 85th percentile of full-time salaried workers nationwide would be sufficient to guard against the unintended exemption of workers who are not bona fide executive, administrative, or professional employees, including those in higher-income regions and industries.

Under the proposed rule, employers that are currently using the HCE test to exempt more highly paid employees would instead need to apply the standard salary and duties test for employees earning between the current HCE threshold (\$107,432) and the annualized weekly earnings of the 85th percentile of full-time salaried workers nationwide. The Department estimates that there are approximately 248,900 salaried white-collar workers earning between \$107,432 and the proposed HCE total annual compensation level (\$143,988) who meet the HCE duties test but do not meet the standard duties test, and who therefore would become nonexempt without some intervening action by their employers.

As with other earning thresholds in the part 541 regulations, the Department is proposing to automatically update the HCE total compensation amount every 3 years to reflect current earnings data, as discussed in greater detail in section IV.D.4. Automatic updates to the HCE threshold would ensure that the threshold remains at an appropriate level in future years.

The Department welcomes comment on its proposed increase to the HCE threshold.

#### *D. Automatic Updates to the Salary and Total Annual Compensation Levels*

In each of its part 541 rulemakings since 2004, the Department recognized the need to regularly update the earnings thresholds to ensure that they remain effective in helping differentiate between exempt and nonexempt employees. As the Department observed in these rulemakings, even a well-calibrated salary level that is not kept up to date becomes obsolete as wages for nonexempt workers increase over time.<sup>260</sup> Long intervals between

<sup>248</sup> Although § 541.602(a)(3) allows employers to use nondiscretionary bonuses to satisfy up to 10 percent of the weekly standard salary level when applying the standard salary and duties tests, the Department's regulation at § 541.601(b)(1) does not permit employers to use nondiscretionary bonuses to satisfy the weekly standard salary level requirement for HCE workers. Employers may use commissions, nondiscretionary bonuses, and other nondiscretionary compensation to satisfy the remaining portion of the HCE total annual compensation amount. See 84 FR 51249.

<sup>249</sup> § 541.601(b)(1). The criteria for determining if an employee is paid on a "salary basis" are identical under the standard exemption criteria and the HCE test. See *Helix Energy Solutions*, 143 S.Ct. at 683.

<sup>250</sup> 69 FR 22269 (§ 541.601(a)).

<sup>251</sup> See *id.* at 22169 (Table 3).

<sup>252</sup> See 81 FR 32429.

<sup>253</sup> See *Nevada*, 275 F. Supp. 3d at 808. The district court's decision did not specifically discuss the HCE test; however, the decision invalidated the entire 2016 rule.

<sup>254</sup> See 84 FR 51307 (§ 541.601(a)(1)); see also *id.* at 51249–50.

<sup>255</sup> 69 FR 22174.

<sup>256</sup> It is the Department's intent that the increase in the HCE total annual compensation threshold is independent of, and severable from, the proposed increase in the standard salary level to the 35th percentile of weekly earnings of full-time salaried employees in the lowest-wage Census Region (the South).

<sup>257</sup> See 69 FR 22174 (explaining the need to avoid the unintended exemption of employees "such as secretaries in New York City or Los Angeles . . . who clearly are outside the scope of the exemptions and are entitled to the FLSA's minimum wage and overtime pay protections.").

<sup>258</sup> See 84 FR 51250.

<sup>259</sup> See 69 FR 22169–70 (Tables 3 and 4).

<sup>260</sup> 84 FR 51250–51; 81 FR 32430; see also 69 FR 22122, 22164.

rulemakings have resulted in eroded earnings thresholds based on outdated earnings data that were ill-equipped to help identify bona fide executive, administrative, and professional employees. This problem was clearly illustrated by the stagnant salary levels in the regulations from 1975 to 2004, during which period increases in the Federal minimum wage meant that earnings of a worker paid the Federal minimum wage exceeded the long test salary level for a 40-hour week and came close to equaling the short test salary level.<sup>261</sup>

To address this problem, in the 2004 and 2019 rules the Department expressed its commitment to regularly updating the salary levels, and in the 2016 rule it included a regulatory provision to automatically update the salary levels.<sup>262</sup> Based on the Department's experience with updating the salary levels, as well as additional considerations discussed below, the Department has concluded that adopting a regulatory provision for automatically updating the standard salary level and the HCE total annual compensation requirement to reflect current wage data, with the ability to pause future updates under certain conditions, would be the most viable and efficient way to ensure the EAP exemption salary levels remain up to date.

## 1. Background

The Department introduced a regulatory provision for automatically updating the salary level tests in its 2016 rulemaking. Prior to the 2016 rule, the Department addressed the subject of automatic updating twice in response to comments by some stakeholders calling for its adoption. In its 1970 rulemaking, the Department stated that a comment “propos[ing] to institute a provision calling for an annual review and adjustment of the salary tests . . . appears to have some merit, particularly since past practice has indicated that approximately 7 years elapse between amendment of the salary level requirements.”<sup>263</sup> Despite recognizing the potential value of this approach, the Department ultimately determined that

“such a proposal will require further study.”<sup>264</sup> Later, in its 2004 rule, the Department declined to adopt commenter requests for automatic increases to the salary level, reasoning in part that “the salary levels should be adjusted when wage survey data and other policy concerns support such a change” and that “the Department finds nothing in the legislative or regulatory history that would support indexing or automatic increases.”<sup>265</sup> In remarking on the lack of historical guidance related to the automatic updating of salary levels, the Department did not otherwise discuss its authority to promulgate such an approach through notice-and-comment rulemaking. Instead, the Department expressed its intent “in the future to update the salary levels on a more regular basis, as it did prior to 1975.”<sup>266</sup> Despite its best intentions, the Department's next rulemaking to update the salary levels did not occur for over a decade. The difficulty in achieving its goal of regularly updating the salary levels caused the Department to examine in greater detail in its 2016 rulemaking the possibility of automatically updating the salary levels.

In the 2016 rule, the Department introduced a new regulatory provision establishing a mechanism for automatically updating the standard salary test, the total annual compensation requirement for highly compensated employees, and the special salary levels for American Samoa and the motion picture industry.<sup>267</sup> Under this provision, future automatic updates would have occurred triennially, using the same methodologies that were used to initially set these earnings thresholds in the 2016 rule. The Department explained that the adopted automatic updating mechanism would “ensure that the salary level test is based on the best available data (and thus would remain a meaningful, bright-line test), produce more predictable and incremental changes in the salary required for the EAP exemption, and therefore provide certainty to employers and promote government efficiency.”<sup>268</sup> The district court decision invalidating the 2016 rule did not separately examine the merits of the automatic updating provision or the Department's authority to automatically update the salary levels. Rather, the court stated, “Having determined the [2016] Final

Rule is unlawful . . . , the Court similarly determines the automatic updating mechanism is unlawful.”<sup>269</sup>

In its 2019 rulemaking, the Department reaffirmed that “the need to update the part 541 earnings thresholds on a regular basis is clear.”<sup>270</sup> The Department elaborated that “[a]s employees' earnings rise over time, they begin surpassing the earnings thresholds set in the past” and make the thresholds “a less useful measure of employees' relative earnings, and a less useful method for identifying exempt employees.”<sup>271</sup> Rather than adopt an automatic updating mechanism, the Department initially proposed to keep the earnings thresholds up to date by publishing an NPRM in the **Federal Register** every 4 years seeking comment on whether to update the earnings thresholds using the existing methodology, with the understanding that the Department could forestall issuing such a proposal due to economic or other factors.<sup>272</sup> However, the Department declined to codify this approach in its final rule<sup>273</sup> or implement a mechanism for automatically updating the salary levels as suggested by some commenters, stating that doing so could deprive the Department of flexibility to adapt to unanticipated circumstances.<sup>274</sup> Instead, the Department reaffirmed its intention to update the salary levels more regularly through notice-and-comment rulemaking.<sup>275</sup>

## 2. The Department's Authority To Automatically Update the Salary Level Tests

The Department's authority to automatically update the salary level tests for the EAP exemption is grounded in section 13(a)(1), which expressly gives the Secretary broad authority to define and delimit the scope of the exemption. During the 2016 and 2019 rulemakings, some stakeholders questioned the Department's authority to automatically update the salary levels, asserting, among other points, that unlike other statutes that expressly provide for indexing, section 13(a)(1)'s silence indicates that Congress did not intend the salary level to be automatically updated, and that an automatic updating mechanism would

<sup>261</sup> The Federal minimum wage was increased to \$4.25 on April 1, 1991, equaling \$170 for a 40-hour week, the same amount as the higher long test salary level for professional employees. On September 1, 1997, the Federal minimum wage was increased to \$5.15, equaling \$206 for a 40-hour week, which was close to the \$250 short test salary level. See History of Federal Minimum Wage Rates Under the Fair Labor Standards Act, 1938–2009, WHD, available at: <https://www.dol.gov/agencies/whd/minimum-wage/history/chart>; 40 FR 7091–92.

<sup>262</sup> 69 FR 22171; 84 FR 51251–52; 81 FR 32430.

<sup>263</sup> 35 FR 884.

<sup>264</sup> *Id.*

<sup>265</sup> 69 FR 22171.

<sup>266</sup> *Id.*

<sup>267</sup> 81 FR 32430, 32443.

<sup>268</sup> *Id.* at 32430.

<sup>269</sup> *Nevada*, 275 F. Supp.3d at 808.

<sup>270</sup> 84 FR 10914.

<sup>271</sup> *Id.*

<sup>272</sup> *Id.* at 10914–15.

<sup>273</sup> See *id.* at 10915 n.140 (explaining how the Department could codify its proposed approach).

<sup>274</sup> 84 FR 51252.

<sup>275</sup> *Id.*

circumvent the Administrative Procedure Act (APA).<sup>276</sup>

As the Department has previously explained, Congress did not specifically set forth precise criteria for defining the EAP exemption, but instead authorized the Secretary to define and delimit the terms of the exemption.<sup>277</sup> Using this broad authority, the Department established the first salary level tests by regulation in 1938. Despite numerous amendments to the FLSA over the past 85 years, Congress has not restricted the Department's use of the salary level tests. Significant changes involving the salary requirements made through regulations issued pursuant to the Secretary's authority to define and delimit the exemption include adding a separate salary level for professional employees in 1940, adopting the two-test system in 1949, and switching to the single standard test and adding the new HCE test in 2004.<sup>278</sup> Despite having amended the FLSA numerous times over the years, Congress has not amended section 13(a)(1) to alter these regulatory salary requirements.

Other than directing the Department in 1990 to include in the EAP regulations certain computer employees paid at least six-and-a-half times the Federal minimum wage on an hourly basis,<sup>279</sup> Congress has never amended the FLSA in a manner that limits the use of the salary level tests.<sup>280</sup> Just as the Department has authority under section 13(a)(1) to establish and update the salary level tests, it likewise has authority to adopt a regulatory mechanism for automatically updating the salary levels to ensure that the tests remain effective. This interpretation is consistent with the well-settled principle that agencies have authority to "fill any gap left, implicitly or

explicitly, by Congress."<sup>281</sup> Further, the Department has determined that an automatic updating mechanism would better fulfill its statutory duty to define and delimit the EAP exemption because it will maintain the effectiveness of the salary levels, which have previously become eroded during large gaps between regulatory updates.

The Department's decision not to institute an automatic updating mechanism in its 2004 and 2019 rulemakings in no way suggests that it lacks authority to do so. In its 2004 rule, the Department stated that it found nothing in the legislative or regulatory history that would support indexing or automatic increases.<sup>282</sup> As the Department elaborated in its 2016 rulemaking, there was likewise no such authority disfavoring automatic updating.<sup>283</sup> The 2004 rule did not discuss the Department's authority to promulgate an automatic updating mechanism through notice-and-comment rulemaking or explore in detail whether automatic updates to the salary levels posed a viable solution to problems created by lapses between rulemakings. Similarly, the Department declined to adopt automatic updating in the 2019 rule because it "believe[d] that it is important to preserve the Department's flexibility to adapt to different types of circumstances,"<sup>284</sup> and not because it lacked authority to do so. While the Department decided not to institute an automatic updating mechanism in its 2019 rule, the Department did not assert that it lacked the legal authority for such a mechanism. And, as noted above, in its 2019 rule the Department reaffirmed its intention to update the salary levels more regularly. Consistent with this stated objective, and upon further consideration, the Department has concluded that the best method to ensure the standard salary level and HCE total compensation threshold remain up to date is an automatic updating mechanism that maintains the Department's flexibility to adapt to different circumstances and change course as necessary.

### 3. Rationale for Automatically Updating the Salary Level Tests

A regulatory mechanism for automatically updating the part 541 earnings thresholds would ensure that the levels keep pace with changes in employee earnings and thus remain effective in helping determine exemption status. As the Department's long experience has shown, earnings thresholds are only a strong measure of exempt status if they are kept up to date, and if left unchanged, such thresholds become substantially less effective in identifying exempt EAP employees as wages for workers increase over time. The Department's regulatory history, marked in many instances by lengthy gaps between rulemakings, underscores the difficulty with updating the earnings thresholds as quickly and regularly as necessary to keep pace with changing employee earnings and to maintain the full effectiveness of the test. Through the proposed automatic updating mechanism, the Department can timely and efficiently update the standard salary level and the HCE total annual compensation requirement by using the same methodologies as initially proposed and adopted through notice-and-comment rulemaking to set these thresholds, while a change to those methodologies would be effectuated through new notice-and-comment rulemaking. The proposed automatic updating mechanism would allow for regular and more predictable updates to the earnings thresholds, which would benefit both employers and employees and better fulfill the Department's statutory duty to define and delimit the EAP exemption by preventing the erosion of those levels over time.

As the Department explained in the 2016 rule, automatically updating the part 541 earnings thresholds would also prevent the more drastic and unpredictable threshold increases associated with less frequent updates. For example, between 1940 and 2019, the time between salary level updates ranged from 5 to 29 years. In part as a result of these breaks, long test salary level increases between 1940 and 1975 ranged from roughly 5 to 50 percent, the 2004 standard salary level test represented a 180 percent increase from the 1975 long test salary levels, and the 2019 standard salary level test represented an approximately 50 percent increase from the 2004 standard salary level. Automatically updating the part 541 earnings thresholds at a predetermined frequency using the same methodology would ensure that future salary level increases occur at a

<sup>276</sup> See 81 FR 32430, 32432; 84 FR 51251.

<sup>277</sup> 29 U.S.C. 213(a)(1).

<sup>278</sup> See section II.B.1–2.

<sup>279</sup> See Public Law 101–583, sec. 2, 104 Stat. 2871 (Nov. 15, 1990) (directing the Secretary to promulgate regulations that permit computer systems analysts, computer programmers, software engineers, and other similarly skilled professional workers as defined in the regulations to qualify as EAP exempt employees under section 13(a)(1), including those paid on an hourly basis if paid at least 6-and-a-half times the Federal minimum wage).

<sup>280</sup> Despite what some commenters asserted in the 2016 rulemaking, the Department's automatic updating mechanism does not conflict with section 13(a)(1)'s "time to time" language. See 81 FR 32431. Adopting a mechanism to ensure that the part 541 earnings thresholds continue screening out the same percentage of salaried workers over time would in no way preclude 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 proposed earnings thresholds are warranted.

<sup>281</sup> *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)).

<sup>282</sup> 69 FR 22171.

<sup>283</sup> See 81 FR 32432–33 (noting that "instituting an automatic updating mechanism . . . is an appropriate modernization and within the Department's authority.").

<sup>284</sup> 84 FR 51252.

known interval and in more gradual increments.

The Department is proposing for automatic updates to occur triennially (*i.e.*, every 3 years). The Department realizes that because employee earnings are constantly changing, annual or biennial automatic updates would keep the salary level more up to date and thereby may better serve the purpose of using earnings thresholds to help identify exempt employees. However, the Department is concerned about the potential burden that possible changes to the tests for exemption on an annual or biennial basis would impose on employers and believes that triennial updates are frequent enough to ensure that the part 541 earnings thresholds fulfill their purpose. This frequency is also consistent with the interval chosen in the 2016 rule following extensive public comment on this issue.<sup>285</sup>

In proposing to automatically update the earnings thresholds, the Department is mindful of previous statements from stakeholders, and the Department's own prior statements, about the need to preserve flexibility to adapt to unanticipated circumstances and prevailing economic conditions when setting the salary level.<sup>286</sup> Events since the Department's 2019 rule, including the COVID pandemic and its widespread impact on workplaces, have served to further validate these concerns. To address these concerns, the Department proposes to include in the regulatory provision the ability for the Department to temporarily delay a scheduled automatic update where unforeseen economic or other conditions warrant. This feature, which is a refinement of the automatic updating mechanism in the 2016 rule, would afford the Department added flexibility to adapt to unforeseen circumstances without sacrificing the benefits provided by automatic updating.

#### 4. Proposal for Automatically Updating the Salary Level Tests

The Department proposes to add a new § 541.607 that would establish a mechanism for automatically updating the standard salary level and the HCE total annual compensation requirement. Specifically, the Department proposes to automatically update the standard salary level and the total annual compensation requirement for highly compensated employees every 3 years to reflect current earnings data.

Under this proposal, the Department would automatically update the

standard salary level by adjusting it to remain at the 35th percentile of weekly earnings of full-time nonhourly workers in the lowest-wage Census Region (currently the South), as set out in section IV.A.3. The HCE test's total annual compensation requirement would be reset triennially at the annualized weekly earnings of the 85th percentile of full-time nonhourly workers nationally, as discussed in section IV.C. This approach, as opposed to other methods such as indexing these thresholds for inflation, would eliminate the risk that future levels will deviate from the underlying salary setting methodology established through rulemaking.<sup>287</sup> The Department proposes to update both thresholds using the most recent available four quarters of data, as published by BLS, preceding the publication of the Department's notice to automatically update the thresholds. Although the 2016 rule called for automatic updates based on a quarter of data,<sup>288</sup> relying on a full year of data would be consistent with the approach used to set the salary level in this proposal. Furthermore, relying on a year of data, rather than a quarter, would balance the Department's goal of accounting for current economic conditions with avoiding variations based on short-term fluctuations.

Under the proposed regulation, automatic updates would occur every 3 years, computed from the last day of the month in which this rulemaking take effect. Because under proposed §§ 541.600 and 541.709 both the special salary level for American Samoa and the base rate for the motion picture industry are set in relation to the standard salary level, those earnings thresholds would also reset at the time the standard salary level is updated. At least 150 days before the date of the update of the standard salary level and the HCE total

<sup>287</sup> During the 2016 rulemaking, the Department extensively considered whether to update the thresholds based on changes in the Consumer Price Index for All Urban Consumers (CPI-U)—a commonly used economic indicator for measuring inflation. See 81 FR 32438–41. The Department chose to update the thresholds using the same methodology used to initially set them in that rulemaking (*i.e.*, a fixed percentile of weekly earnings of full-time salaried workers), observing that the objectives that justify setting the salary level using a fixed percentile methodology also supported updating the thresholds using the same methodology. See *id.* at 32440. For this and other reasons discussed in detail in the 2016 rule, the Department concludes that updating the earnings thresholds by applying the same methodology used to set the initial levels instead of indexing them for inflation best ensures that the earnings thresholds continue to fulfill their objective of effectively differentiating between bona fide EAP employees and those who are entitled to overtime pay, and work appropriately under the duties test.

<sup>288</sup> *Id.* at 32551.

annual compensation requirement, the Department would publish in the **Federal Register** and on WHD's website a notice with the new earnings levels described above. Consistent with the 2016 rule, the Department is proposing this interval to provide employers ample notice and sufficient time to make any necessary adjustments. A period substantially longer than 150 days could hinder the Department's ability to ensure that the thresholds that take effect are based on the most up to date data.

Finally, the Department's proposal includes a provision delaying a scheduled automatic update while the Department engages in notice-and-comment rulemaking to change the earnings requirements and/or updating mechanism, where economic or other conditions merit. The delay occurs only if the Department publishes an NPRM proposing to change the salary level methodology (for example, changing the earnings percentile) and/or modify the automatic updating mechanism (for example, changing the updating frequency) before the date on which it publishes the notice of the revised salary and compensation levels under the regulations. The notice must state, in addition to the updated levels, that the automatic update will be paused for 120 days from the day the update was set to occur while the Department engages in rulemaking, and that the pause will be lifted on the 121st day unless by that time the Department finalizes a rule changing the salary level methodology and/or automatic updating mechanism. Accordingly, this proposal provides for 270 days—150 days before, and 120 days after, the effective date for the scheduled automatic update—to complete this process. The Department chose this interval to provide time for a public comment period and to issue a final rule. If the Department does not issue a final rule by the prescribed deadline, the pause on the scheduled automatic update would be lifted and the new salary levels would take effect on the 121st day after they were originally scheduled to take effect. So as not to disrupt the automatic updating schedule and given the relative shortness of the delay, the 120-day pause would not affect the date for the next scheduled automatic update. The next automatic update, therefore, would occur 3 years from the date the delayed automatic update would have been originally effective.

As discussed in section V below, the Department intends for the proposed automatic updating mechanism to be severable from the increases to the earnings thresholds proposed in this

<sup>285</sup> See 81 FR 32438.

<sup>286</sup> See, *e.g.*, 84 FR 51251–52.

rulemaking. Regardless of the methodology used to set the standard salary level and HCE total compensation requirement, the utility of these thresholds as a means of distinguishing exempt from nonexempt employees necessarily erodes over time unless they are regularly updated. Automatically updating the standard salary level and HCE total compensation requirement based on current earnings data and on a set schedule would ensure that the thresholds remain effective into the future and thus better fulfill the Department's statutory duty to define and delimit the EAP exemption. Therefore, even if the increases to the standard salary level and the HCE total annual compensation threshold in this proposal are determined to be invalid, the Department intends for the automatic updating mechanism to apply to the existing compensation thresholds. For example, it is the Department's intent that if the proposed increase to the standard salary level to the 35th percentile of weekly earnings of salaried white collar workers in the lowest-wage Census region is invalidated, the automatic update to the standard salary level would occur using the same methodology that is in effect on the date the Department publishes the required notice of the revised salary and compensation levels—which, as noted above, must be no less than 150 days before the scheduled update.

The Department welcomes comments on all aspects of the proposed automatic updating mechanism.

#### *E. Effective Date*

The Department is proposing that all aspects of this proposed rule would become effective 60 days after publication of a final rule. This proposed effective date is consistent with the 60 days mandated for a “major rule” under the Congressional Review Act and exceeds the 30-day minimum required under the APA.<sup>289</sup> The Department recognizes that the 60-day proposed effective date is shorter than the effective dates for the 2004, 2016, and 2019 rules, which were between approximately 90 and 180 days. The Department believes that a 60-day effective date is appropriate, however, in part because employers and employees are familiar with the procedures in the current regulations from the 2019 rulemaking and changed economic circumstances have caused a strong need to update the standard salary level. The Department seeks comments on the proposed effective date. It also seeks comments on whether

to apply different effective dates to different provisions of the proposed rule.

As discussed in detail below in sections VII.B–C, the Department's proposal to increase the HCE total annual compensation threshold to the annualized weekly earnings of the 85th percentile of full-time salaried workers nationwide would result in employers applying the standard duties test to some employees who are currently subject to the streamlined HCE duties test. However, employers are familiar with the standard duties test and only approximately 248,900 employees who earn between the current and proposed HCE compensation thresholds would not meet the standard duties test and be affected by this change. Accordingly, the Department believes the proposed 60-day effective date for the proposed increase to the HCE total compensation threshold would provide sufficient time for stakeholders to adjust. The Department seeks comments on the proposed effective date for the HCE compensation threshold increase.

As discussed below in sections VII.B.C, the Department's proposed standard salary level—the 35th percentile of weekly earnings of full-time nonhourly workers in the lowest-wage Census Region—would affect 3.4 million employees who earn between the current salary threshold of \$684 per week and the proposed threshold of \$1,059 per week. As discussed above, the Department believes it is important to update the standard salary level, both to account for earnings growth since the Department last updated the salary level in the 2019 rule and to build on the lessons learned in the Department's most recent rulemakings to better define and delimit employees working in a bona fide EAP capacity. The Department has also deliberately selected a proposed standard salary level that would ensure that duties remain determinative of exemption status for a significant majority of salaried white-collar employees and that would affect the exemption status of a relatively small group of currently exempt employees, more than half of whom earn below the long test salary level using contemporary data. At the same time, the Department recognizes that it updated the regulations approximately 4 years ago, economic conditions have changed significantly since then, and its proposed standard salary level would be a meaningful increase from the current standard salary level.

The Department seeks comments on whether the effective date for the increase of the standard salary level to the 35th percentile of weekly earnings

of full-time salaried workers in the lowest-wage Census Region should be 60 days after publication as proposed or if the increase should be made effective at some later date, such as 6 months or a year after publication of a final rule. If the effective date were longer than 60 days, the Department seeks comments on whether it should initially adjust the salary level to reflect recent wage growth (for example, making an initial adjustment for wage growth 60 days after publication of a final rule and having the final rule standard salary level be effective 6 months or a year after publication). Additionally, the Department seeks comments on the methodology it could use for such an initial update, were it to follow such an approach. In particular, the Department invites comments on whether to implement an initial update to the standard salary level, effective 60 days after publication of a final rule, that uses the current salary level methodology (the 20th percentile of weekly earnings of full-time nonhourly workers in the lowest-wage Census region and retail nationally) and applies it to the most recent data available (\$822 per week based on current data).

The Department also seeks comments on whether its proposed application of the standard salary level to employees in Puerto Rico, Guam, the U.S. Virgin Islands, and the CNMI, its proposed update to the special salary level for employees in American Samoa, and its proposed update to the special salary level for employees in the motion picture production industry, should also go into effect 60 days after a final rule as proposed, or if any of these changes should instead go into effect at a later date, such as 6 months or a year after publication. If the effective date for these provisions were longer than 60 days, the Department seeks comments on whether it should make an initial adjustment to these levels 60 days after publication of a final rule and, if so, what methodology should be used for the initial adjustment.

Finally, the Department is proposing that the first automatic update to the proposed compensation levels be effective 3 years after the proposed 60-day effective date. The Department seeks comments on whether the date for the first automatic update should be adjusted if it were to make an initial adjustment to any of these levels as discussed above.

#### **V. Severability**

The Department proposes to include a severability provision in part 541 so that if one or more of the provisions of part 541 is held invalid or stayed pending

<sup>289</sup> See 5 U.S.C. 801(a)(3)(A); 5 U.S.C. 553(d).



further agency action, the remaining provisions would remain effective and operative. The Department proposes to add this provision as § 541.5.

It is the Department's intent that any final rule following from this proposal apply to its greatest extent even if one or more provisions of such rule are invalidated or stayed. For example, as noted above, it is the Department's intent that the proposed automatic updating mechanism be effective even if the proposed increase in the standard salary level is invalidated. Similarly, it is the Department's intent that the increase in the HCE total annual compensation requirement be effective even if the increase in the standard salary level is invalidated. It is also the Department's intent that the standard salary level apply in territories subject to the Federal minimum wage even if the increase in the standard salary level in this rulemaking is invalidated. Additionally, it is the Department's intent that the earnings thresholds set in this rulemaking apply even if the mechanism for automatically updating them in the future is determined to be invalid. In all circumstances, whether or not specifically discussed, it is the Department's intent that the provisions of any final rule be construed to give the maximum effect to the provisions permitted by law, and that any invalidated provisions be considered severable from part 541 and not affect the remainder of a final rule.

## VI. Paperwork Reduction Act

The Paperwork Reduction Act of 1995 (PRA), 44 U.S.C. 3501 *et seq.*, and its attendant regulations, 5 CFR part 1320, require the Department to consider the agency's need for its information collections, their practical utility, the impact of paperwork and other information collection burdens imposed on the public, and how to minimize those burdens. The PRA typically requires an agency to provide notice and seek public comments on any proposed collection of information contained in a proposed rule. See 44 U.S.C. 3506(c)(2)(B); 5 CFR 1320.8.

This rulemaking would revise the burdens for the existing information collection previously approved under OMB control number 1235-0018, Records to be kept by Employers—Fair Labor Standards Act and under OMB control number 1235-0021, Employment Information Form. The information collection approved under OMB control number 1235-0021 is currently encumbered by another rulemaking. As a result, the Department has created a duplicate information collection under OMB control number

1235-0NEW to allow the public to comment on the burden estimates associated with this collection. The Department anticipates that at the time of publication of any potential final rule associated with this NPRM, no encumbrance will exist. Should a final rule be published, the Department will revert to the collection currently approved under OMB control number 1235-0021. As required by the PRA, the Department has submitted information collections as revisions to existing collections to OMB for review to reflect changes to existing burdens that will result from the implementation of this rulemaking. The Department has incorporated the increased universe of employers and employees (from Figure 1 and Table 32 of this NPRM) since the last PRA submission as well as the number of affected workers from Table 4 into the PRA burden analysis found in the supporting statements referenced below.

**Summary:** FLSA section 11(c) requires all employers covered by the FLSA to make, keep, and preserve records of employees and of wages, hours, and conditions of employment. An FLSA-covered employer must maintain the records for such period of time as prescribed by regulations issued by the Secretary. The Department has promulgated regulations at 29 CFR part 516 establishing the basic FLSA recordkeeping requirements. This NPRM, if finalized, would not impose any new information collection requirements; rather burdens under existing requirements would change as more employees become entitled to minimum wage and overtime protections.

**Purpose and use:** This proposed rule, which would revise 29 CFR part 541, affects the following provisions that could be considered to entail collections of information: (1) disclosure and recordkeeping requirements for covered employers; and (2) the complaint process under which employees may file a complaint with the Department to investigate potential violations of the FLSA. The proposed rule could potentially affect the number of employees for whom employers may need to maintain records and could potentially affect the number of complaints the Department receives from employees.

WHD obtains PRA clearance under OMB control number 1235-0018 for an information collection with respect to recordkeeping. An Information Collection Request (ICR) has been submitted to revise the approval and adjust the burdens for this collection. WHD obtains PRA clearance under

control number 1235-0021 for an information collection covering complaints alleging violations of various labor standards that the agency already administers and enforces. As noted, for the purpose of this NPRM, the Department has created a duplicate ICR (1235-0NEW) to allow the public to comment. An ICR has been submitted to revise the approval to revise the burdens applicable to complaints in this proposed rule.

**Information and technology:** There is no particular order or form of records prescribed in the current regulations or in the proposed rule. An employer may meet the requirements of this proposed rule using paper or electronic means. WHD, to reduce the burden caused by the filing of complaints that are not actionable by the agency, uses a complaint filing process in which complainants discuss their concerns with WHD professional staff. This process allows agency staff to refer complainants raising concerns that are not actionable under Federal wage and hour laws and regulations to an agency that may be able to offer assistance. WHD uses employer records to determine compliance with various FLSA requirements. Employers use the records to document compliance with the FLSA, including demonstrating qualification for various exemptions. WHD uses the Employment Information Form (1235-0021) to document allegations of non-compliance with labor standards the agency administers. To allow the public to comment, the Department has created duplicate ICR 1235-0NEW.

**Minimizing Small Entity Burden:** Although the FLSA recordkeeping requirements involve small entities, including small state and local government agencies, the Department minimizes respondent burden by requiring no specific order or form of records in responding to this information collection. Burden is reduced on complainants by providing a template to guide answers.

**Public comments:** As part of its continuing effort to reduce paperwork and respondent burden, the Department conducts a preclearance consultation program to provide the general public and Federal agencies with an opportunity to comment on proposed and continuing collections of information in accordance with the PRA. This program helps to ensure that requested data can be provided in the desired format, reporting burden (time and financial resources) is minimized, collection instruments are clearly understood, and the impact of collection requirements on respondents can be

properly assessed. The Department seeks comments on its analysis (contained in the supporting statements referenced below) that this NPRM creates a slight increase in paperwork burden associated with ICR 1235–0021, Employment Information Form (reflected in duplicate ICR 1235–0NEW), and affects the recordkeeping requirements and burdens on the regulated community in ICR 1235–0018, Records to be kept by Employers—Fair Labor Standards Act. Commenters may send their views on the Department’s PRA analysis in the same way they send comments in response to the NPRM as a whole (e.g., through the [www.regulations.gov](http://www.regulations.gov) website), including as part of a comment responding to the broader NPRM. Alternatively, commenters may submit a comment specific to this PRA analysis by sending an email to [WHDPRAComments@dol.gov](mailto:WHDPRAComments@dol.gov). While much of the information provided to OMB in support of the information collection request appears in the preamble, interested parties may obtain a copy of the supporting statements for the affected ICRs by sending a written request to the mail address shown in the **ADDRESSES** section at the beginning of this preamble. Alternatively, a copy of the ICR applicable supporting documentation, including a description of the likely respondents, proposed frequency of response, and estimated total burden, may be obtained free of charge from the [RegInfo.gov](http://RegInfo.gov) website. Similarly, the complaint process ICR is available by visiting <http://www.reginfo.gov/public/do/PRAMain>.

*OMB and the Department are particularly interested in comments that:*

- Evaluate whether the proposed collections of information are necessary for the proper performance of the functions of the agency, including whether the information will have practical utility;
- Evaluate the accuracy of the agency’s estimate of the burden of the proposed collection of information, including the validity of the methodology and assumptions used;
- Enhance the quality, utility, and clarity of the information to be collected; and
- Minimize the burden of the collection of information on those who are to respond, including through the use of appropriate automated, electronic, mechanical, or other technological collection techniques or other forms of information technology, e.g., permitting electronic submission of responses.

- Total burden for the recordkeeping and complaint process information collections, including the burdens that will be affected by this proposed rule and any changes, are summarized below. For the complaint ICR, the Department used actual data from FY22 and added additional burden related to this rulemaking using the number of affected workers from Table 4 of the RIA and multiplying by .05%. This is an approximate estimate of potential new complaints should the rule become final (please see the draft supporting statements referenced above for an explanation of how these estimates were derived). With respect to the FLSA recordkeeping ICR, the Department first revised the overall burden for the collection as the baseline number of employers and employees within the U.S. economy has changed since the collection was last submitted to OMB. The Department then added the newly affected workers described in the NPRM (see Table 4 of the RIA) to account for additional burden employers could potentially be subject to when a final rule is published.

*Type of review:* New collection (duplicate ICR to allow for public comment revising a currently approved information collection).

*Agency:* Wage and Hour Division, Department of Labor.

*Title:* Employment Information Form.

*OMB Control Number:* 1235–0NEW.

*Affected public:* Private sector, businesses or other for-profits and Individuals or Households.

*Estimated number of respondents:* 28,824 (1,824 from this rulemaking).

*Estimated number of responses:* 28,824 (1,824 from this rulemaking).

*Frequency of response:* On occasion.

*Estimated annual burden hours:* 9,608 (608 burden hours due to this NPRM).

*Estimated annual burden costs (capital/startup):* \$0 (\$0 from this rulemaking).

*Estimated annual burden costs (operations/maintenance):* \$0 (\$0 from this rulemaking).

*Estimated annual burden costs:* \$0 (\$0 from this rulemaking).

*Type of Review:* Revision to a currently approved information collection.

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

*OMB Control Number:* 1235–0018.

*Affected public:* Private sector, businesses or other for-profits and Individuals or Households.

*Estimated number of respondents:* 4,068,419.

*Estimated number of responses:* 41,160,407 (8,971,488 from this NPRM).

*Frequency of response:* Various.

*Estimated annual burden hours:* 1,105,833 (299,050 from this NPRM).

*Estimated annual burden costs:* \$51,277,476.

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

Under Executive Order 12866, OMB’s Office of Information and Regulatory Affairs (OIRA) determines whether a regulatory action is significant and, therefore, subject to the requirements of the Executive Order and OMB review. As amended by Executive Order 14094, section 3(f) of Executive Order 12866 defines a “significant regulatory action” as a regulatory action that is likely to result in a rule that may: (1) have an annual effect on the economy of \$200 million or more; or adversely affect in a material way the economy, a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or state, local, territorial, or tribal governments or communities; (2) create a serious inconsistency or otherwise interfere with an action taken or planned by another agency; (3) materially alter the budgetary impact of entitlements, grants, user fees or loan programs or the rights and obligations of recipients thereof; or (4) raise legal or policy issues for which centralized review would meaningfully further the President’s priorities or the principles set forth in the Executive Order. OIRA has determined that this proposed rule is a “significant regulatory action” within the scope of section 3(f)(1) of Executive Order 12866.

Executive Order 13563 directs agencies to, among other things, propose or adopt a regulation only upon a reasoned determination that its benefits justify its costs; that it is tailored to impose the least burden on society, consistent with obtaining the regulatory objectives; and that, in choosing among alternative regulatory approaches, the agency has selected those approaches that maximize net benefits. Executive Order 13563 recognizes that some costs and benefits are difficult to quantify and provides that, when appropriate and permitted by law, agencies may consider and discuss qualitatively values that are difficult or impossible to quantify, including equity, human dignity, fairness, and distributive impacts. The analysis below outlines the impacts that the Department of Labor (Department) anticipates may result from this proposed rule, if finalized, and was prepared pursuant to the above-mentioned executive orders.

*A. Introduction*

## 1. 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 their employees and of the wages, hours, and other conditions and practices of employment.

The FLSA provides a number of exemptions from the Act's minimum wage and overtime pay provisions, including one for bona fide executive, administrative, and professional (EAP) employees. The exemption applies to employees employed in a bona fide executive, administrative, or professional capacity, as those terms are "defined and delimited" by the Department.<sup>290</sup> The Department's regulations implementing these "white-collar" exemptions are codified at 29 CFR part 541. Since 1940, the regulations implementing the exemption have generally required each of the following three tests to be met: (1) the employee must be paid a predetermined and fixed salary that is not subject to reduction because of variations in the quality or quantity of work performed (the salary basis test); (2) the amount of salary paid must meet a minimum specified amount (the salary level test); and (3) the employee's job duties must primarily involve executive, administrative, or professional duties as

defined by the regulations (the duties test).

The Department has updated the salary level test many times since its implementation in 1938. Table 1 presents the weekly salary levels associated with the EAP exemptions since 1938, organized by exemption and long/short/standard duties tests. From 1949 to 2004, the Department determined exemption status using a two-test system comprised of a long test (a lower salary level paired with a more rigorous duties test that limited performance of nonexempt work to no more than 20 percent for most employees) and a short test (a higher salary level paired with a less rigorous primary duties requirement that did not have a numerical limit on the amount of nonexempt work). In 2004, rather than update the two-test system, the Department chose to establish a new single-test system for determining exemption status, setting the standard salary level test at \$455 a week, which was equivalent to the long test salary level, and pairing it with a standard duties test that was substantially equivalent to the more lenient short duties test. Because the single standard duties test was equivalent to the short duties test, employees who met the long test salary level and previously passed either the more rigorous long, or less rigorous short, duties test passed the standard duties test. The Department also added a new highly compensated employee (HCE) test, which used a very minimal duties test and a very high total compensation test set at \$100,000 per year (*see* section II.B.2. for further discussion). In 2016, to address the

concern that the standard test exempted lower-paid salaried employees performing large amounts of nonexempt work who had previously been protected by the more rigorous long duties test, the Department published a final rule setting the standard salary level at \$913 per week, which was equivalent to the low end of the historic range of short test salary levels, and the HCE annual compensation level at \$134,004. This approach restored overtime protection for employees performing substantial amounts of nonexempt work who earned between the long test salary level and the low end of the short test salary range, as they failed the new standard salary level test. As previously discussed, the U.S. District Court for Eastern District of Texas held the 2016 rule invalid. In 2019, in part to address the concern raised in the litigation that the approach taken in the 2016 rulemaking would have prevented employers from using the exemption for employees who earned between the long test salary level and the low end of the short test salary range and met the more rigorous long duties test, the Department returned to the methodology used in the 2004 rule and set the salary level at the 20th percentile of weekly earnings of full-time salaried workers in the South and in the retail industry nationally. Applying this method to the earnings data available in 2019 produced a standard salary level that was below the long test salary level. The current earnings thresholds, as published in 2019, are \$684 a week for the standard salary test and \$107,432 per year for the HCE test.

TABLE 1—HISTORICAL SALARY LEVELS FOR THE EAP EXEMPTIONS

Date enacted	Long duties test			Short duties test
	Executive	Administrative	Professional	
1938 .....	* \$30	\$30 .....	.....	.....
1940 .....	30	\$200 (per month) ...	\$200 (per month) ...	.....
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 duties test				
2004 .....	\$455			
2019 .....	\$684			

\* Unless otherwise specified, all figures are dollars per week.

<sup>290</sup> 29 U.S.C. 213(a)(1).

## 2. Need for Rulemaking

The goal of this rulemaking is not only to update the single standard salary level to account for earnings growth since the 2019 rule, but also to build on the lessons learned in the Department's most recent rulemakings to more effectively define and delimit employees working in a bona fide EAP capacity. Specifically, the Department is proposing to update the standard salary level by setting it equal to the 35th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (currently the South), based on the most recent Current Population Survey (CPS) data.<sup>291</sup> Using 2022 CPS Merged Outgoing Rotation Group (MORG)<sup>292</sup> data, the salary level would be set at \$1,059 per week.

The Department's proposed standard salary level will, in combination with the standard duties test, better define and delimit which employees are employed in a bona fide EAP capacity in a one-test system. As explained in greater detail in sections III and IV.A., above, setting the standard salary level at or below the long test salary level, as the 2004 and 2019 rules did, results in the exemption of lower-salaried employees who traditionally were entitled to overtime protection under the long test either because of their low salary or because they perform large amounts of nonexempt work, in effect significantly broadening the exemption compared to the two-test system. Setting the salary level at the low end of the historic range of short test salary levels, as the 2016 rule did, would have restored overtime protections to those employees who perform substantial amounts of nonexempt work and earned between the long test salary level and the low end of the short test salary range. However, it also would have resulted in denying employers the use of the exemption for lower-salaried employees who traditionally were not entitled to overtime compensation under the long test, which raised

concerns that the Department was in effect narrowing the exemption. By setting a salary level above what would currently be the equivalent of the long test salary level, the proposal would restore the right to overtime pay for salaried white-collar employees who prior to the 2019 rule were always considered nonexempt if they earned below the long test (or long test-equivalent) salary level. And it would ensure that fewer lower paid white-collar employees who perform significant amounts of nonexempt work are included in the exemption. At the same time, by setting it well below what would currently be the equivalent of the short test salary level, the proposal would allow employers to continue to use the exemption for many lower paid white-collar employees who were made exempt under the 2004 standard duties test. The proposed salary level would also more reasonably distribute between employees and their employers what the Department now understands to be the impact of the shift from a two-test to a one-test system on employees earning between the long and short test salary levels.

As the Department has previously noted, the amount paid to an employee is "a valuable and easily applied index to the 'bona fide' character of the employment for which exemption is claimed, as well as the "principal[]" "delimiting requirement" "prevent[ing] abuse" of the exemption."<sup>293</sup> Additionally, the salary level test facilitates application of the exemption by saving employees and employers from having to apply the more time-consuming duties analysis to a large group of employees who will not pass it. For these reasons, the salary level test has been a key part of how the Department defines and delimits the EAP exemption since the beginning of its rulemaking on the EAP exemption.<sup>294</sup> At the same time, the salary test's role in defining and delimiting the scope of the EAP exemption must allow for appropriate examination of employee duties.<sup>295</sup> Under the Department's proposal, duties would continue to determine the exemption status for most salaried white-collar employees, addressing the legal concerns that have been raised about excluding from the EAP exemption too many white-collar employees solely based on their salary level.

The Department also proposes to update the HCE total annual

compensation requirement to the annualized weekly earnings of the 85th percentile of full-time salaried workers nationally (\$143,988 in 2022). Though not as high a percentile as the HCE threshold initially adopted in 2004, which covered 93.7 percent of all full-time salaried workers,<sup>296</sup> the Department's proposed increase to the HCE threshold would ensure it continues to serve its intended function, because the HCE total annual compensation level would be high enough to exclude all but those employees at the very top of the economic ladder.

In accordance with the Department's traditional practice, and in the interest of applying the FLSA uniformly to areas subject to the Federal minimum wage, the Department is also proposing to apply the standard salary level to all territories that are subject to the Federal minimum wage and to update the special salary levels for American Samoa and the motion picture industry in relation to the new standard salary level. Having not increased these levels since 2004, there is a need to increase the salary levels in U.S. territories, particularly for employees in those territories that are subject to the Federal minimum wage.

In its three most recent part 541 rulemakings, the Department has expressed its commitment to keeping the earnings thresholds up to date to ensure that they remain effective in helping differentiate between exempt and nonexempt employees. Long intervals between rulemakings have resulted in eroded earnings thresholds based on outdated earnings data that were ill-equipped to help identify bona fide EAP employees. This rulemaking is motivated in part by the need to keep the part 541 earnings thresholds up to date. Based on its long experience with updating the salary levels, the Department has determined that adopting a regulatory provision for automatically updating the salary levels, with an exception for pausing future updates under certain conditions, is the most viable and efficient way to ensure the EAP exemption earnings thresholds keep pace with changes in employee pay and thus remain effective in helping determine exemption status. Accordingly, the Department is including in this proposed rule a mechanism for automatically updating the salary and compensation levels every 3 years. As explained in greater detail in section IV.D., employees and employers alike would benefit from the

<sup>291</sup> The Department uses the terms *salaried* and *nonhourly* interchangeably in this rule because, consistent with its 2004, 2016, and 2019 rules, the Department considered data representing compensation paid to nonhourly workers to be an appropriate proxy for compensation paid to salaried workers. The Department also notes that the terms *employee* and *worker* are used interchangeably throughout this analysis.

<sup>292</sup> MORG is a supplement to the CPS and is conducted on approximately one-fourth of the CPS sample monthly to obtain information on weekly hours worked and earnings. The Department relied on CPS MORG data for calendar year 2022 to develop this NPRM. The Department will update the data used in any final rule resulting from this proposal.

<sup>293</sup> Stein Report at 19, 24; see also 81 FR 32422.

<sup>294</sup> See 84 FR 51237.

<sup>295</sup> See 84 FR 51238.

<sup>296</sup> See 69 FR 22169 (Table 3).

certainty and stability of regularly scheduled updates.

### 3. 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 proposed rule using pooled CPS MORG data. *See* section VII.B.2. The Department estimates in the first year after implementation, there would be 3.6 million affected workers.<sup>297</sup> This includes 3.4 million workers who meet the standard duties test and earn at least \$684 per week but less than \$1,059 per week and would either become eligible for overtime or have their salary increased to at least \$1,059 per week (Table 2).<sup>298</sup> An estimated 248,900 workers would be

affected by the proposed increase in the HCE compensation test from \$107,432 per year to \$143,988 per year. In Year 10, with automatic updating, the Department estimates that 4.3 million workers would be affected by the proposed change in the standard salary level test and 768,700 workers would be affected by the proposed change in the HCE total annual compensation test.<sup>299</sup>

This analysis quantifies three direct costs to employers: (1) regulatory familiarization costs; (2) adjustment costs; and (3) managerial costs (*see* section VII.C.3). Total annualized direct employer costs over the first 10 years were estimated to be \$663.6 million, assuming a 7 percent discount rate.<sup>300</sup> This proposed rule would also transfer income from employers to employees in the form of increased wages. The

Department estimated annualized transfers would be \$1.3 billion. Most of these transfers would be attributable to wages paid under the FLSA's overtime provision; a smaller share would be attributable to the FLSA's minimum wage requirement. These transfers also account for employers who may choose to increase the salary of some affected workers to at least the new threshold so that they can continue to use the EAP exemption.

The Department also provides a qualitative discussion of the potential benefits of this proposed rule, including strengthened overtime protections for some workers, increased worker productivity, increased personal time for workers, and reduced reliance on social assistance programs. *See* section VII.C.5.

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

Impact	Year 1	Future years <sup>a</sup>		Annualized value	
		Year 2	Year 10	3% Real discount rate	7% Real discount rate
Affected Workers (1,000s)					
Standard .....	3,399	2,999	4,288	( <sup>b</sup> )	( <sup>b</sup> )
HCE .....	249	269	769	( <sup>b</sup> )	( <sup>b</sup> )
Total .....	3,648	3,268	5,057	( <sup>b</sup> )	( <sup>b</sup> )
Costs and Transfers (Millions in \$2022) <sup>c</sup>					
Direct employer costs .....	\$1,202.8	\$508.3	\$748.0	\$656.4	\$663.6
Transfers [d] .....	1,234.2	949.0	1,981.2	1,318.1	1,294.3

<sup>a</sup> These cost and transfer figures represent a range over the nine-year span.

<sup>b</sup> Not annualized.

<sup>c</sup> Costs and transfers for affected workers passing the standard and HCE tests are combined.

<sup>d</sup> This is the net transfer from employers to workers. There may also be transfers of hours and income from some workers to others.

## B. Number of Affected EAP Workers

### 1. Overview

This section explains the methodology used to estimate the number of workers who would be affected by the proposed rule. Workers who are currently EAP exempt are potentially affected by the proposed rule. In this proposed rule, as in

previous rules, the Department estimated the current 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. The methodology described here is consistent with the approach the

Department used in the 2004, 2016, and 2019 final rules.<sup>301</sup> To estimate the number of workers who would be affected by the rule, the proposed standard salary level and proposed HCE total annual compensation threshold are applied to the earnings of current EAP exempt workers.

<sup>297</sup> The term “affected workers” refers to the population of potentially affected EAP workers who either pass the standard duties test and earn at least \$684 but less than the new salary level of \$1,059 per week, or pass only the HCE duties test and earn at least \$107,432 but less than the new HCE compensation level of \$143,988 per year.

<sup>298</sup> Here and elsewhere in this analysis, numbers are reported at varying levels of aggregation, and are generally rounded to a single decimal point. However, calculations are performed using exact numbers. Therefore, some numbers may not match

the reported totals or the calculations shown due to rounding of components.

<sup>299</sup> In later years, earnings growth will cause some initially affected workers to no longer be affected because their earnings will exceed the new salary or compensation threshold. This is possible in both non-update and update years but is much more likely to occur in non-update years. Additionally, some workers will become newly affected because their earnings will reach at least \$684 per week, and in the absence of this proposed rule they would have lost their overtime protections. To estimate the

total number of affected workers over time, the Department accounts for both of these effects.

<sup>300</sup> Hereafter, unless otherwise specified, annualized values will be presented using the 7 percent real discount rate.

<sup>301</sup> *See* 69 FR 22196–209; 81 FR 32453–60; 84 FR 51255–60. Where the proposal follows the methodology used to determine affected workers in the 2004, 2016, and 2019 final rules, citations to these rules are not always included.

## 2. Data

All estimates of numbers of workers used in this analysis were based on data from the CPS MORG, which is sponsored jointly by the U.S. Census Bureau and Bureau of Labor Statistics (BLS).<sup>302</sup> The CPS is a large, nationally representative sample. Households are surveyed for 4 months, excluded from the survey for 8 months, surveyed for an additional 4 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.<sup>303</sup> This supplement contains the detailed information on earnings necessary to estimate a worker's exemption status. Responses are based on the reference week, which is always the week that includes the 12th day of the month.

Although the CPS MORG is a large-scale survey, administered to approximately 15,000 households monthly representing the entire nation, it is still possible to have relatively few observations when looking at subsets of employees, such as 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 3 years of CPS MORG data (2020–2022). Earnings for each observation from 2020 and 2021 were inflated to 2022 dollars using the Consumer Price Index for All Urban Consumers (CPI-U).<sup>304</sup> 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 2022 CPS MORG. Thus, the pooled CPS MORG sample uses roughly three times as many observations to represent the same total number of workers in 2022. The additional observations allow the Department to better characterize certain attributes of the potentially affected labor force. This pooled dataset is used to estimate all impacts of the proposed rulemaking.

Some assumptions and adjustments were necessary to use these data as the basis for the analysis. For example, the Department eliminated workers who reported that their weekly hours vary and who provided no additional information on hours worked. This was done because the Department cannot estimate effects for these workers since it is unknown whether they work overtime and therefore unknown

whether there would be any need to pay for overtime if their status changed from exempt to nonexempt. The Department reweighted the rest of the sample to account for this change (*i.e.*, to keep the same total employment estimates).<sup>305</sup> 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 vary. The Department believes that without more information this is an appropriate assumption.<sup>306</sup>

## 3. Number of Workers Subject to the FLSA and the Department's Part 541 Regulations

As a starting point for the analysis, based on the CPS MORG data, the Department estimates that there would be 166.2 million wage and salary workers in Year 1. Figure 1 illustrates how the Department analyzed the U.S. civilian workforce through successive stages to estimate the number of affected workers.

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<sup>302</sup> In 2015, RAND released results from a survey conducted to estimate EAP exempt workers. However, this survey does not have the variables or sample size necessary for the Department to base its regulatory impact analysis (RIA) on this analysis. Rohwedder, S. and Wenger, J.B. (2015). The Fair Labor Standards Act: Worker Misclassification and the Hours and Earnings Effects of Expanded Coverage. RAND Labor and Population.

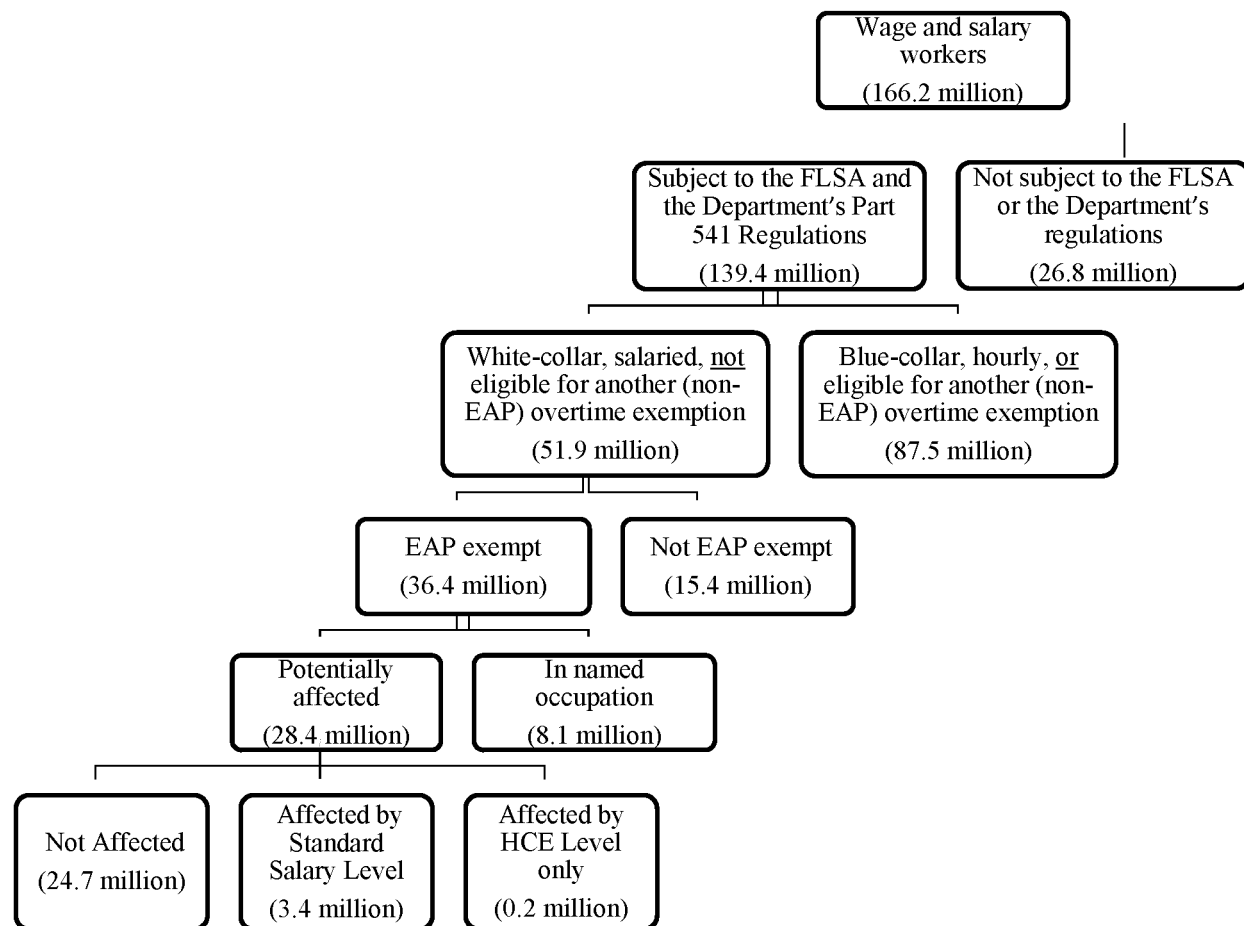
<sup>303</sup> This is the outgoing rotation group (ORG); however, this analysis uses the data merged over 12 months and thus it is referred to as MORG.

<sup>304</sup> Previous rulemakings also adjusted salaries in the pooled data using the CPI-U, but the Department recognizes that the relationship between wage growth and inflation between 2020 and 2022 may not be consistent. During the pandemic, large employment losses in low-wage industries resulted in stronger wage growth at the aggregate level. In the latter part of the 2020–2022 period, high inflation outpaced wage growth. Given these mixed effects, the Department decided to continue its prior practice of adjusting these observations using CPI-U.

<sup>305</sup> The Department also reweighted for workers reporting zero earnings. In addition, the Department eliminated, without reweighting, workers who reported both usually working zero hours and working zero hours in the past week.

<sup>306</sup> 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 4.5 percent. To the extent these excluded workers are exempt, if they tend to work more overtime than other workers, then transfer payments and costs may be underestimated. Conversely, if they work fewer overtime hours, then transfer payments and costs may be overestimated.

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

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The Department first excluded workers who are unemployed, not subject to its regulations, or not covered by the FLSA from the overall total number of wage and salary workers. Excluded workers include military personnel, unpaid volunteers, self-employed individuals, clergy and other religious workers, and Federal employees (with a few exceptions described below).

Many of these workers are excluded from the CPS MORG, including members of the military on active duty and unpaid volunteers. Self-employed and unpaid workers are included in the CPS MORG, but have no earnings data reported and thus are excluded from the analysis. The Department identified religious workers by their occupation codes: 'clergy' (Census occupational code 2040), 'directors, religious activities and education' (2050), and 'religious workers, all other' (2060). Most employees of the Federal Government are covered by the FLSA but not the Department's part 541

regulations because the Office of Personnel Management (OPM) regulates their entitlement to minimum wage and overtime pay.<sup>307</sup> Exceptions exist for U.S. Postal Service employees, Tennessee Valley Authority employees, and Library of Congress employees.<sup>308</sup> The analysis identified and included these covered Federal workers using occupation and/or industry codes and removed other Federal employees.<sup>309</sup>

The FLSA also does not cover employees of firms that have annual revenue of less than \$500,000 and who

<sup>307</sup> See 29 U.S.C. 204(f). Federal workers are identified in the CPS MORG with the class of worker variable PEIO1COW.

<sup>308</sup> See *id.*

<sup>309</sup> Postal Service employees were identified with the Census industry classification for postal service (6370). Tennessee Valley Authority employees were identified as Federal workers employed in the electric power generation, transmission, and distribution industry (570) and in Kentucky, Tennessee, Mississippi, Alabama, Georgia, North Carolina, or Virginia. Library of Congress employees were identified as Federal workers under Census industry 'libraries and archives' (6770) and residing in Washington DC.

are not engaged in interstate commerce. The Department does not exclude them from the analysis, however, because there is no data set that would adequately inform an estimate of the size of this worker population, although the Department believes it is a small percentage of workers. The 2004, 2016, and 2019 final rules similarly did not adjust for these workers.

Of the 166.2 million wage and salary workers in the United States, the Department estimates that 139.4 million are covered by the FLSA and subject to the Department's regulations (83.9 percent). The remaining 26.8 million workers are excluded from FLSA coverage for the reasons described above.

#### 4. Number of Workers Who Are White-Collar, Salaried, Not Eligible for Another (Non-EAP) Overtime Exemption

After limiting the analysis to workers covered by the FLSA and subject to the Department's part 541 regulations,



several other groups of workers were identified and excluded from further analysis since this proposed rule is unlikely to affect them. These include blue-collar workers,<sup>310</sup> workers paid on an hourly basis, and workers who are exempt under certain other (non-EAP) exemptions.

The Department excluded a total of 87.5 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). For example, the Department estimated that there are 47.5 million blue-collar workers. These workers were identified in the CPS MORG data following the methodology from the U.S. Government Accountability Office's (GAO) 1999 white-collar exemptions report<sup>311</sup> and the Department's 2004, 2016, and 2019 regulatory impact analyses.<sup>312</sup> Supervisors in traditionally blue-collar industries were classified as white-collar workers because their duties are generally managerial or administrative, and therefore they were not excluded as blue-collar workers. Using the CPS variable indicating a respondent's hourly wage status, the Department determined that 77.8 million workers were paid on an hourly basis in 2022.<sup>313</sup>

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, they would independently remain exempt from the FLSA's minimum wage and/or overtime pay provisions based on the non-EAP exemptions. The Department excluded an estimated 3.8 million workers, including some agricultural and transportation workers, from further analysis because they are subject to another (non-EAP) overtime exemption. See Appendix A: Methodology for Estimating Exemption Status, contained in the rulemaking docket, for details on how this population was identified.

Agricultural and transportation workers are two of the largest groups of workers excluded from the population of potentially affected EAP workers in the current analysis, and with some exceptions, they were similarly excluded in other recent rulemakings.

The 2004 rule excluded all workers in agricultural industries from the analysis,<sup>314</sup> while more recent analyses only excluded agricultural workers from specified occupational-industry combinations since not all workers in agricultural industries qualify for the agricultural overtime pay exemptions. This proposed rule followed the more recent analyses and only excluded agricultural workers in certain occupation-industry combinations. The exclusion of transportation workers matched the method for the 2004, 2016, and 2019 final rules. Transportation workers are defined as those who are subject to the following FLSA exemptions: section 13(b)(1), section 13(b)(2), section 13(b)(3), section 13(b)(6), or section 13(b)(10). The Department excluded 1.1 million agricultural workers and 2.0 million transportation workers from the analysis.

In addition, the Department excluded another 21,800 workers who qualify for one or more other FLSA minimum wage and overtime exemptions (and are not either blue-collar or hourly). The criteria for determining exemption status for these workers are detailed in Appendix A.

After excluding workers not subject to the Department's FLSA regulations and workers who are unlikely to be affected by this proposed rule (*i.e.*, blue-collar workers, workers paid hourly, workers who are subject to another (non-EAP) overtime exemption), the Department estimated there are 51.9 million salaried white-collar workers for whom employers might claim either the standard EAP exemption or the HCE exemption.

#### 5. Number of Current EAP Exempt Workers

To determine the number of workers for whom employers might currently claim the EAP exemption, the standard EAP test and HCE test were applied. Both tests include earnings thresholds and duties tests. Aside from workers in named occupations (which are not subject to an earnings requirement and are discussed in the next subsection), to be exempt under the standard EAP test, the employee generally 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);<sup>315</sup>

<sup>314</sup> 69 FR 22197.

<sup>315</sup> Some computer employees may be exempt even if they are not paid on a salary basis. Hourly computer employees who earn at least \$27.63 per hour and perform certain duties are exempt under section 13(a)(17) of the FLSA. These workers are

- earn at least a designated salary amount (the standard salary level test, currently \$684 per week); and
- primarily perform exempt work, as defined by the regulations (the standard duties test).

The HCE test allows certain highly paid employees to qualify for exemption if they customarily and regularly perform one or more exempt job duties (the HCE duties test). The current HCE annual compensation level is \$107,432, including at least \$684 per week paid on a salary or fee basis.

#### i. Salary Basis

The Department included only nonhourly workers in the analysis based on CPS data.<sup>316</sup> For this NPRM, the Department considered data representing compensation paid to nonhourly workers to be an appropriate proxy for compensation paid to salaried workers. The Department notes that it made the same assumption regarding nonhourly workers in the 2004, 2016, and 2019 final rules.<sup>317</sup>

The CPS population of "nonhourly" workers includes salaried workers along with those who are paid on a piece-rate, a day-rate, or largely on bonuses or commissions. Data in the CPS are not available to distinguish between salaried workers and these other nonhourly workers. However, the Panel Study of Income Dynamics (PSID) provides additional information on how nonhourly workers are paid.<sup>318</sup> In the PSID, respondents are asked how they are paid on their main job and are also asked for more detail if their response is other than salaried or hourly. Possible responses include piecework, commission, self-employed/farmer/profits, and by the job/day/mile. The Department analyzed the PSID data and found that relatively few nonhourly workers were paid by methods other than salaried. The Department is not aware of any statistically robust source

considered part of the EAP exemptions but were excluded from the analysis because they are paid hourly and will not be affected by this proposed rule (these workers were similarly excluded in the 2004, 2016, and 2019 analyses). 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 proposed rule. Additionally, administrative and professional employees may be paid on a fee basis, as opposed to a salary basis. § 541.605(a). Although the CPS MORG does not identify workers paid on a fee basis, they are considered nonhourly workers in the CPS and consequently are correctly classified as "salaried" (as was done in previous rules).

<sup>316</sup> The CPS variable PEERNHRY identifies workers as either hourly or nonhourly.

<sup>317</sup> See 69 FR 22197; 81 FR 32414; 84 FR 51258.

<sup>318</sup> University of Michigan, Institute for Social Research. 2019 PSID. Data available at: <https://simba.isr.umich.edu/data/data.aspx>.

<sup>310</sup> "The section 13(a)(1) exemptions and the regulations in [Part 541] do not apply to manual laborers or other 'blue collar' workers who perform work involving repetitive operations with their hands, physical skill and energy." § 541.3(a).

<sup>311</sup> GAO/HEHS. (1999). Fair Labor Standards Act: White Collar Exemptions in the Modern Work Place. GAO/HEHS-99-164, 40-41, <https://www.gao.gov/assets/230/228036.pdf>.

<sup>312</sup> See 69 FR 22240-44.

<sup>313</sup> CPS MORG variable PEERNHRY.

that more closely reflects salary as defined in its regulations.

## ii. Salary Level

Weekly earnings are available in the CPS MORG data, which allowed the Department to estimate how many nonhourly workers pass the compensation thresholds.<sup>319</sup> However, the CPS earnings variable does not perfectly reflect the Department's definition of earnings. First, the CPS includes all nondiscretionary bonuses and commissions if they are part of usual weekly earnings. However, the regulation allows nondiscretionary bonuses and commissions to satisfy up to 10 percent of the standard salary level. This discrepancy between the earnings variable used and the regulatory definition of salary may cause a slight overestimation or underestimation of the number of workers estimated to meet the standard salary level and HCE compensation tests.<sup>320</sup> Second, CPS earnings data include overtime pay. 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 accurately in the data. Third, the earnings measure includes tips and discretionary commissions which do not qualify towards the required salary. The Department believes tips are an uncommon form of

payment for these white-collar workers. Discretionary commissions tend to be paid irregularly and hence are unlikely to be counted as "usual earnings." Additionally, as noted above, most salaried workers do not receive commissions.

Lastly, the CPS annual earnings variable is topcoded at \$150,000. Topcoding refers to how data sets handle observations at the top of the distribution. For the CPS annual earnings variable, workers earning above \$2,884.61 (\$150,000 ÷ 52 weeks) per week are reported as earning \$2,884.61 per week. The Department imputed earnings for topcoded workers in the CPS data to adequately estimate impacts.<sup>321</sup>

## iii. Duties

The CPS MORG data do not capture information about job duties. Therefore, the Department used probability estimates of passing the duties test by occupational title to estimate the number of workers passing the duties test. This is the same methodology used in recent part 541 rulemakings, and the Department believes it continues to be the best available methodology. The probabilities of passing the duties test are from an analysis performed by WHD in 1998 in response to a request from the GAO. Because WHD enforces the FLSA's overtime requirements and regularly assesses workers' exempt

status, WHD was uniquely qualified to provide the analysis. The analysis was originally published in the GAO's 1999 white-collar exemptions report.<sup>322</sup>

WHD examined 499 occupational codes and determined that 251 occupational codes likely included EAP exempt workers.<sup>323</sup> For each, WHD assigned one of four probability codes reflecting the estimated likelihood, expressed as ranges, that a worker in that occupation would perform duties required to meet the EAP duties tests (Table 3). All occupations and their associated probability codes are listed in Appendix A. Just as in the 2004, 2016, and 2019 final rules, the Department has supplemented this analysis to account for the HCE exemption. The Department modified the four probability codes to reflect probabilities of passing the HCE duties test based on its analysis of the provisions of the highly compensated test relative to the standard duties test. To illustrate, WHD assigned exempt probability code 4 to the occupation "first-line supervisors/managers of construction trades and extraction workers" (Census code 6200), which indicates that a worker in this occupation has a 0 to 10 percent likelihood of meeting the standard EAP duties test. However, if that worker earned at least \$100,000 annually (now \$107,432 annually), they were assigned a 15 percent probability of passing the more lenient HCE duties test.<sup>324</sup>

TABLE 3—PROBABILITY WORKER IN CATEGORY PASSES THE DUTIES TESTS

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

The occupations identified in GAO's 1999 report map to an earlier occupational classification scheme (the 1990 Census occupational codes).<sup>325</sup> For this proposed rule, the Department used

occupational crosswalks to map the previous occupational codes to the 2018 Census occupational codes, which are used in the CPS MORG 2020 through 2022 data. 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

<sup>319</sup> The CPS MORG variable PRERNWA, which measures weekly earnings, is used to identify weekly salary.

<sup>320</sup> In some instances, this may include too much nondiscretionary bonuses and commissions (*i.e.*, when it is more than 10 percent of usual earnings). But in other instances, it may not include enough nondiscretionary bonuses and commissions (*i.e.*, when the respondent does not count them as usual earnings).

<sup>321</sup> The Department used the standard Pareto distribution approach to impute earnings above the topcoded value as described in Armour, P. and

Burkhauser, R (2013). Using the Pareto Distribution to Improve Estimates of Topcoded Earnings. Center for Economic Studies (CES).

<sup>322</sup> Fair Labor Standards Act: White Collar Exemptions in the Modern Work Place, *supra* note 311, at 40–41.

<sup>323</sup> WHD excluded nine that were not relevant to the analysis for various reasons. For example, 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.

<sup>324</sup> The HCE duties test is used in conjunction with the HCE total annual compensation requirement 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.

<sup>325</sup> Census occupation codes were also updated in 2002 and 2010. References to occupational codes in this analysis refer to the 2002 Census occupational codes. Crosswalks and methodology available at: <https://www.census.gov/topics/employment/industry-occupation/guidance/code-lists.html>.

codes, rounded to the closest probability code.

These codes provide information on the likelihood that an employee met the duties tests, but they do not identify the workers in the CPS MORG who passed the test. For example, for every ten public relations managers, between five and nine are assumed to pass the standard duties test (based on probability category 2). However, it is unknown which of these ten workers are exempt; therefore, for the purposes of producing an estimate, the Department must assign a status to 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.<sup>326</sup>

The Department estimated the probability of qualifying for the standard exemption for each worker as a function of both earnings and the occupation's exempt probability category using a gamma distribution.<sup>327</sup>

<sup>326</sup> 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 rule). Therefore, the gamma model and the linear model would produce similar results for highly compensated workers. See 69 FR 22204–08, 22215–16.

<sup>327</sup> 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).

Based on these revised probabilities, each worker was assigned exempt or nonexempt status based on a random draw from a binomial distribution using the worker's revised probability as the probability of success. Thus, if this method is applied to ten workers who each have a 60 percent probability of being exempt, six workers would be expected to be designated as exempt.<sup>328</sup> For details, *see* Appendix A (in the rulemaking docket).

The Department acknowledges that the probability codes used to determine the share of workers in an occupation who are EAP exempt are 25 years old. However, the Department believes the probability codes continue to estimate exemption status accurately given the fact that the standard duties test is not substantively different from the former short duties tests reflected in the codes. For the 2016 rulemaking, the Department reviewed O\*NET<sup>329</sup> to determine the extent to which the 1998 probability codes reflected current occupational duties. The Department's review of O\*NET verified the continued appropriateness of the 1998 probability codes.<sup>330</sup>

The Department estimates that of the existing 51.9 million salaried white-collar workers considered in the analysis, 36.4 million currently qualify for the EAP exemption.

<sup>328</sup> 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.

<sup>329</sup> The O\*NET database contains hundreds of standardized and occupation-specific descriptors. See <http://www.onetcenter.org>.

<sup>330</sup> 81 FR 32459.

## 6. Potentially Affected Exempt EAP Workers

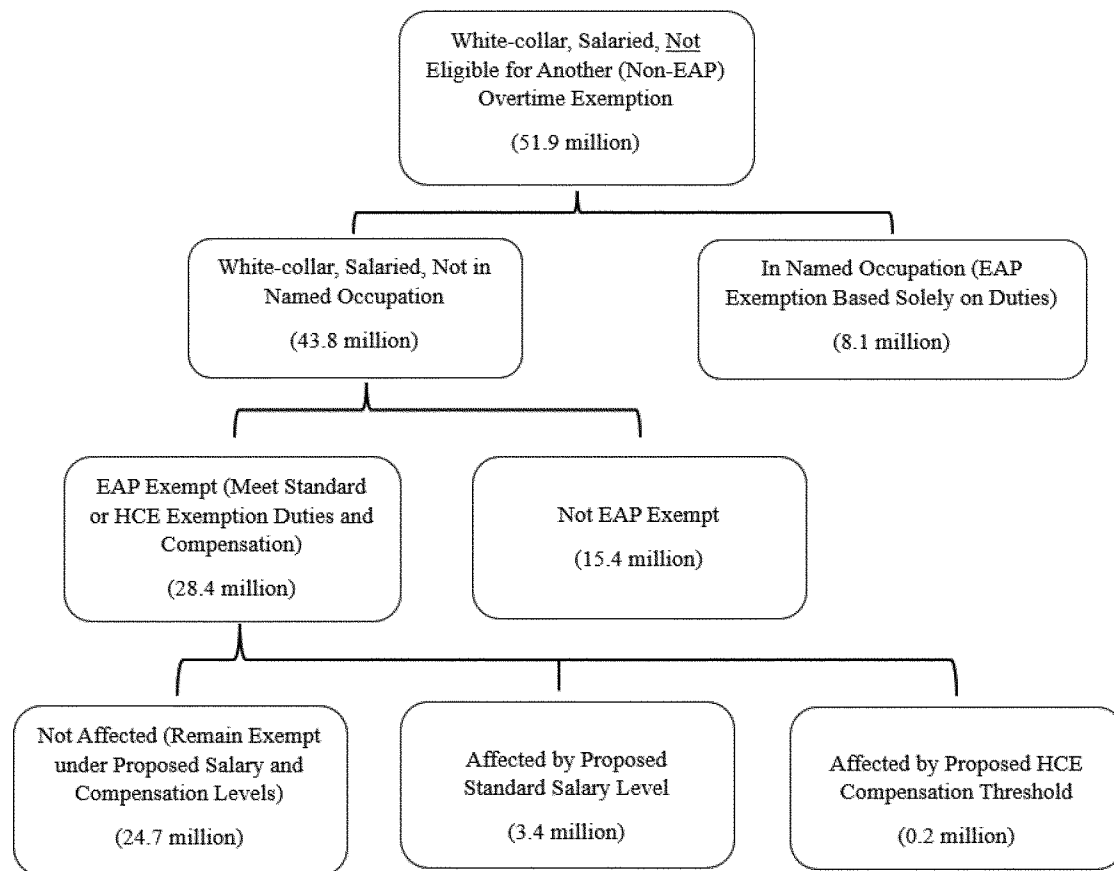
The Department excluded some of the current EAP exempt workers from further analysis because the proposed rule would not affect them. Specifically, the Department excluded workers in named occupations who are not required to pass the salary requirements (although they must still pass a duties test) and therefore whose exemption status does not depend on their earnings. These occupations include physicians (identified with Census occupation codes 3010, 3040, 3060, 3120), lawyers (2100), teachers (occupations 2200–2550 and industries 7860 or 7870), academic administrative personnel (school counselors (occupation 2000 and industries 7860 or 7870) and educational administrators (occupation 0230 and industries 7860 or 7870)), and outside sales workers (a subset of occupation 4950). Out of the 36.4 million workers who were EAP exempt, 8.1 million, or 22.1 percent, were expected to be in named occupations. Thus, the proposed changes to the standard salary level and HCE compensation tests would not affect these workers. The 28.4 million EAP exempt workers remaining in the analysis are referred to in this proposed rule as "potentially affected" (17.1 percent of all workers).

Based on analysis of the occupational codes and CPS earnings data (described above), the Department has concluded there are 28.4 million potentially affected EAP workers.<sup>331</sup>

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<sup>331</sup> Of these workers, approximately 16.0 million pass only the standard test, 11.9 million pass both the standard and the HCE tests, and 420,000 pass only the HCE test.

Figure 2: Exemption Status and Number of Affected Workers



As shown in Figure 2 above, 8.1 million of the 51.9 million salaried white-collar workers are in named occupations and will not be affected by a change in the earnings requirements. The Department also estimates that of the remaining 43.8 million salaried white-collar workers, about 11.7 million earn below the Department's proposed standard salary level of \$1,059 per week and about 32.1 million earn above the Department's proposed salary level.

Thus, approximately 27 percent of salaried white-collar employees earn below the proposed salary level, whereas approximately 73 percent of salaried white-collar employees earn above the salary level and would have their exemption status turn on their job duties.

#### 7. Number of Affected EAP Workers

The Department estimated that the proposed increase in the standard salary level from \$684 per week to \$1,059 per

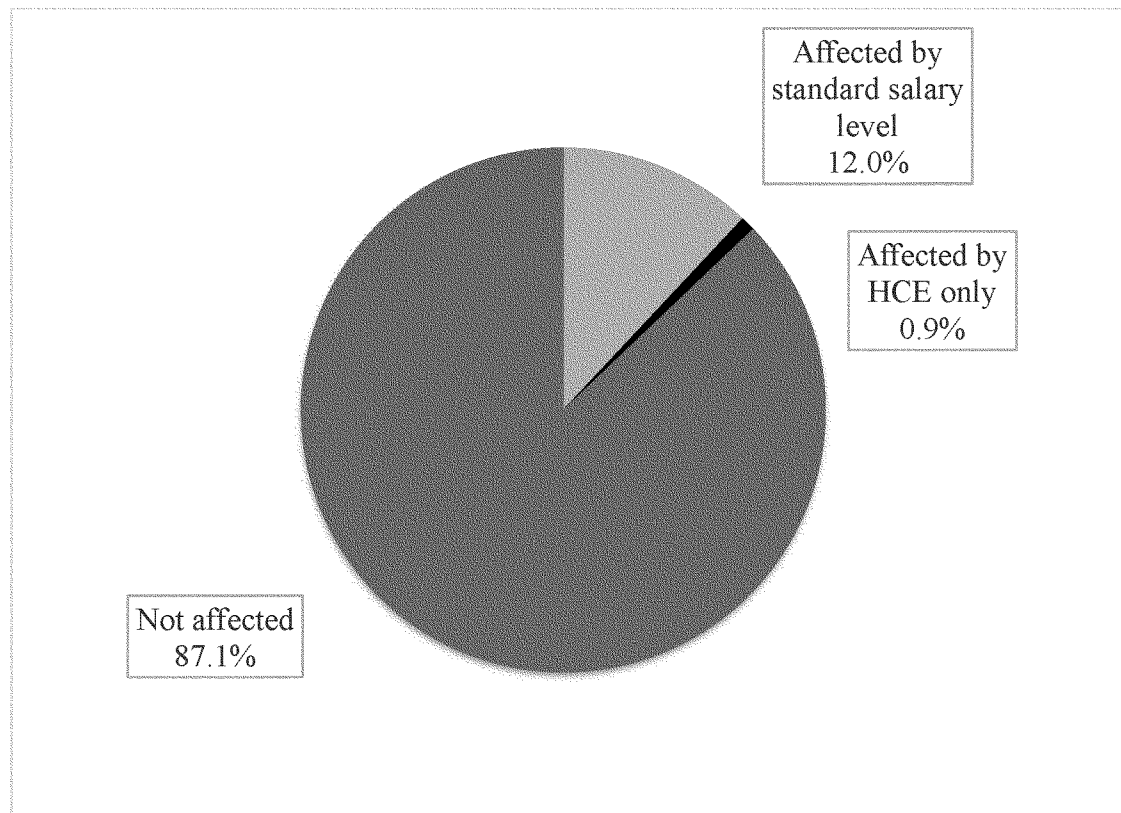
week would affect 3.4 million workers in Year 1 (of these 3.4 million affected employees, 1.8 million earn less than the long test salary level (\$925)).<sup>332</sup> The Department estimated that the proposed increase in the HCE annual compensation level from \$107,432 to \$143,988 would impact 248,900 workers (Figure 3).<sup>333</sup> In total, the Department expects that 3.6 million workers out of the 28.4 million potentially affected workers would be affected in Year 1.

<sup>332</sup> See section VII.C.8 (Alternative 2). As discussed in section IV.A, such employees were always excluded from the EAP exemption prior to 2019, either by the long test salary level itself, or under the 2004 rule salary level, which was equivalent to

the long test salary level. The remaining 1.6 million of these affected employees earn between the long test salary level and the Department's proposed standard salary level.

<sup>333</sup> This group includes workers who may currently be nonexempt under more protective state EAP laws and regulations, such as some workers in Alaska, California, Colorado, Maine, New York, Washington, and Wisconsin.

Figure 3: Pie Chart of Potentially Affected Employees and their Affected Status



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## 8. Supplemental Analysis on the Number of Affected Workers in the Territories

The Department is proposing to apply the standard salary level to all territories that are subject to the Federal minimum wage, including the Commonwealth of the Northern Mariana Islands (CNMI), Guam, Puerto Rico, and the U.S. Virgin Islands, and to update the special salary level for American Samoa in relation to the new standard salary level. In American Samoa, the salary level would be set at 84 percent of the new standard salary level, or \$890 per week (\$1,059 x 84 percent). In the other territories, the salary level would be set at the proposed standard salary level of the 35th percentile of weekly nonhourly earnings in the lowest wage Census region (currently the South), or \$1,059 per week. The salary levels in the territories have not been updated since 2004, when the salary level for Puerto Rico, Guam, the U.S. Virgin Islands, and the CNMI was set to \$455 per week and the salary level for American Samoa was set to \$380 per week. Therefore, the increases in those salary levels will be more pronounced than in the 50 states and the District of Columbia. This may lead to larger impacts resulting from the

increased standard salary level in the territories. Unfortunately, data are not available to conduct a full analysis of impacts in the territories. Therefore, the Department applied reasonable assumptions to the available data to estimate the number of affected workers in the territories.<sup>334</sup>

The CPS data used for the impact analysis does not include data for the territories, and no other data source provides individual level data on earnings, occupation, and pay basis (*i.e.*, hourly or salaried). The Department identified several data sources with pertinent information on the territories:

- BLS Occupational Employment and Wage Statistics (OEWS)
- The Puerto Rico Community Survey
- The Census of Island Areas
- The Economic Census
- County Business Patterns (CBP)

For Puerto Rico, Guam, and the U.S. Virgin Islands the Department used OEWS data.<sup>335</sup> The OEWS does not include American Samoa or the CNMI; the Department used CBP (discussed below) data on the number of workers

for these territories. The Department believes OEWS is more appropriate for this analysis than CBP because it provides the number of white-collar workers and information about earnings, which CBP does not.<sup>336</sup> The Puerto Rico Community Survey provides individual-level earnings information for Puerto Rico that is not available in the OEWS.<sup>337</sup> However, the Department chose to use OEWS because it includes data on additional territories, and to limit the number of data sets used for consistency. The Department welcomes comments on the choice of data set for this analysis, and the overall methodology for estimating the impact on territories. The Department also welcomes recommendations for additional sources of data on workers in the territories.

The OEWS reports the number of workers by detailed occupation, to which the Department applied the

<sup>336</sup> CBP includes total quarterly payroll and the number of employees, but no information about the distribution of these earnings.

<sup>337</sup> The Government Accountability Office assessed the impacts of the 2016 rulemaking in Puerto Rico using the Puerto Rico Community Survey. GAO. (2018). Limited Federal Data Hinder Analysis of Economic Condition and DOL's 2016 Overtime Rule. <https://www.gao.gov/assets/700/693309.pdf>.

<sup>334</sup> The Department was unable to estimate transfer payments in the territories because of the additional assumptions that would be necessary.

<sup>335</sup> OEWS 2022. <https://www.bls.gov/oes/tables.htm>.

probability codes to estimate the number of white-collar workers who meet the duties test requirements for the EAP exemption. The OEWS does not have information on the share of employees in each occupation who are salaried. In order to estimate this share, the Department calculated the share of workers in the 50 states and DC who meet the duties requirement in the CPS

data who are salaried, controlling for the distribution of workers across occupations in each of the three territories.<sup>338</sup> The Department then multiplied the share of workers who meet the duties requirement who are salaried in each occupation by the number of workers who meet the duties requirements in that territory.

The OEWS also reports select percentiles of the earnings distribution for each occupation (10th, 25th, 50th, 75th, and 90th). This allows the Department to estimate an earnings distribution for each occupation and approximate the number of workers who earn between the old and new salary levels.<sup>339</sup> These calculations are summarized in Table 4.

TABLE 4—ESTIMATED NUMBER OF AFFECTED WORKERS IN TERRITORIES USING OEWS

Population or parameter	Puerto Rico	Guam	U.S. Virgin Islands
Workers <sup>a</sup> .....	907,930	51,340	27,860
Workers who meet duties requirements .....	169,241	10,413	5,808
Share of workers meeting duties requirements who are salaried <sup>b,c</sup> .....	54%	60%	57%
Salaried workers meeting duties requirements .....	91,919	6,285	3,333
Share between salary thresholds (\$455–\$1,059) .....	49%	38%	32%
Salaried workers meeting duties requirements between thresholds ( <i>i.e.</i> , affected workers) .....	44,881	2,407	1,071

<sup>a</sup> Limited to wage and salary workers in nonfarm establishments.

<sup>b</sup> Also removes workers unlikely to be impacted by this rulemaking such as workers in named occupations and workers exempt under another non-EAP overtime exemption.

<sup>c</sup> Ratio calculated from CPS data for employees in the 50 states and the District of Columbia while controlling for occupation distribution.

There are several reasons why the estimated number of workers calculated from the OEWS may over or underestimate the true number of affected workers. The Department does not know the size of the biases and so does not know which dominate. First, the share of workers who are salaried in the territories may differ from in the 50 states and the District of Columbia. If the share is higher in the territories than the states, then the Department's approach will underestimate the number of affected workers but overestimate the number if the share is lower. Second, the OEWS is limited to

wage and salary workers in nonfarm establishments which may lead to an undercount of affected workers.<sup>340</sup>

The Department used 2021 CBP data to estimate the number of affected workers in American Samoa and the CNMI. The methodology is largely the same as for the analysis using OEWS data. Table 5 shows estimates using CBP data for all five territories to facilitate a comparison of OEWS and CBP results for Puerto Rico, Guam, and the U.S. Virgin Islands.

CBP provides employment data for each territory. To estimate the number of workers who may be exempt, the

Department calculated the share of workers in the OEWS analysis who meet the duties requirements and are salaried in each of the other three territories and applied that weighted average to American Samoa and the CNMI. The Department also calculated the share of exempt workers who earn between the current and proposed salary thresholds in the three territories covered by the OEWS data and applied them to American Samoa and the CNMI. The Department then multiplied the number of workers by these two shares to estimate the number of affected workers.<sup>341</sup>

TABLE 5—ESTIMATED NUMBER OF AFFECTED WORKERS IN TERRITORIES USING CBP

Population or parameter	Puerto Rico	Guam	U.S. Virgin Islands	American Samoa	CNMI
Workers .....	660,654	49,876	25,652	7,808	12,763
Share who are salaried and meet duties requirements <sup>a</sup> .....	10%	12%	12%	10%	10%
Salaried workers meeting duties requirements .....	66,885	6,106	3,069	803	1,313
Share between salary thresholds <sup>b</sup> .....	49%	38%	32%	48%	48%
Salaried workers meeting duties requirements between thresholds ( <i>i.e.</i> , affected workers) .....	32,657	2,339	986	383	625

<sup>a</sup> Ratio calculated from OEWS data for Puerto Rico, Guam, and U.S. Virgin Islands. Average used for American Samoa and the CNMI. Excludes workers unlikely to be impacted by this rulemaking such as workers in named occupations and workers exempt under another non-EAP overtime exemption.

<sup>b</sup> "Excludes workers unlikely to be impacted by this rulemaking such as workers in named occupations and workers exempt under another non-EAP overtime exemption."

<sup>338</sup> The Department also excluded workers who are unlikely to be affected by this rulemaking, including workers in named occupations and workers exempt under another non-EAP overtime exemption.

<sup>339</sup> The Department interpolated values between the reported percentiles by assuming a uniform distribution for each segment (*e.g.*, between the 10th and the 25th percentiles the Department assumed the earnings distribution is linear). The

Department assumed a minimum value of \$100 and a maximum value of three times the 90th percentile.

<sup>340</sup> In particular, "The OEWS survey excludes the majority of the agricultural sector, with the exception of logging (NAICS 113310), support activities for crop production (NAICS 1151), and support activities for animal production (NAICS 1152). Private households (NAICS 814) also are excluded. OEWS Federal Government data include the U.S. Postal Service and the Federal executive branch only. All other industries, including state

and local government, are covered by the survey." See [https://www.bls.gov/oes/current/oes\\_tec.htm](https://www.bls.gov/oes/current/oes_tec.htm).

<sup>341</sup> American Samoa has lower current and proposed salary thresholds. However, earnings are also lower in American Samoa. Therefore, the Department believes to estimate American Samoa impacts, it is more appropriate to use the salary thresholds in the other territories when applied to wage data for those territories, rather than using the lower American Samoa thresholds combined with the higher earnings data for other territories.

In general, the same potential biases apply here as with the OEWS analysis. However, employment coverage differs slightly between the OEWS and CBP. The CBP excludes government workers (including state and local workers) and covered workers in a few select NAICS, resulting in a downward bias in the number of affected workers.<sup>342</sup> Additionally, the estimates for American Samoa and the CNMI assume the share of workers in these territories who meet the duties requirements and are salaried, and the share of these workers who earn between the current and proposed salary thresholds, are similar to those shares in Puerto Rico, Guam, and the U.S. Virgin Islands.

As a sensitivity analysis, the Department compared the results from the CBP analysis to the OEWS analysis for Puerto Rico, Guam, and the U.S. Virgin Islands. The two estimates of the number of affected workers are within 10 percent for both Guam and the U.S. Virgin Islands. The Puerto Rico estimates differ by a larger amount because the CBP number of workers in Puerto Rico is smaller than the OEWS number due to differences in the covered population. Table 6 includes the estimated number of affected workers by area using the preferred data source for each (i.e., OEWS for Puerto Rico, Guam, and U.S. Virgin Islands and CBP for

American Samoa and the CNMI). The share of workers affected by the rule ranges from 3.8 to 4.9 percent for each territory, with an average of 4.9 percent over all territories, which is higher than the average of 2.2 percent estimated for the 50 states and the District of Columbia. The effect is larger in the territories than the states for two reasons. First, the increase in salary level will be larger since the salary level wasn't increased for these territories in the 2019 rulemaking. Second, earnings tend to be lower in the territories, and so more workers may fall within the impacted salary range.

TABLE 6—SUMMARY OF NUMBER OF AFFECTED WORKERS BY TERRITORY

Territory	All workers	Number of affected workers	Affected as share of all workers (%)
Puerto Rico .....	907,930	44,881	4.9
Guam .....	51,340	2,407	4.7
U.S. Virgin Islands .....	27,860	1,071	3.8
American Samoa .....	7,808	383	4.9
CNMI .....	12,763	625	4.9
Total .....	1,007,701	49,367	4.9

Although the share of affected workers to total workers in the territories is larger, these workers still comprise only a fraction of the workforce. As is true for the mainland U.S., the Department believes that many of these workers are unlikely to work regular overtime. The Department welcomes comments and data on the prevalence of overtime work in the territories. The Department has not included this supplemental estimate of affected workers in the territories in the larger analysis of affected workers due to the limitations of the estimates and the inability to estimate transfers. Even if this supplemental estimate were to be included in the broader analysis, the total number of affected workers would be little changed, as the number of affected workers in the territories (49,367) is less than 1.5% of our affected workers estimate (3.6 million).

*C. Effects of Revised Salary and Compensation Levels*

1. Overview and Summary of Quantified Effects

The Department is proposing to set the standard salary level using the 35th percentile of earnings of full-time salaried workers in the lowest-wage Census region (currently the South) and to set the HCE compensation level at the annualized weekly earnings of the 85th percentile of full-time salaried workers nationwide. In both cases the Department used 2022 CPS data to calculate the levels.<sup>343</sup> The levels presented in this analysis are likely lower than the corresponding levels would be at the time a final rule is published, given that the Department would use the most recent data available. However, the economic impacts estimated here are an appropriate proxy for the effects likely to occur at the time of implementation if the proposal is finalized. Both transfers from employers to employees and between employees, and direct employer costs, would depend on

how employers respond to this rulemaking. Employer response is expected to vary by the characteristics of the affected EAP workers. Assumptions related to employer responses are discussed below. Table 7 presents the estimated number of affected workers, costs, and transfers associated with increasing the standard salary and HCE compensation levels. The Department estimated that the direct employer costs of this proposed rule, if finalized, would total \$1.2 billion in the first year, with 10-year annualized direct costs of \$664 million per year using a 7 percent discount rate. In addition to these direct costs, this proposed rule would transfer income from employers to employees. Estimated Year 1 transfers would equal \$1.2 billion, with annualized transfers of \$1.3 billion per year using both the 3 percent and 7 percent real discount rates. Potential employer costs due to reduced profits and additional hiring were not quantified but are discussed in section VII.C.3.v.

<sup>342</sup> In particular, “CBP covers most NAICS industries excluding crop and animal production; rail transportation; Postal Service; pension, health, welfare, and vacation funds; trusts, estates, and

agency accounts; office of notaries; private households; and public administration. CBP also excludes most establishments reporting government

employees.” See <https://www.census.gov/programs-surveys/cbp/about.html>.  
<sup>343</sup> Full-time is defined as 35 or more hours per week.



TABLE 7—SUMMARY OF AFFECTED WORKERS AND REGULATORY COSTS AND TRANSFERS

Impact <sup>a</sup>	Year 1	Future years <sup>b</sup>		Annualized value	
		Year 2	Year 10	3% Real discount rate	7% Real discount rate
Affected Workers (1,000s)					
Standard .....	3,399	2,999	4,288	( <sup>c</sup> )	( <sup>c</sup> )
HCE .....	249	269	769	( <sup>c</sup> )	( <sup>c</sup> )
Total .....	3,648	3,268	5,057	( <sup>c</sup> )	( <sup>c</sup> )
Direct Employer Costs (Millions in \$2022)					
Regulatory familiarization .....	\$427.2	\$0.0	\$65.1	\$67.9	\$75.0
Adjustment <sup>c</sup> .....	\$240.8	\$8.1	\$15.0	\$35.7	\$40.0
Managerial .....	\$534.9	\$500.2	\$667.9	\$552.8	\$548.5
Total direct costs <sup>d</sup> .....	\$1,202.8	\$508.3	\$748.0	\$656.4	\$663.6
Transfers from Employers to Workers (Millions in \$2022) <sup>e</sup>					
Due to minimum wage .....	\$48.6	\$27.1	\$17.2	\$25.2	\$25.9
Due to overtime pay .....	\$1,185.6	\$921.8	\$1,963.9	\$1,292.9	\$1,268.5
Total transfers <sup>f</sup> .....	\$1,234.2	\$949.0	\$1,981.2	\$1,318.1	\$1,294.3

<sup>a</sup> Additional costs and benefits of the rule that could not be quantified or monetized are discussed in the text.

<sup>b</sup> These costs/transfers represent a range over the nine-year span.

<sup>c</sup> Not annualized.

<sup>d</sup> Adjustment costs occur in all years when there are newly affected workers. Adjustment costs may occur in years without updated earnings thresholds because some workers' projected earnings are estimated using negative earnings growth.

<sup>e</sup> Components may not add to total due to rounding.

<sup>f</sup> This is the net transfer from employers to workers. There may also be transfers between workers.

## 2. Characteristics of Affected EAP Workers

Table 8 presents the number of affected EAP workers, the mean number of overtime hours they work per week, and their average weekly earnings. The Department considered two types of overtime workers in this analysis: regular overtime workers and occasional overtime workers.<sup>344</sup> Regular overtime workers typically worked more than 40 hours per week. Occasional overtime workers typically worked 40 hours or less per week, but they worked more than 40 hours in the week they were surveyed. The Department considered these two populations separately in the analysis because labor market responses to overtime pay requirements may differ for these two types of workers.

The 3.4 million workers affected by the increase in the standard salary level work on average 1.6 usual hours of overtime per week and earn on average

\$914 per week.<sup>345</sup> However, most of these workers (about 85 percent) usually do not work overtime. The 15 percent of affected workers who usually work overtime average 11.0 hours of overtime per week. In a representative week, roughly 121,000 (or 3.6%) of the 3.4 million affected workers occasionally work overtime; they averaged 8.7 hours of overtime in the weeks they worked overtime.<sup>346</sup> Finally, 8,000 (or 0.2%) of all workers affected by the increase in the salary level earn less than the minimum wage.

The 248,900 workers affected by the change in the HCE compensation level average 3.1 hours of overtime per week and earn an average of \$2,355 per week (\$122,460 per year). About 72 percent of these workers do not usually work overtime, while the 28 percent who usually work overtime average 11.1 hours of overtime per week. Among the 3.8% who occasionally work overtime,

they averaged 12.7 hours in the weeks that they worked overtime.

Although most affected workers who typically do not work overtime would be unlikely to experience significant changes in their daily work routine, those who regularly work overtime may experience significant changes. Moreover, affected EAP workers who routinely work overtime and earn less than the minimum wage would be most likely to experience significant changes.<sup>347</sup>

Employers might respond by paying overtime premiums; reducing or eliminating overtime hours; reducing employees' regular wage rates to keep overall compensation consistent (provided that the reduced rates still exceed the minimum wage); increasing employees' salaries to the updated earnings threshold to preserve their exempt status;<sup>348</sup> or using some combination of these responses.

<sup>344</sup> Regular overtime workers were identified in the CPS MORG with variable PEHRUSL1. Occasional overtime workers were identified with variables PEHRUSL1 and PEHRACT1.

<sup>345</sup> CPS defines "usual hours" as hours worked 50 percent or more of the time.

<sup>346</sup> This group represents the number of workers with occasional overtime hours in the week the CPS MORG survey was conducted. Because the survey week is a representative week, the Department

believes the prevalence of occasional overtime in the survey week and the characteristics of these workers are representative of other weeks (even though a different group of workers would be identified as occasional overtime workers in a different week).

<sup>347</sup> A small proportion (0.2 percent) of affected EAP workers earn implicit hourly wages that are less than the applicable minimum wage (the higher of the state or Federal minimum wage). The implicit hourly wage is calculated as total weekly earnings

divided by total weekly hours worked. For example, workers earning the \$684 per week standard salary level would earn less than the Federal minimum wage if they work 95 or more hours in a week (\$684 ÷ 95 hours = \$7.20 per hour).

<sup>348</sup> Increasing employees' salaries to the updated salary level would be less common for affected workers earning below the minimum wage and more generally would be inversely correlated with baseline salary and compensation.

TABLE 8—NUMBER OF AFFECTED EAP WORKERS, MEAN OVERTIME HOURS, AND MEAN WEEKLY EARNINGS, YEAR 1

Type of affected EAP worker	Affected EAP workers <sup>a</sup>		Mean overtime hours	Mean usual weekly earnings
	Number (1,000s)	% of total		
Standard Salary Level				
All affected EAP workers .....	3,399	100	1.6	\$914
Earn less than the minimum wage <sup>b</sup> .....	8	0.2	33.2	809
Regularly work overtime .....	494	14.5	11.0	917
Occasionally work overtime <sup>c</sup> .....	121	3.6	8.7	914
HCE Compensation Level				
All affected EAP workers .....	249	100	3.1	2,355
Earn less than the minimum wage <sup>b</sup> .....	70	28.3	11.1	2,332
Regularly work overtime .....	9	3.8	12.7	2,347
Occasionally work overtime <sup>c</sup> .....				

**Note:** Pooled CPS data for 2020–2022 adjusted to reflect 2022.

<sup>a</sup> Estimated number of workers exempt under the EAP exemptions who will be entitled to overtime protection under the updated salary levels (if their weekly earnings do not increase to the new salary levels).

<sup>b</sup> The applicable minimum wage is the higher of the Federal minimum wage and the state minimum wage. These workers all regularly work overtime and are also included in that row. HCE workers will not be affected by the minimum wage provision.

<sup>c</sup> 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.

This section characterizes the population of affected workers by industry, occupation, employer type, location of residence, and demographics. The Department chose to provide as much detail as possible while maintaining adequate sample sizes.

Table 9 presents the distribution of affected EAP workers by industry and occupation, using Census industry and occupation codes. The industry with the most affected EAP workers is professional and business services (687,000), while the industry with the highest percentage of EAP workers affected is agriculture, forestry, fishing,

and hunting (about 22 percent). The occupational category with the most affected EAP workers is management, business, and financial (1.6 million), while the occupation category with the highest percentage of EAP workers affected is services (about 31 percent).

Potentially affected workers in private-sector nonprofits are more likely to be affected than workers in private-sector for-profit firms (16.8 percent compared with 12.0 percent). However, as discussed in section VII.B.3, the estimates of workers subject to the FLSA include workers employed by enterprises that are not subject to the FLSA under the law's enterprise

coverage requirements because there is no data set that would adequately inform an estimate of the size of this worker population in order to exclude them from these estimates. Although failing to exclude workers who work for non-covered enterprises would only affect a small percentage of workers generally, it may have a larger effect (and result in a larger overestimate) for workers in nonprofits because when determining FLSA enterprise coverage only revenue derived from business operations, not charitable activities, is included.

TABLE 9—ESTIMATED NUMBER OF EXEMPT WORKERS WITH THE CURRENT AND PROPOSED SALARY LEVELS, BY INDUSTRY AND OCCUPATION, YEAR 1

Industry/occupation/nonprofit	Workers subject to FLSA (millions)	Potentially affected EAP workers (millions) <sup>a</sup>	Not-affected (millions) <sup>b</sup>	Affected (millions) <sup>c</sup>	Affected as share of potentially affected (%)
Total .....	139.40	28.36	24.71	3.65	12.9
<b>By Industry <sup>d</sup></b>					
Agriculture, forestry, fishing, & hunting .....	1.33	0.06	0.04	0.01	22.1
Mining .....	0.62	0.17	0.16	0.01	7.3
Construction .....	8.91	1.19	1.03	0.15	13.0
Manufacturing .....	15.13	3.90	3.58	0.32	8.1
Wholesale trade .....	3.23	0.85	0.75	0.10	12.2
Retail trade .....	15.38	1.85	1.54	0.31	16.7
Transportation & utilities .....	8.51	1.03	0.91	0.12	11.5
Information .....	2.56	0.96	0.84	0.12	12.3
Financial activities .....	9.85	4.25	3.77	0.48	11.3
Professional & business services .....	16.78	6.75	6.07	0.69	10.2
Education .....	14.02	1.12	0.92	0.202	18.0
Healthcare & social services .....	20.53	3.60	2.97	0.627	17.4
Leisure & hospitality .....	11.60	0.87	0.69	0.18	21.1
Other services .....	5.31	0.74	0.60	0.14	18.9

TABLE 9—ESTIMATED NUMBER OF EXEMPT WORKERS WITH THE CURRENT AND PROPOSED SALARY LEVELS, BY INDUSTRY AND OCCUPATION, YEAR 1—Continued

Industry/occupation/nonprofit	Workers subject to FLSA (millions)	Potentially affected EAP workers (millions) <sup>a</sup>	Not-affected (millions) <sup>b</sup>	Affected (millions) <sup>c</sup>	Affected as share of potentially affected (%)
Public administration .....	5.63	1.01	0.83	0.18	18.0
<b>By Occupation <sup>d</sup></b>					
Management, business, & financial .....	23.57	14.56	12.91	1.65	11.3
Professional & related .....	34.77	10.18	8.92	1.26	12.4
Services .....	21.84	0.13	0.09	0.04	31.0
Sales and related .....	12.63	2.36	1.95	0.41	17.5
Office & administrative support .....	15.81	0.93	0.67	0.26	28.1
Farming, fishing, & forestry .....	0.93	0.00	0.00	0.00	0.00
Construction & extraction .....	6.72	0.03	0.02	0.01	19.6
Installation, maintenance, & repair .....	4.53	0.04	0.04	0.00	6.4
Production .....	7.98	0.09	0.08	0.01	12.3
Transportation & material moving .....	10.60	0.04	0.04	0.01	13.5
<b>By Nonprofit and Government Status</b>					
Nonprofit, private .....	9.80	2.27	1.89	0.38	16.8
For profit, private .....	110.90	23.90	21.03	2.87	12.0
Government (state, local, and Federal) .....	18.70	2.20	1.80	0.40	18.1

**Note:** Pooled CPS data for 2020–2022 adjusted to reflect 2022.

<sup>a</sup> Exempt workers who are white-collar, salaried, not eligible for another (non-EAP) overtime exemption, and not in a named occupation.

<sup>b</sup> Workers who continue to be exempt after the increases in the salary levels (assuming affected workers earning below the new salary level do not have their weekly earnings increased to the new level).

<sup>c</sup> Estimated number of workers exempt under the EAP exemptions who will be entitled to overtime protection under the updated salary levels (if their weekly earnings do not increase to the new salary levels).

<sup>d</sup> Census industry and occupation categories.

Table 10 presents the distribution of affected EAP workers based on Census Regions and Divisions, and metropolitan statistical area (MSA) status. The region with the most affected workers will be the South (1.5 million), but the South's percentage of potentially affected workers who are estimated to be affected is relatively small (15.2 percent). Although 90 percent of affected EAP workers will reside in MSAs (3.28 of 3.65 million), so do a

corresponding 88 percent of all workers subject to the FLSA.<sup>349</sup>

Employers in low-wage industries, regions, and in non-metropolitan areas may be more affected because they typically pay lower wages and salaries. The Department believes the salary level included in this proposed rule is appropriate for these lower-wage sectors, in part because the proposed methodology uses earnings data from the lowest-wage census region. Moreover, the duties test would

continue to determine exemption status for the vast majority of workers in low-wage regions and industries under the proposed rule. For example, as displayed in Table 10, 84.8 percent of potentially affected EAP workers in the South Census Region earn more than the proposed salary level and thus would not be affected by the proposed rule (8.39 ÷ 9.89). Effects by region and industry are considered in section VII.C.7.

TABLE 10—ESTIMATED NUMBER OF EXEMPT WORKERS WITH THE CURRENT AND PROPOSED SALARY LEVELS, BY REGION, DIVISION, AND MSA STATUS, YEAR 1

Region/division/metropolitan status	Workers subject to FLSA (millions)	Potentially affected EAP workers (millions) <sup>a</sup>	Not-affected (millions) <sup>b</sup>	Affected (millions) <sup>c</sup>	Affected as share of potentially affected (%)
Total .....	139.40	28.36	24.71	3.65	12.9
<b>By Region/Division</b>					
<i>Northeast</i> .....	24.75	5.74	5.10	0.64	11.1
New England .....	6.83	1.71	1.54	0.17	9.9
Middle Atlantic .....	17.92	4.03	3.56	0.47	11.6
<i>Midwest</i> .....	30.39	5.87	5.07	0.80	13.7
East North Central .....	20.47	4.01	3.48	0.53	13.3
West North Central .....	9.92	1.86	1.59	0.27	14.6
<i>South</i> .....	51.42	9.89	8.39	1.50	15.2

<sup>349</sup> Identified with CPS MORG variable GTMETSTA.

TABLE 10—ESTIMATED NUMBER OF EXEMPT WORKERS WITH THE CURRENT AND PROPOSED SALARY LEVELS, BY REGION, DIVISION, AND MSA STATUS, YEAR 1—Continued

Region/division/metropolitan status	Workers subject to FLSA (millions)	Potentially affected EAP workers (millions) <sup>a</sup>	Not-affected (millions) <sup>b</sup>	Affected (millions) <sup>c</sup>	Affected as share of potentially affected (%)
South Atlantic .....	26.76	5.50	4.68	0.81	14.8
East South Central .....	7.69	1.22	1.00	0.22	18.3
West South Central .....	16.97	3.18	2.71	0.47	14.7
West .....	32.83	6.86	6.15	0.70	10.3
Mountain .....	10.73	2.07	1.79	0.28	13.7
Pacific .....	22.10	4.78	4.36	0.42	8.8
<b>By Metropolitan Status</b>					
Metropolitan .....	122.92	26.61	23.33	3.28	12.3
Non-metropolitan .....	15.47	1.62	1.28	0.34	20.8
Not identified .....	1.01	0.13	0.10	0.03	22.1

**Note:** Pooled CPS data for 2020–2022 adjusted to reflect 2022.

<sup>a</sup> Exempt workers who are white-collar, salaried, not eligible for another (non-EAP) overtime exemption, and not in a named occupation.

<sup>b</sup> Workers who continue to be exempt after the increases in the salary levels (assuming affected workers earning below the new salary level do not have their weekly earnings increased to the new level).

<sup>c</sup> Estimated number of workers exempt under the EAP exemptions who will be entitled to overtime protection under the updated salary levels (if their weekly earnings do not increase to the new salary levels).

Table 11 presents the distribution of affected EAP workers by demographics. Potentially affected women, Black workers, Hispanic workers, young workers, and workers with less education are all more likely to be affected than other worker types. This is because EAP exempt workers with these characteristics are more likely to earn within the affected standard salary range than EAP exempt workers without these characteristics. For example, of potentially affected workers, women tend to have lower salaries and are

therefore more likely to be in the affected range. Median weekly earnings for potentially affected women are \$1,649 compared to \$2,074 for men.

Among potentially affected workers, certain demographic groups—women, Black workers, Hispanic workers, young workers, and workers with less education—have an increased likelihood of being affected by this rulemaking, even though workers in these demographic groups are less likely to be EAP exempt in the first place. Therefore, as a share of all workers, not

just potentially affected workers, workers in these demographic groups may not be more likely to be affected. For example, when looking at potentially affected workers, 19.7 percent of potentially affected Black workers are affected, while only 12.7 percent of potentially affected white workers are affected. However, when looking at total workers, about the same shares of total Black and total white workers would be affected (2.5 percent of Black workers and 2.6 percent of white workers).

TABLE 11—ESTIMATED NUMBER OF EXEMPT WORKERS WITH THE CURRENT AND PROPOSED SALARY LEVELS, BY DEMOGRAPHICS, YEAR 1

Demographic	Workers subject to FLSA (millions)	Potentially Affected EAP Workers (millions) <sup>a</sup>	Not-Affected (millions) <sup>b</sup>	Affected (millions) <sup>c</sup>	Affected as share of all workers (%)	Affected as share of potentially affected (%)
Total .....	139.40	28.36	24.71	3.65	2.6	12.9
<b>By Sex</b>						
Male .....	72.15	16.62	15.04	1.57	2.2	9.5
Female .....	67.25	11.74	9.67	2.08	3.1	17.7
<b>By Race</b>						
White only .....	107.29	22.05	19.25	2.80	2.6	12.7
Black only .....	17.66	2.26	1.82	0.44	2.5	19.7
All others .....	14.45	4.05	3.65	0.40	2.8	9.9
<b>By Ethnicity</b>						
Hispanic .....	25.66	2.57	2.15	0.42	1.6	16.3
Not Hispanic .....	113.74	25.79	22.56	3.23	2.8	12.5
<b>By Age</b>						
16–25 .....	21.21	1.28	0.92	0.36	1.7	28.3
26–35 .....	33.47	7.17	6.06	1.11	3.3	15.5

TABLE 11—ESTIMATED NUMBER OF EXEMPT WORKERS WITH THE CURRENT AND PROPOSED SALARY LEVELS, BY DEMOGRAPHICS, YEAR 1—Continued

Demographic	Workers subject to FLSA (millions)	Potentially Affected EAP Workers (millions) <sup>a</sup>	Not-Affected (millions) <sup>b</sup>	Affected (millions) <sup>c</sup>	Affected as share of all workers (%)	Affected as share of potentially affected (%)
36–45 .....	29.84	7.49	6.68	0.81	2.7	10.9
46–55 .....	27.37	6.73	6.02	0.72	2.6	10.6
56+ .....	27.50	5.69	5.04	0.65	2.4	11.4
<b>By Education</b>						
No degree .....	10.35	0.13	0.09	0.05	0.4	35.1
High school diploma .....	58.01	4.56	3.58	0.98	1.7	21.4
Associate's degree .....	14.70	1.91	1.54	0.37	2.5	19.6
Bachelor's degree .....	35.80	13.61	12.02	1.59	4.4	11.7
Master's degree .....	15.52	6.80	6.24	0.56	3.6	8.3
Professional degree .....	2.03	0.38	0.35	0.04	1.8	9.3
PhD .....	2.98	0.98	0.91	0.07	2.3	7.2

**Note:** Pooled CPS data for 2020–2022 adjusted to reflect 2022.

<sup>a</sup> Exempt workers who are white-collar, salaried, not eligible for another (non-EAP) overtime exemption, and not in a named occupation.

<sup>b</sup> Workers who continue to be exempt after the increases in the salary level (assuming affected workers' weekly earnings do not increase to the new salary level).

<sup>c</sup> 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 level).

### 3. Costs

#### i. Summary

The Department quantified three direct costs to employers in this analysis: (1) regulatory familiarization costs; (2) adjustment costs; and (3) managerial costs. These are the same

costs quantified in the 2016 and 2019 rulemakings. The Department estimated that in Year 1, regulatory familiarization costs would be \$427.2 million, adjustment costs would be \$240.8 million, and managerial costs would be \$534.9 million (Table 12). Total direct

employer costs in Year 1 would be \$1.2 billion. Recurring costs are projected in section VII.C.10. The Department discusses costs that are not quantified in section VII.C.3.v. The Department welcomes comments on its cost estimates.

TABLE 12—SUMMARY OF YEAR 1 DIRECT EMPLOYER COSTS  
[millions]

Direct employer costs	Standard salary level	HCE compensation level	Total
Regulatory familiarization <sup>a</sup> .....	.....	.....	\$427.2
Adjustment .....	\$224.4	\$16.4	240.8
Managerial .....	485.5	49.4	534.9
Total direct costs .....	709.8	65.9	1,202.8

<sup>a</sup> Regulatory familiarization costs are assessed jointly for the proposed change in the standard salary level and the HCE compensation level.

#### ii. Regulatory Familiarization Costs

This rulemaking would impose direct costs on firms by requiring them to review the regulation. To estimate these “regulatory familiarization costs,” three pieces of information must be estimated: (1) the number of affected establishments; (2) a wage level for the employees reviewing the rule; and (3) the amount of time spent reviewing the rule. The Department generally used the same methodology for calculating regulatory familiarization costs that it used in recent rulemakings.

Regulatory familiarization costs can be calculated at an establishment level or at a firm level. The Department assumed that regulatory familiarization occurs at a decentralized level and used the number of establishments in its cost

estimate; this results in a higher estimate than would result from using the number of firms. The most recent data on private sector establishments and firms at the time this proposed rule was drafted are from the 2020 Statistics of U.S. Businesses (SUSB), which reports 8.00 million establishments with paid employees.<sup>350</sup> Additionally, there were an estimated 90,126 state and local governments in 2017, the most recent data available.<sup>351</sup> The Department thus estimated 8.09 million entities (the term entity is used to refer to the combination of establishments and governments).

<sup>350</sup> Statistics of U.S. Businesses 2020, <https://www.census.gov/programs-surveys/susb.html>.

<sup>351</sup> 2017 Census of Governments. Table 1, <https://www.census.gov/data/tables/2017/econ/gus/2017-governments.html>.

The Department assumes that all entities would incur some regulatory familiarization costs, even if they do not employ exempt workers, because all entities would need to confirm whether this rulemaking affects their employees. Entities with more affected EAP workers would likely spend more time reviewing the regulation than entities with fewer or no affected EAP workers (since a more careful reading of the regulation will probably follow the initial decision that the entity is affected). However, the Department did not know the distribution of affected EAP workers across entities, so it used an average cost per entity.

The Department believes an average of one hour per entity is appropriate because the regulated community is

likely to be familiar with the content of this rulemaking. EAP exemptions have existed in one form or another since 1938, and a final rule was published as recently as 2019. Furthermore, employers who use the exemptions must apply them every time they hire an employee whom they seek to classify as exempt. Thus, employers should be familiar with the exemptions. The most significant changes in this proposed rulemaking are setting a new standard salary level and a new HCE compensation level for exempt workers and establishing a mechanism for keeping these thresholds up to date. The changed regulatory text is only a few pages, and the Department will provide summaries and other compliance assistance materials that will help inform employers that are implementing the final rule. The Department thus believes, consistent with its approach in the 2016 and 2019 rules, that one hour is an appropriate average estimate for the time each entity would spend reviewing the changes made by this rulemaking. Additionally, the estimated 1 hour for regulatory familiarization represents an assumption about the average for all entities in the U.S., even those without any affected or exempt workers, which are unlikely to spend much time reviewing the rulemaking. Some businesses, of course, would spend more than 1 hour, and some would spend less.

The Department's analysis assumes that compensation, benefits, and job analysis specialists (SOC 13-1141) with a median wage of \$32.59 per hour would review the rulemaking.<sup>352 353</sup> The Department also assumed that benefits are paid at a rate of 45 percent of the base wage<sup>354</sup> and overhead costs are paid at a rate of 17 percent of the base wage,<sup>355</sup> resulting in an hourly rate of \$52.80. The Department thus estimates regulatory familiarization costs in Year 1 would be \$427.2 million (\$52.80 per hour × 1 hour × 8.09 million entities).

The Department also conducted a sensitivity analysis. First, as previously noted, the Department used the number of establishments rather than the number of firms, which results in a higher estimate of the regulatory familiarization cost. Using the number of firms, 6.2 million, would result in a reduced regulatory familiarization cost estimate of \$329.0 million in Year 1.

#### iii. Adjustment Costs

This rulemaking would also impose direct costs on establishments by requiring them to evaluate the exemption status of employees, update and adapt overtime policies, notify employees of policy changes, and adjust their payroll systems. The Department believes the size of these "adjustment costs" would depend on the number of affected EAP workers and would occur in any year when exemption status is changed for any workers. To estimate adjustment costs, three pieces of information must be estimated: (1) a wage level for the employees making the adjustments; (2) the amount of time spent making the adjustments; and (3) the estimated number of newly affected EAP workers. The Department again estimated that the average wage with benefits and overhead costs for a mid-level human resource worker is \$52.80 per hour (as explained above).

The Department estimated that it would take establishments an average of 75 minutes per affected worker to make the necessary adjustments. This is the same time estimate as used in the 2016 and 2019 rulemakings. Little applicable data were identified from which to estimate the amount of time required to make these adjustments. The estimated number of affected EAP workers in Year 1 is 3.6 million (as discussed in section VII.B.7). Therefore, total estimated Year 1 adjustment costs would be \$240.8 million ( $\$52.80 \times 1.25 \text{ hours} \times 3.6 \text{ million workers}$ ).

The Department notes that the 75-minute-per-worker average time estimate is an assumption about the average across all workers. This estimate assumes that the time is focused on analyzing more complicated situations. For example, employers are likely to incur relatively low adjustment costs for some workers, such as those who work no overtime (described below as Type 1 workers). This leaves more time for employers to spend on adjustment costs for workers who work overtime either occasionally or regularly. To demonstrate, if the aggregate time spent on adjustments (75 min × 3.6 million workers) was spread out over only workers who regularly work overtime,

then the time estimate is 4.4 hours per worker.

The Department used a time estimate per affected worker, rather than per establishment, because the distribution of affected workers across establishments is unknown. However, it may be helpful to present the total time estimate per establishment based on a range of affected workers. If an establishment has five affected workers, the time estimate for adjustment costs is 6.25 hours. If an establishment has 25 affected workers, the time estimate for adjustment costs is 31.25 hours. And if an establishment has 50 affected workers, the time estimate for adjustment costs is 62.5 hours.

A reduction in the cost to employers of determining employees' exemption status may partially offset adjustment costs. Currently, to determine whether an employee is exempt, employers must apply the duties test to salaried workers who earn \$684 or more per week. However, when the rule takes effect, firms would no longer be required to apply the duties test to employees earning less than the new standard salary level. While this would be a clear cost savings to employers for these employees, the Department did not estimate the potential size of this cost savings.

#### iv. Managerial Costs

If an employee becomes nonexempt due to the changes in the salary levels, then firms may incur ongoing managerial costs because the employer may spend more time developing work schedules and closely monitoring an employee's hours to minimize or avoid paying that employee overtime. For example, the manager of a newly nonexempt worker may have to assess whether the marginal benefit of scheduling the worker for more than 40 hours exceeds the marginal cost of paying the overtime premium. Additionally, the manager may have to spend more time monitoring the employee's work and productivity since the marginal cost of employing the worker per hour has increased. Unlike regulatory familiarization and adjustment costs, which occur primarily in Year 1, managerial costs are incurred more uniformly every year.

The Department applied managerial costs to workers who (1) become nonexempt, overtime-protected and (2) either regularly work overtime or occasionally work overtime, but on a predictable basis—an estimated 738,000 workers (see Table 16 and accompanying explanation). Consistent with its approach in its 2019 rule, the Department assumed that management

<sup>352</sup> OEWS 2022. Available at: <https://www.bls.gov/oes/current/oes131141.htm>.

<sup>353</sup> Previous related rulemakings used the CPS to estimate wage rates. The Department is using OEWS data now to conform with standard practice for the Department's economic analyses.

<sup>354</sup> The benefits-earnings ratio is derived from BLS's Employer Costs for Employee Compensation data using variables CMU1020000000000D and CMU1030000000000D. This fringe benefit rate includes some fixed costs such as health insurance.

<sup>355</sup> The Department believes that the overhead costs associated with this rulemaking 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, the Department has included an overhead rate of 17 percent.

would spend an additional ten minutes per week scheduling and monitoring each affected worker expected to become nonexempt, overtime-eligible as a result of this rule, and whose hours would be adjusted.

There was little precedent or data to aid in evaluating managerial costs. Prior to the 2016 rulemaking, earlier part 541 rulemakings did not estimate managerial costs. The Department likewise found no estimates of managerial costs after reviewing the literature. Thus, the Department used the same methodology as the 2019 rule.

The Department believes these additional managerial costs would not be prohibitive. Currently, EAP exempt employees account for about 22 percent of the U.S. labor force; as such, the Department expects that most employers of EAP exempt workers also employ nonexempt workers. Those employers already have in place recordkeeping systems and standard operating procedures for ensuring employees only work overtime under employer-prescribed circumstances. Thus, such systems generally do not need to be invented for managing formerly exempt EAP employees. The Department also notes that under the FLSA recordkeeping regulations in part 516, employers determine how to make and keep an accurate record of hours worked by employees. For example, employers may tell their workers to write their own time records and any timekeeping plan is acceptable if it is complete and accurate. Additionally, if the nonexempt employee works a fixed schedule, *e.g.*, 9:00 a.m.–5:30 p.m. Monday–Friday, the employer may keep a record showing the exact schedule of daily and weekly hours and merely indicate exceptions to that schedule.<sup>356</sup>

As discussed in detail below, most affected workers do not currently work overtime, and there is no reason to expect their hours worked to change when their status changes from exempt to nonexempt. For that group of workers, management would have little or no need to increase their monitoring of hours worked; therefore, these workers are not included in the managerial cost calculation. Under these assumptions, the additional managerial hours worked per week would be 123,000 hours ((10 minutes ÷ 60 minutes) × 738,000 workers).

The median hourly wage in 2022 for a manager was \$51.62.<sup>357</sup> Together with

a 45 percent benefits rate and a 17 percent overhead cost, this totals \$83.63 per hour.<sup>358</sup> Thus, the estimated Year 1 managerial costs total \$534.9 million (123,000 hours per week × 52 weeks × \$83.63/hour). Although the exact magnitude would vary each year with the number of affected EAP workers, the Department anticipates that employers would incur managerial costs annually.

#### v. Other Potential Costs

In addition to the costs discussed above, the Department notes that the 2016 and 2019 final rules discussed other potential costs that could not be quantified. These potential costs are discussed qualitatively below. The Department welcomes comments on the potential costs associated with this proposed rule and any data that could help to quantify them.

##### (a) Reduced Scheduling Flexibility

To the extent that some employers spend more time monitoring nonexempt workers' hours, the proposed rule could impose costs on newly nonexempt, overtime eligible workers who could have a more limited ability to adjust their schedules. However, the proposed rule does not require employers to reduce scheduling flexibility. Employers can continue to offer flexible schedules and require workers to monitor their own hours and to follow the employers' timekeeping rules. Additionally, some exempt workers already monitor their hours for billing purposes. A study by Lonnie Golden 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 than they would 'lose' if they become more like their hourly counterparts."<sup>359</sup> Because there is little data or literature on these potential costs, the Department did not quantify potential costs regarding scheduling flexibility.

##### (b) Preference for Salaried Status

Some of the workers who would become nonexempt as a result of the proposed rule could have their pay changed from salaried to hourly status

be an overestimate of the wage rate for managers who monitor workers' hours because (1) it includes very highly paid employees such as CEOs, and (2) some lower-level supervisors are not counted as managers in the data.

<sup>358</sup> The benefits ratio is derived from BLS' 2022 Employer Costs for Employee Compensation data using variables CMU102000000000D and CMU1030000000000D.

<sup>359</sup> Golden, L. (2014). Flexibility and Overtime Among Hourly and Salaried Workers. Economic Policy Institute. [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2597174](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2597174).

despite preferring to remain salaried. Research has shown that salaried workers are more likely than hourly workers to receive benefits such as paid vacation time and health insurance<sup>360</sup> and are more satisfied with their benefits.<sup>361</sup> Additionally, when employer demand for labor decreases, hourly workers tend to see their hours cut before salaried workers, making earnings for hourly workers less predictable.<sup>362</sup> However, this literature generally does not control for differences between salaried and hourly workers such as education, job title, or earnings; therefore, this correlation is not necessarily attributable to hourly status.

If workers become nonexempt and the employer chooses to pay them on an hourly rather than salary basis, this may result in the employer reducing the workers' benefits. But the Department notes that this rulemaking would not require employers to reduce workers' benefits. These newly nonexempt workers may continue to be paid a salary, as long as that salary is equivalent to a base wage at least equal to the minimum wage rate for every hour worked, and the employee receives a 50 percent premium on that employee's regular rate for any overtime hours each week.<sup>363</sup> Similarly, employers may continue to provide these workers with the same level of benefits as before, whether paid on an hourly or salary basis. Lastly, the nature of the market mechanism may be such that employers cannot reduce benefits without risking workers leaving, resulting in turnover costs to employers. The Department did not quantify potential costs regarding reduction in workers' benefits.

##### (c) Increased Prices

As discussed in the transfers section below, businesses may be able to help mitigate increased labor costs following this rulemaking by rebalancing the hours that their employees are working. Businesses that are unable to rebalance these hours and do incur increased

<sup>360</sup> Lambert, S. J. (2007). Making a Difference for Hourly Employees. In A. Booth, & A. C. Crouter, *Work-Life Policies that Make a Real Difference for Individuals, Families, and Communities*. Washington, DC: Urban Institute Press.

<sup>361</sup> Balkin, D. B., & Griffeth, R. W. (1993). The Determinants of Employee Benefits Satisfaction. *Journal of Business and Psychology*, 7(3), 323–339.

<sup>362</sup> Lambert, S. J., & Henly, J. R. (2009). *Scheduling in Hourly Jobs: Promising Practices for the Twenty-First Century Economy*. The Mobility Agenda. Lambert, S. J. (2007). Making a Difference for Hourly Employees. In A. Booth, & A. C. Crouter, *Work-Life Policies that Make a Real Difference for Individuals, Families, and Communities*. Washington, DC: Urban Institute Press.

<sup>363</sup> 29 CFR 778.113–.114.

<sup>356</sup> See Fact Sheet #21: Recordkeeping Requirements under the Fair Labor Standards Act, available at: <https://www.dol.gov/whd/regs/compliance/whdfs21.pdf>.

<sup>357</sup> OEWS 2022. Available at: <https://www.bls.gov/oes/current/oes110000.htm>. This may



labor costs might pass along these increased labor costs to consumers through higher prices. The Department anticipates that some firms could offset part of the additional labor costs through charging higher prices for the firms' goods and services. However, because costs and transfers would be, on average, small relative to payroll and revenues, the Department does not expect the proposed rule to have a significant effect on prices. The Department estimated that, on average, costs and transfers make up less than 0.03 percent of payroll and 0.005 percent of revenues, although for specific industries and firms this percentage may be larger (see Table 27). Therefore, any potential change in prices related to costs and transfers from this rulemaking would be modest. Further, any significant price increases would not represent a separate category of effects from those estimated in this economic analysis. Rather, such price increases (where they occur) would be the channel through which consumers, rather than employers or employees, bear rule-induced costs (including transfers).

While economic theory suggests that an increase in labor costs in excess of productivity gains would lead to increases in prices, much of the empirical literature has found that wage inflation does not predict price inflation.<sup>364</sup> For example, Peneva et al. (2015) explore the relationship between labor costs and price inflation between 1965 and 2012, finding that the influence of labor costs on prices has decreased over the past several decades and have made a relatively small contribution to price inflation in recent years.<sup>365</sup>

(d) Reduced Profits

The increase in workers' earnings resulting from the proposed salary levels would be a transfer of income from firms to workers, not a cost. 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 businesses. Thus, the Department acknowledges that the increased employer costs and transfer payments as a result of this proposed rule may reduce the profits of business firms, although (1) some firms may offset some of these costs and transfers by making payroll adjustments, and (2) some firms may mitigate their reduced profits due to these costs and transfers through increased prices. Because costs and transfers are, on average, small relative to payroll revenues, the Department does not expect this rulemaking to have a significant effect on profits.

(e) Hiring Costs

To the extent that firms respond to this proposed rule by reducing overtime hours, they may do so by spreading hours to other workers, including current workers employed for fewer than 40 hours per week by that employer, current workers who remain nonexempt, and newly hired workers. If new workers are hired to absorb these transferred hours, then the associated hiring costs would be a cost of this proposed rule. However, new employees would likely only be hired if their wages, onboarding costs, and training costs are less than the cost of overtime pay for the newly affected workers. The Department does not know how many new employees would be hired and thus did not estimate this cost.

(f) Hours-Related Worker Effects

Following the implementation of this rulemaking, some workers may see an increase in hours worked. For some affected workers, if their employers respond to the rule by increasing their salary to keep their exemption status, the change may also be accompanied by an increase in assigned hours. Additionally, some employers might respond to this regulation by reducing the overtime hours of affected workers and transferring these hours to other workers who remain exempt. This increase in hours could result in reduced personal time for these workers.

4. Transfers

i. Overview

Transfer payments occur when income is redistributed from one party to another. The Department has quantified two transfers from employers to employees that would result from the proposed rule: (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 due to the minimum wage provision were estimated to be \$48.6 million. The increase in the HCE compensation level does not affect minimum wage transfers because workers eligible for the HCE exemption earn well above the minimum wage. The Department estimates that transfers due to the applicability of the FLSA's overtime pay provision would be \$1.2 billion: \$932.1 million from the increased standard salary level and \$253.5 million from the increased HCE compensation level. Total Year 1 transfers are estimated at \$1.2 billion (Table 13).

TABLE 13—TOTAL ANNUAL CHANGE IN EARNINGS FOR AFFECTED EAP WORKERS BY PROVISION, YEAR 1  
[Millions]

Provision	Total	Standard salary level	HCE compensation level
Total .....	\$1,234.2	\$980.7	\$253.5
Minimum wage only .....	48.6	48.6	.....
Overtime pay only <sup>a</sup> .....	1,185.6	932.1	253.5

<sup>364</sup> Church, J.D. and Akin, B. (2017). "Examining price transmission across labor compensation costs, consumer prices, and finished-goods prices," *Monthly Labor Review*, U.S. Bureau of Labor Statistics; Emery, K. & Chang, C. (1996). *Do Wages Help Predict Inflation?*, Federal Reserve Bank of Dallas, Economic Review First Quarter 1996.

<https://www.dallasfed.org/-/media/documents/research/er/1996/er9601a.pdf>; Jonsson, M. & Palmqvist, S. (2004). *Do Higher Wages Cause Inflation?* Sveriges Riksbank Working Paper Series 159. [http://archive.riksbank.se/Upload/WorkingPapers/WP\\_159.pdf](http://archive.riksbank.se/Upload/WorkingPapers/WP_159.pdf).

<sup>365</sup> Pevena, E. V. and Rudd, J. B. (2015). "The Passthrough of Labor Costs to Price Inflation," Finance and Economics Discussion Series 2015–042. Washington: Board of Governors of the Federal Reserve System. <http://dx.doi.org/10.17016/FEDS.2015.042>.

Because the overtime premium depends on the employee's regular rate of pay, 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. Then, the Department estimated overtime payments.

#### ii. Transfers Due to the Minimum Wage Provision

For this analysis, the hourly rate of pay was calculated as usual weekly earnings divided by usual weekly hours worked. To earn less than the Federal or most state minimum wages, this set of workers must work many hours per week. For example, a worker paid \$684 per week must work 94.3 hours per week to earn less than the Federal minimum wage of \$7.25 per hour ( $\$684 \div \$7.25 = 94.3$ ).<sup>366</sup> The applicable minimum wage is the higher of the Federal minimum wage and the state minimum wage as of January 1, 2022. Most affected EAP workers already receive at least the minimum wage; only

an estimated 0.2 percent (8,200 in total) earn an implicit hourly rate of pay less than the Federal 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.<sup>367</sup>

In response to an increase in the regular rate of pay to the minimum wage, employers may reduce the workers' hours. In theory, since the quantity of labor hours demanded is inversely related to wages, a higher mandated wage would, all things being equal, result in fewer hours of labor demanded. However, the weight of the empirical evidence finds that increases in the minimum wage that are similar in magnitude to what would be caused by this regulatory provision have caused little or no significant job loss.<sup>368</sup> Thus, in the case of this proposed 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. According to the Wolfson and Belman (2016) meta-

analysis cited above, the consensus range for labor demand elasticity was  $-0.05$  to  $-0.12$ . However for Year 1 of this analysis, the Department estimated the potential disemployment effects (*i.e.*, the estimated reduction in hours) of the transfer attributed to the minimum wage by multiplying the percent change in the regular rate of pay by a labor demand elasticity of  $-0.2$  (years 2–10 use a long run elasticity of  $-0.4$ ).<sup>369 370</sup> The Department chose this labor demand elasticity because it was used in the 2019 final rule and is consistent with the labor demand elasticity estimates used when estimating other transfers further below.

At the new standard salary level, the Department estimated that 8,200 affected EAP workers would, on average, see an hourly wage increase of \$1.99, work 3.2 fewer hours per week and receive an increase in weekly earnings of \$113.88 as a result of coverage by the minimum wage provisions (Table 14). The total change in weekly earnings due to the payment of the minimum wage was estimated to be \$0.9 million per week ( $\$113.88 \times 8,200$ ) or \$48.6 million in Year 1.

TABLE 14—MINIMUM WAGE ONLY: MEAN HOURLY WAGES, USUAL WEEKLY HOURS AND WEEKLY EARNINGS FOR AFFECTED EAP WORKERS, YEAR 1

Time period	Hourly wage <sup>a</sup>	Usual weekly hours	Usual weekly earnings	Total weekly transfer (1,000s)
Before rule .....	\$11.35	73.2	\$808.60	.....
After rule .....	13.34	69.9	922.48	.....
Change .....	1.99	–3.2	113.88	\$934

**Note:** Pooled data for 2020–2022 adjusted to reflect 2022.

<sup>a</sup> The applicable minimum wage is the higher of the Federal minimum wage and the state minimum wage.

#### iii. Transfers Due to the Overtime Pay Provision

##### (a) Introduction

The FLSA requires covered employers to pay an overtime premium to nonexempt covered workers who work in excess of 40 hours per week. For workers who become nonexempt, the rulemaking would result in a transfer of income to the affected workers, increasing the marginal cost of labor, which employers would likely try to

offset by adjusting the wages and/or hours of affected workers. The size of the transfer would depend largely on how employers choose to respond to the updated salary levels. Employers may respond by: (1) paying overtime premiums to affected workers; (2) reducing overtime hours of affected workers and potentially transferring some of these hours to other workers; (3) reducing the regular rate of pay for affected workers working overtime (provided that the reduced rates still

exceed the minimum wage); (4) increasing affected workers' salaries to the updated salary or compensation level to preserve their exempt status; or (5) using some combination of these responses. How employers would 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.

<sup>366</sup> The Federal minimum wage has not increased since 2009. Workers in states with minimum wages higher than the Federal minimum wage could earn less than the state minimum wage working fewer hours.

<sup>367</sup> Because these workers' hourly wages will be set at the minimum wage after this proposed 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.

<sup>368</sup> Wolfson, Paul J. and Belman, Dale, 15 Years of Research on U.S. Employment and the Minimum Wage (December 10, 2016). Tuck School of Business Working Paper No. 2705499. [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2705499](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2705499). Dube, Arindrajit, Impacts of Minimum Wages: Review of the International Evidence (November 2019). [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/844350/impacts\\_of\\_minimum\\_wages\\_](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/844350/impacts_of_minimum_wages_review_of_the_international_evidence_Arindrajit_Dube_web.pdf)

[review\\_of\\_the\\_international\\_evidence\\_Arindrajit\\_Dube\\_web.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/844350/impacts_of_minimum_wages_review_of_the_international_evidence_Arindrajit_Dube_web.pdf).

<sup>369</sup> Labor demand elasticity is the percentage change in labor hours demanded in response to a one percent change in wages.

<sup>370</sup> This elasticity estimate represents a short run demand elasticity for general labor, and is based on the Department's analysis of Lichter, A., Peichl, A. & Sieglösch, A. (2014). The Own-Wage Elasticity of Labor Demand: A Meta-Regression Analysis. IZA DP No. 7958.

## (b) Literature on Employer Adjustments

Two conceptual models are useful for thinking about how employers may respond to when certain employees become eligible for overtime: (1) the “fixed-wage” or “labor demand” model, and (2) the “fixed-job” or “employment contract” model.<sup>371</sup> These models make different assumptions about the demand for overtime hours and the structure of the employment agreement, which result in different implications for predicting employer responses.

The fixed-wage model assumes that the standard hourly wage is independent of the statutory overtime premium. Under the fixed-wage model, a transition of workers from overtime exempt to overtime nonexempt would cause a reduction in overtime hours for affected workers, an increase in the prevalence of a 40-hour workweek among affected workers, and an increase in the earnings of affected workers who continue to work overtime.

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

The Department conducted a literature review to evaluate studies of how labor markets adjust to a change in the requirement to pay overtime. These studies are generally supportive of the fixed-job model of labor market adjustment, in that wages adjust to offset the requirement to pay an

overtime premium as predicted by the fixed-job model, but do not adjust enough to completely offset the overtime premium as predicted by the model.

As in the 2016 and 2019 rules, the Department believes the two most important papers in this literature are the studies by Trejo (1991) and Barkume (2010). Analyzing the economic effects of the overtime pay provisions of the FLSA, Trejo (1991) found “the data analyzed here suggest the wage adjustments occur to mitigate the purely demand-driven effects predicted by the fixed-wage model, but these adjustments are not large enough to neutralize the overtime pay regulations completely.” Trejo noted, “In accordance with the fixed job model, the overtime law appears to have a greater impact on minimum-wage workers.” He also stated, “[T]he finding that overtime-pay coverage status systematically influences the hours-of-work distribution for nonminimum-wage workers is supportive of the fixed-wage model. No significant differences in weekly earnings were discovered between the covered and non-covered sectors, which is consistent with the fixed-job model.” However, “overtime pay compliance is higher for union than for nonunion workers, a result that is more easily reconciled with the fixed wage model.” Trejo’s findings are supportive of the fixed-wage model whose adjustment is incomplete largely due to the minimum-wage requirement.<sup>372</sup>

A second paper by Trejo (2003) took a different approach to testing the consistency of the fixed-wage adjustment models with overtime coverage and data on hours worked.<sup>373</sup> In this paper, he examined time-series data on employee hours by industry. After controlling for underlying trends in hours worked over 20 years, he found changes in overtime coverage had no impact on the prevalence of overtime hours worked. This result supports the fixed-job model. Unlike the 1991 paper, however, he did not examine impacts of overtime coverage on employees’ weekly or hourly earnings, so this finding in support of the fixed-job model only analyzes one implication of the model.

Barkume (2010) built on the analytic method used in Trejo (1991).<sup>374</sup> However, Barkume observed that Trejo did not account for “quasi-fixed” employment costs (e.g., benefits) that do not vary with hours worked, and therefore affect employers’ decisions on overtime hours worked. After incorporating these quasi-fixed costs in the model, Barkume found results consistent with those of Trejo (1991): “though wage rates in otherwise similar jobs declined with greater overtime hours, they were not enough to prevent the FLSA overtime provisions from increasing labor costs.” Barkume also determined that the 1991 model did not account for evidence that in the absence of regulation some employers may voluntarily pay workers some overtime premium to entice them to work longer hours, to compensate workers for unexpected changes in their schedules, or as a result of collective bargaining. Barkume found that how much wages and hours worked adjusted in response to the overtime pay requirement depended on what overtime pay would be in absence of regulation.

In addition, Bell and Hart (2003) examined the standard hourly wage, average hourly earnings (including overtime), the overtime premium, and overtime hours worked in Britain.<sup>375</sup> Unlike the United States, Britain does not have national labor laws regulating overtime compensation. Bell and Hart found that after accounting for overtime, average hourly earnings are generally uniform in an industry because firms paying below-market level straight-time wages tend to pay above-market overtime premiums and firms paying above-market level straight-time wages tend to pay below-market overtime premiums. Bell and Hart concluded “this is consistent with a model in which workers and firms enter into an implicit contract that specifies total hours at a constant, market-determined, hourly wage rate. Their research is also consistent with studies showing that employers may pay overtime premiums either in the absence of a regulatory mandate (e.g., Britain), or when the mandate exists but the requirements are not met (e.g., United States).<sup>376</sup>

On balance, consistent with its 2016 and 2019 rulemakings, the Department

<sup>371</sup> 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.

<sup>372</sup> Trejo, S.J. (1991). The Effects of Overtime Pay Regulation on Worker Compensation. *American Economic Review*, 81(4), 719–740.

<sup>373</sup> Trejo, S.J. (2003). Does the Statutory Overtime Premium Discourage Long Workweeks? *Industrial and Labor Relations Review*, 56(3), 375–392.

<sup>374</sup> Barkume, A. (2010). The Structure of Labor Costs with Overtime Work in U.S. Jobs. *Industrial and Labor Relations Review*, 64(1), 128–142.

<sup>375</sup> Bell, D.N.F. and Hart, R.A. (2003). Wages, Hours, and Overtime Premia: Evidence from the British Labor Market. *Industrial and Labor Relations Review*, 56(3), 470–480.

<sup>376</sup> Hart, R.A. and Yue, M. (2000). Why Do Firms Pay an Overtime Premium? IZA Discussion Paper No. 163.

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

To determine the magnitude of the adjustment, the Department accounted for the following findings. Earlier research had demonstrated that in the absence of regulation some employers may voluntarily pay workers some overtime premium to entice them to work longer hours, to compensate workers for unexpected changes in their schedules, or as a result of collective bargaining.<sup>377</sup> Barkume (2010) found that the measured adjustment of wages and hours to overtime premium requirements depended on what overtime premium might be paid in absence of any requirement to do so. Thus, when Barkume assumed that workers would receive an average voluntary overtime pay premium of 28 percent in the absence of an overtime pay regulation, which is the average overtime premium that Bell and Hart (2003) found British employers paid in the absence of any overtime regulations, the straight-time hourly wage adjusted downward by 80 percent of the amount that would occur with the fixed-job model.<sup>378</sup> When Barkume assumed workers would receive no voluntary overtime pay premium in the absence of an overtime pay regulation, the results were more consistent with Trejo's (1991) findings that the adjustment was a smaller percentage. The Department modeled an adjustment process between these two findings. Although it seemed reasonable that some premium was paid

for overtime in the absence of regulation, Barkume's assumption of a 28 percent initial overtime premium is likely too high for the salaried workers potentially affected by a change in the salary and compensation level requirements for the EAP exemptions because this assumption is based on a study of workers in Britain. British workers were likely paid a larger voluntary overtime premium than American workers because Britain did not have a required overtime pay regulation and so collective bargaining played a larger role in implementing overtime pay.<sup>379</sup> In the sections that follow, the Department uses a method between these two papers to model transfers.

#### (c) Identifying Types of Affected Workers

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

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

The Department began by identifying the number of workers in each type. After modeling employer adjustments, it estimated transfer payments. Type 3 and 4 workers were identified as those who regularly work overtime (CPS variable PEHRUSL1 greater than 40). To distinguish Type 3 workers from Type 4 workers, the Department first estimated each worker's weekly earnings if they became nonexempt, to which it added weekly managerial costs for each affected worker of \$13.94 (\$83.63 per hour  $\times$  (10 minutes  $\div$  60 minutes)).<sup>380</sup> Then, the Department identified as Type 4 those workers whose expected nonexempt earnings plus weekly managerial costs exceeds the updated standard salary level, and, conversely, as Type 3 those whose expected nonexempt earnings plus weekly managerial costs are less than

the new standard salary. The Department assumed that firms would include incremental managerial costs in their determination of whether to treat an affected employee as a Type 3 or Type 4 worker because those costs are only incurred if the employee is a Type 3 worker.

Identifying Type 2 workers involved two steps. First, using CPS MORG data, the Department identified those who do not usually work overtime but did work overtime in the survey week (the week referred to in the CPS questionnaire, variable PEHRACT1 greater than 40). Next, the Department supplemented the CPS data with data from the Survey of Income and Program Participation (SIPP) to look at likelihood of working some overtime during the year. Based on 2021 data, the most recent available, the Department found that 31.3 percent of non-hourly workers worked overtime at some point in a year. Therefore, the Department classified a share of workers who reported they do not usually work overtime, and did not work overtime in the reference week, as Type 2 workers such that a total of approximately 31.3 percent of affected workers were Type 2, 3, or 4. Type 2 workers are subdivided into Types 2A and 2B later in the analysis (Table 15).

TABLE 15—TYPES OF AFFECTED WORKERS

Type of worker	Percent of total
Type 1 .....	69
Type 2A .....	8
Type 2B .....	8
Type 3 .....	12
Type 4 .....	3

**Note:** Pooled CPS data for 2020–2022 adjusted to reflect 2022.

\* *Type 1:* Workers who do not work overtime and gain overtime protection.

\* *Type 2:* Workers who work occasional overtime and gain overtime protection.

• *Type 2A:* Those who work *unexpected* overtime hours.

• *Type 2B:* Those who work *expected* overtime.

\* *Type 3:* Workers who work regular overtime and gain overtime protection.

\* *Type 4:* Workers who work regular overtime and remain exempt (*i.e.*, earnings increase to the updated salary or compensation level).

#### (d) Modeling Changes in Wages and Hours

The incomplete fixed-job model predicts that employers would adjust wages of regular overtime workers but not to the full extent indicated by the fixed-job model, and thus some employees would receive a small increase in weekly earnings due to overtime pay coverage. The Department

<sup>377</sup> 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.

<sup>378</sup> Barkume, A. (2010). The Structure of Labor Costs with Overtime Work in U.S. Jobs. *Industrial and Labor Relations Review*, 64(1), 128–142.

<sup>379</sup> Bell, D.N.F. and Hart, R.A. (2003). Wages, Hours, and Overtime Premia: Evidence from the British Labor Market. *Industrial and Labor Relations Review*, 56(3), 470–480.

<sup>380</sup> See section VII.C.3.iv (managerial costs).

used the average of two estimates of the incomplete fixed-job model adjustments to model impacts of this proposed rule:<sup>381</sup>

- Trejo's (1991) estimate that the overtime-induced wage change is 40 percent of the adjustment toward the amount predicted by the fixed-job model, assuming an initial zero overtime pay premium, and
- Barkume's (2010) estimate that the wage change is 80 percent of the predicted adjustment assuming an initial 28 percent overtime pay premium.

This is approximately equivalent to assuming that salaried overtime workers implicitly receive the equivalent of a 14 percent overtime premium in the absence of regulation (the midpoint between 0 and 28 percent).

Modeling changes in hourly wages, hours, and earnings for Type 1 and Type 4 workers was relatively straightforward. Type 1 affected EAP workers would become overtime-eligible, but because they do not work overtime, they would see no change in their wages, hours, or weekly earnings. Type 4 workers would remain exempt because their earnings would be raised to at least the updated EAP level (either the standard salary level or HCE compensation level). These workers' earnings would increase by the difference between their current earnings and the amount necessary to satisfy the new salary or compensation level. It is possible employers would increase these workers' hours in response to paying them a higher salary, but the Department did not have enough information to model this potential change.<sup>382</sup>

Modeling changes in wages, hours, and earnings for Type 2 and Type 3 workers was more complex. The Department distinguished those who regularly work overtime (Type 3 workers) from those who occasionally

work overtime (Type 2 workers) because employer adjustment to the rule may differ accordingly. Employers are more likely to adjust hours worked and wages for regular overtime workers because their hours are predictable. Conversely, in response to a transient, perhaps unpredicted, shift in market demand for the good or service such employers provide, employers are more likely to pay for occasional overtime rather than adjust hours worked and pay.

The Department treated Type 2 affected workers in two ways due to the uncertainty of the nature of these occasional overtime hours. The Department assumed that 50 percent of these occasional overtime workers worked *unexpected* overtime hours (Type 2A) and the other 50 percent worked *expected* overtime (Type 2B). Workers were randomly assigned to these two groups. Workers with *expected* occasional overtime hours were treated like Type 3 affected workers (incomplete fixed-job model adjustments). Workers with *unexpected* occasional overtime hours were assumed to receive a 50 percent pay premium for the overtime hours worked and receive no change in base wage or hours (full overtime premium model).<sup>383</sup> When modeling Type 2 workers' hour and wage adjustments, the Department treated those identified as Type 2 using the CPS data as representative of all Type 2 workers.<sup>384</sup> The Department estimated employer adjustments and transfers assuming that the patterns observed in the CPS reference week are representative of an average week in the year. Thus, the Department assumes total transfers for the year are equal to 52 times the transfers estimated for a representative week for which the Department has CPS data. However, these transfers are spread over a larger group including those who occasionally work overtime but did not do so in the CPS reference week.<sup>385</sup>

<sup>381</sup> Both studies considered a population that included hourly workers. Evidence is not available on how the adjustment towards the fixed-job model differs between salaried and hourly workers. The fixed-job 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 fixed-job model as estimated by these studies may overestimate the transfers from employers to salaried workers. The Department does not attempt to quantify the magnitude of this potential overestimate, but welcomes comments on how to refine the quantitative approach.

<sup>382</sup> Cherry, Monica, "Are Salaried Workers Compensated for Overtime Hours?" *Journal of Labor Research* 25(3): 485–494, September 2004, found that exempt full-time salaried employees earn more when they work more hours, but her results do not lend themselves to the quantification of the effect on hours of an increase in earnings.

<sup>383</sup> The Department uses the term "full overtime premium" to describe the adjustment process as modeled. The full overtime premium model is a special case of the general fixed-wage model in that the Department assumes the demand for labor under these circumstances is completely inelastic. That is, employers make no changes to employees' hours in response to these temporary, unanticipated changes in demand.

<sup>384</sup> As explained in the previous section, to estimate the population of Type 2 workers, the Department supplemented workers who report working overtime in the CPS reference week with some workers who do not work overtime in the reference week to reflect the fact that different workers work occasional overtime in different weeks.

<sup>385</sup> If a different week was chosen as the survey week, then some of these workers would not have worked overtime. However, because the data are

Since employers would pay more for the same number of labor hours, for Type 2 and Type 3 EAP workers, the quantity of labor hours demanded by employers would decrease. The reduction in hours is calculated using the elasticity of labor demand with respect to wages. The Department used a short-term demand elasticity of  $-0.20$  to estimate the percentage decrease in hours worked in Year 1 and a long-term elasticity of  $-0.4$  to estimate the percentage decrease in hours worked in Years 2–10. These elasticity estimates are based on the Department's analysis of Lichter et al. (2014).<sup>386</sup> Brown and Hamermesh (2019) estimated the elasticity of overtime hours for EAP-exempt workers.<sup>388</sup> This estimate is based on a difference-in-differences in hours for two groups of workers between two time periods. However, some groups of workers are incorrectly defined, so the Department has not used these estimates.<sup>389</sup>

For Type 3 affected workers, and the 50 percent of Type 2 affected workers who worked *expected* overtime, the Department estimated adjusted total hours worked after making wage adjustments using the incomplete fixed-job model. To estimate adjusted hours worked, the Department set the percent change in total hours worked equal to the percent change in average wages multiplied by the wage elasticity of labor demand.<sup>390</sup> Figure 4 is a flow

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.

<sup>386</sup> Lichter, A., Peichl, A. & Sieglösch, A. (2014). *The Own-Wage Elasticity of Labor Demand: A Meta-Regression Analysis*. IZA DP No. 7958.

<sup>387</sup> Some researchers have estimated larger impacts on the number of overtime hours worked. For example, Hamermesh and Trejo (2000) conclude the price elasticity of demand for overtime hours is at least  $-0.5$ . The Department decided to use a general measure of elasticity applied to the average change in wages since the increase in the overtime wage is somewhat offset by a decrease in the non-overtime wage as indicated in the fixed-job model. 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.

<sup>388</sup> Brown, Charles C., and Daniel S. Hamermesh. (2019). "Wages and Hours Laws: What Do We Know? What Can Be Done?" RSF: The Russell Sage Foundation Journal of the Social Sciences 5(5): 68–87. DOI: 10.7758/RSF.2019.5.5.04.

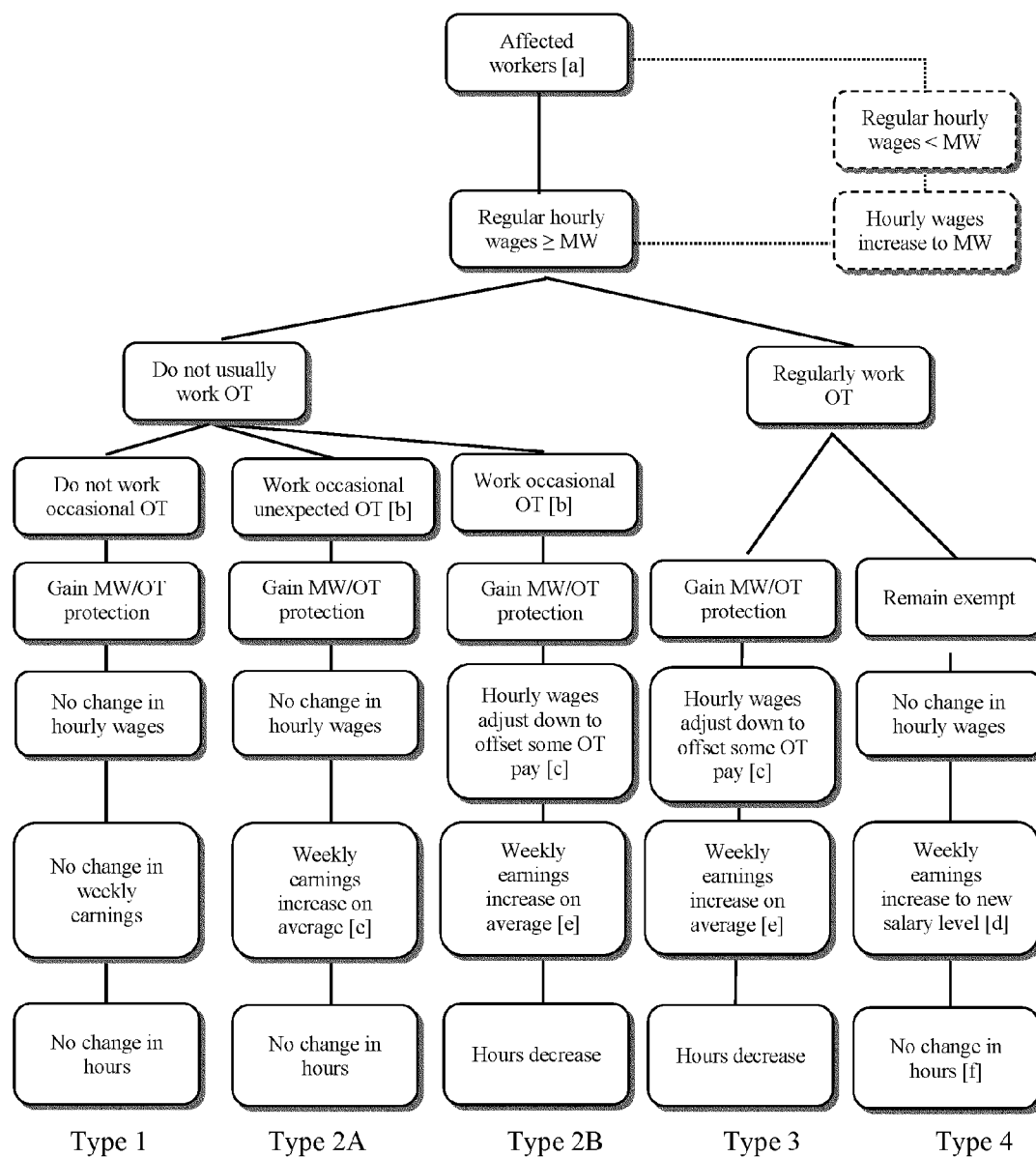
<sup>389</sup> For example, the authors defined the "non-exempt 1987–1989" group as workers earning above \$223 but below \$455 during this period. Because the salary level for the long test was \$155 or \$170 and was \$250 for the short test, see section VII.A.1 (Table 1), some of these workers would be exempt.

<sup>390</sup> 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.

chart summarizing the four types of affected EAP workers. Also shown are the effects on exempt status, weekly

earnings, and hours worked for each type of affected worker.  
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Figure 4: Flow Chart of Proposed Rule's Effect on Earnings and Hours Worked



[a] 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] The Department used two methods to identify occasional overtime workers. The first includes workers who report they usually work 40 hours or fewer 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 fewer per week, and in the reference week worked 40 hours or fewer, to match the proportion of workers measured in other data sets who work overtime at any point in the year.



[c] The amount wages are adjusted downwards depends on whether the fixed-job model or the fixed-wage model holds. The Department's primary method uses a combination of the two.

Employers reduce the regular hourly wage rate somewhat in response to overtime pay requirements, but the wage is not reduced enough to keep total compensation constant.

[d] Based on hourly wage and weekly hours it is more cost efficient for the employer to increase the worker's weekly salary to the updated salary level than to pay overtime pay.

[e] On average, the Department's modeling of regulatory effects yields a result in which employees' overall weekly earnings will increase despite a small decrease in average hours worked. In some limited cases, employers might decrease employees' hours enough to cause those employees' weekly earnings to decrease.

[f] The Department assumed hours would not change; however, it is possible employers will increase these workers' hours in response to paying them a higher salary or to avoid paying overtime premiums to newly nonexempt coworkers.

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(e) Estimated Number of and Effects on Affected EAP Workers

The Department estimated the proposed rule would affect 3.6 million

workers (Table 16), of which 2.5 million are Type 1 workers (68.7 percent of all affected EAP workers), 579,200 were estimated to be Type 2 workers (15.9 percent), 448,400 were Type 3 workers

(12.3 percent), and 115,700 were estimated to be Type 4 workers (3.2 percent).

TABLE 16—AFFECTED EAP WORKERS BY TYPE (1,000S), YEAR 1

EAP test	Total	No overtime (T1)	Occasional overtime (T2)	Regular overtime	
				Newly nonexempt (T3)	Remain exempt (T4)
Standard salary level .....	3,399.4	2,335.7	569.9	384.9	108.9
HCE compensation level .....	248.9	169.2	9.3	63.5	6.8
Total .....	3,648.3	2,504.9	579.2	448.4	115.7

**Note:** Pooled CPS data for 2020–2022 adjusted to reflect 2022.

\* *Type 1:* Workers who do not work overtime and gain overtime protection.

\* *Type 2:* Workers who work occasional overtime and gain overtime protection.

\* *Type 3:* Workers who work regular overtime and gain overtime protection.

\* *Type 4:* Workers who work regular overtime and remain exempt (*i.e.*, earnings increase to the updated salary level).

The proposed rule would affect some affected workers' hourly wages, hours, and weekly earnings. Predicted changes in implicit wage rates are outlined in Table 17, changes in hours in Table 18, and changes in weekly earnings in Table 19. How these would change depends on the type of worker, but on average the Department projects that weekly earnings would be unchanged or increase while hours worked would be unchanged or decrease.

Type 1 workers would have no change in wages, hours, or earnings due to the overtime pay provision because these workers do not work overtime.<sup>391</sup>

<sup>391</sup> It is possible that these workers may experience an increase in hours and weekly earnings because of transfers of hours from other newly nonexempt workers who do usually work overtime. Due to the high level of uncertainty in employers' responses regarding the transfer of hours, the Department did not have credible evidence to support an estimation of the number of hours transferred to other workers.

Some Type 1 workers who earn less than the Federal or state minimum wage would see an increase in wages, a decrease in hours, and an increase in weekly earnings.

For Type 2A workers, the Department assumed employers would be unable to adjust the hours or regular rate of pay for these occasional overtime workers whose overtime is irregularly scheduled and unpredictable. These workers would receive a 50 percent premium on their regular hourly wage for each hour worked in excess of 40 hours per week, and so average weekly earnings would increase.<sup>392</sup>

<sup>392</sup> Type 2 workers will not see increases in regular earnings to the new salary or compensation levels (as Type 4 workers do) even if their new earnings in this week exceed those new levels. This is because the estimated new earnings only reflect their earnings in those weeks when overtime is worked; their earnings in typical weeks when they do not work overtime do not exceed the salary or compensation level.

For Type 3 workers and Type 2B workers (the 50 percent of Type 2 workers who regularly work occasional overtime, an estimated 738,000 workers), the Department used the incomplete fixed-job model to estimate changes in the regular rate of pay. These workers would see a decrease in their average regular hourly wage and a small decrease in hours. However, because these workers would receive a 50 percent premium on their regular hourly wage for each hour worked in excess of 40 hours per week, their average weekly earnings would increase. The reduction in hours is relatively small and is due to a decrease in labor demand from the increase in the average hourly wage as predicted by the incomplete fixed-job model (Table 18).

Type 4 workers' implicit hourly rates of pay and weekly earnings would increase to meet the updated standard salary level or HCE annual

compensation level. Type 4 workers' hours may increase to offset the additional earnings, but due to lack of

data, the Department assumed hours would not change.

TABLE 17—AVERAGE REGULAR RATE OF PAY BY TYPE OF AFFECTED EAP WORKER, YEAR 1

Time period	Total	No overtime (T1)	Occasional overtime (T2)	Regular overtime	
				Newly non- exempt (T3)	Remain ex- empt (T4)
Standard Salary Level					
Before rule .....	\$23.55	\$24.18	\$25.48	\$17.82	\$20.07
After rule .....	\$23.43	\$24.18	\$25.36	\$16.90	\$20.42
Change (\$) .....	−\$0.11	\$0.00	−\$0.12	−\$0.92	\$0.34
Change (%) .....	−0.5%	0.0%	−0.5%	−5.2%	1.7%
HCE Compensation Level					
Before rule .....	\$56.10	\$60.07	\$58.90	\$45.92	\$48.63
After rule .....	\$55.31	\$60.07	\$54.99	\$43.31	\$49.78
Change (\$) .....	−\$0.79	\$0.00	−\$3.91	−\$2.61	\$1.15
Change (%) .....	−1.4%	0.0%	−6.6%	−5.7%	2.4%

**Note:** Pooled CPS data for 2020–2022 adjusted to reflect 2022.

\*Type 1: Workers who do not work overtime and gain overtime protection.

\*Type 2: Workers who work occasional overtime and gain overtime protection.

\*Type 3: Workers who work regular overtime and gain overtime protection.

\*Type 4: Workers who work regular overtime and remain exempt (*i.e.*, earnings increase to the updated salary level).

TABLE 18—AVERAGE WEEKLY HOURS BY TYPE OF AFFECTED EAP WORKER, YEAR 1

Time period	Total	No overtime worked (T1)	Occasional OT (T2)	Regular OT	
				Newly non-exempt (T3)	Remain exempt (T4)
Standard Salary Level <sup>a</sup>					
Before rule .....	41.0	38.9	40.9	50.4	52.9
After rule .....	41.0	38.9	40.9	50.0	52.9
Change (hours) .....	0.0	0.0	0.0	− 0.4	0.0
Change (%) .....	− 0.1%	0.0%	− 0.1%	− 0.8%	0.0%
HCE Compensation Level <sup>a</sup>					
Before rule .....	43.3	39.5	52.7	50.6	56.0
After rule .....	43.2	39.5	52.3	50.3	56.0
Change (hours) .....	− 0.1	0.0	− 0.4	− 0.3	0.0
Change (%) .....	− 0.2%	0.0%	− 0.7%	− 0.7%	0.0%

**Note:** Pooled CPS data for 2020–2022 adjusted to reflect 2022.

<sup>a</sup> Usual hours for Types 1, 3, and 4 but actual hours for Type 2 workers identified in the CPS MORG.

\*Type 1: Workers who do not work overtime and gain overtime protection.

\*Type 2: Workers who work occasional overtime and gain overtime protection.

\*Type 3: Workers who work regular overtime and gain overtime protection.

\*Type 4: Workers who work regular overtime and remain exempt (*i.e.*, earnings increase to the updated salary level).

TABLE 19—AVERAGE WEEKLY EARNINGS BY TYPE OF AFFECTED EAP WORKER, YEAR 1

Time period	Total	No overtime (T1)	Occasional overtime (T2)	Regular overtime	
				Newly non- exempt (T3)	Remain ex- empt (T4)
Standard Salary Level <sup>a</sup>					
Before rule .....	\$913.71	\$904.82	\$947.26	\$882.62	\$1,038.69
After rule .....	\$919.26	\$904.82	\$960.66	\$906.04	\$1,059.00
Change (\$) .....	\$5.55	\$0.00	\$13.39	\$23.42	\$20.31
Change (%) .....	0.6%	0.0%	1.4%	2.7%	2.0%
HCE Compensation Level <sup>a</sup>					
Before rule .....	\$2,354.99	\$2,323.22	\$3,101.59	\$2,292.51	\$2,704.08

TABLE 19—AVERAGE WEEKLY EARNINGS BY TYPE OF AFFECTED EAP WORKER, YEAR 1—Continued

Time period	Total	No overtime (T1)	Occasional overtime (T2)	Regular overtime	
				Newly non- exempt (T3)	Remain ex- empt (T4)
After rule .....	\$2,374.58	\$2,323.22	\$3,193.44	\$2,348.79	\$2,769.00
Change (\$) .....	\$19.59	\$0.00	\$91.85	\$56.28	\$64.92
Change (%) .....	0.8%	0.0%	3.0%	2.5%	2.4%

**Note:** Pooled CPS data for 2020–2022 adjusted to reflect 2022.

<sup>a</sup> 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 who do not work overtime and gain overtime protection.

\*Type 2: Workers who work occasional overtime and gain overtime protection.

\*Type 3: Workers who work regular overtime and gain overtime protection.

\*Type 4: Workers who work regular overtime and remain exempt (*i.e.*, earnings increase to the updated salary level).

At the new standard salary level, the average weekly earnings of affected workers would increase \$5.55 (0.6 percent), from \$913.71 to \$919.26. Multiplying the average change of \$5.55 by the 3.4 million EAP workers affected by the change in the standard salary level and 52 weeks equals an increase in earnings of \$1.0 billion in the first year. For workers affected by the change in the HCE compensation level, average weekly earnings would increase by \$19.59. When multiplied by 248,900 affected workers and 52 weeks, the national increase would be \$253.5 million in the first year. Thus, total Year 1 transfer payments attributable to this proposed rule would total \$1.2 billion.

The Department is only aware of one paper that modeled the impacts of the 2019 rule's increases in the salary and compensation levels. Quach (2021)<sup>393</sup> used administrative payroll data from May 2008 to January 2020 to estimate the impacts of the rescinded 2016 rule and the 2019 rule on employment, earnings, and salary status.<sup>394</sup> The paper has not been published in a peer-reviewed journal and has significant limitations, including that its use of administrative payroll data from ADP means that the findings are not representative as ADP customers do not represent a random sample of the workplace. Furthermore, the paper's analysis only includes the 22 states that have not updated their state or local minimum wages since 2014.<sup>395</sup>

In terms of its findings, concerning employment, the author did not find the impact to be statistically different from

zero for either rule, although he did find a significant decrease in employment when state overtime exemption laws were incorporated. Concerning earnings, he found an increase in base weekly earnings and an increase in overtime pay for both rules. The percent change in total pay that he estimates, around 1 to 2 percent depending on the rule, is not vastly different than the Department's estimate of 0.6 percent. Concerning salary status, he found an increase in the number of hourly jobs after the 2016 rule but not after the 2019 rule. His analysis of both rules showed a shift in the number of salaried workers from below to above the threshold (as does the Department's analysis).

The Department has not adjusted its methodology in response to this paper given the concerns listed above, but remains interested in further peer-reviewed research that may provide relevant findings.

Additionally, it can be informative to look at papers which predict the impact of rulemakings. For example, Rohwedder and Wenger (2015) analyzed the effects of increasing the standard salary level from the then baseline level of \$455 per week.<sup>396</sup> They compared hourly and salaried workers in the CPS using quantile treatment effects. This methodology estimates the effect of a worker becoming nonexempt by comparing similar workers who are hourly and salaried. They found no statistically significant change in hours or wages on average. However, their point estimates, averaged across all affected workers, show small increases in earnings and decreases in hours, similar to the Department's analysis. For example, using a salary level of \$750, they estimated weekly earnings may increase between \$2 and \$22 and

weekly hours may decrease by approximately 0.4 hours.

#### iv. Potential Transfers Not Quantified

This proposed rule could lead to additional transfers that the Department is unable to quantify. For example, in response to this proposed rule, some employers may decrease the hours of newly nonexempt workers who usually work overtime. These hours may be transferred to other workers, such as non-overtime workers and exempt workers who are not affected by the rule. Depending on how these hours are transferred, it could lead to either a reduction or increase in earnings for other workers. Employers may also offset increased labor costs by reducing bonuses or benefits instead of reducing base wages or hours worked. If this occurs, an employee's overall compensation may not be affected.

The rule could also reduce reliance on social assistance programs for some workers who may receive a transfer of income resulting from this proposed rule if finalized. For low-income workers, this transfer could result in a reduced need for social assistance programs such as Medicaid, the Earned Income Tax Credit (EITC), 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. A worker earning the current salary level of \$684 per week earns \$35,568 annually, which is roughly equivalent to the Federal poverty level for a family of five and makes the family eligible for many social assistance programs.<sup>397</sup> Thus, transferring income to these workers

<sup>393</sup> Quach, S. (2022). The Labor Market Effects of Expanding Overtime Coverage. [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3608506](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3608506).

<sup>394</sup> The Department notes that the effective date of the 2019 final rule was in January 2020, so using data from this month may not fully capture the effects of the 2019 rule.

<sup>395</sup> This is a reasonable restriction to minimize the influence of exogenous factors. However, it makes the sample unrepresentative of the U.S.

<sup>396</sup> 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.

<sup>397</sup> Department of Health and Human Services (2023). Federal Poverty Level. <https://www.healthcare.gov/glossary/federal-poverty-level-fpl/>.

could reduce eligibility for government social assistance programs and could therefore also reduce government expenditures.

The Department requests comments and data on additional transfers that could occur if this rule were finalized as proposed.

## 5. Benefits and Cost Savings

The Department expects that this proposed rule could lead to multiple benefits, which are discussed qualitatively below. The Department welcomes comments on the potential benefits associated with this proposed rule and any data that could help to quantify them.

First, the updated salary level would strengthen the overtime protection of salaried, white-collar employees who do not pass the standard duties test and who earn between the current salary standard salary level and the proposed salary level. These employees are nonexempt but, because they satisfy the current salary level threshold, employers must apply the duties test to determine their exemption status. At the proposed salary level, the number of white-collar salaried employees who fail the duties test but earn at or above the salary level would decrease by 4.1 million. Because these nonexempt employees would not meet the proposed salary level, employers would be able to determine their exemption status based solely on the salary test. If any of these employers previously spent significant time evaluating the duties of these workers to determine exemption status, the change to determining exemption status based on the salary level could lead to some cost savings.

As the Department has noted in prior EAP rulemakings, some salaried, white-collar employees who meet the salary level threshold but do not meet the duties test may be misclassified as exempt from overtime protection due to misapplication of the duties test.<sup>398</sup> To the extent that some of the 4.1 million salaried, white-collar employees who do not meet the duties test and earn between the current \$684 per week salary level and the proposed \$1,059 per week salary level are misclassified as exempt, the proposed salary level would make it more clear for workers and employers that such workers are not EAP exempt.<sup>399</sup>

<sup>398</sup> See 84 FR 51279–80; 81 FR 32463; 69 FR 22213.

<sup>399</sup> See 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. RAND conducted a survey to identify the number of workers who may have failed the

Second, this proposed rule could potentially lead to increased worker productivity if workers receive an increase in compensation. Increased productivity could occur through numerous channels, such as employee retention and level of effort. A strand of economic research, commonly referred to as “efficiency wage” theory, considers how an increase in compensation may be met with greater productivity.<sup>400</sup> Efficiency wages may elicit greater effort on the part of workers, making them more effective on the job.<sup>401</sup> Other research on increases in the minimum wage have demonstrated a positive relationship between increased compensation and worker productivity. For example, Kim and Jang (2019) showed that wage raises increase productivity for up to two years after the wage increase.<sup>402</sup> They found that in both full and limited-service restaurants productivity increased due to improved worker morale after a wage increase.

Additionally, research demonstrates a correlation between increased earnings and reduced employee turnover.<sup>403</sup> Reducing turnover, in turn, may increase productivity because new employees have less firm-specific skills and knowledge and thus could be less productive and require additional

standards duties test and yet are classified as EAP exempt. The survey, a special module to the American Life Panel, asked respondents: (1) their hours worked, (2) whether they are paid on an hourly or salary basis, (3) their typical earnings, (4) whether they perform certain job responsibilities that are treated as proxies for whether they would justify exempt status, and (5) whether they receive any overtime pay. Using these data, Rohwedder and Wenger found that “11.5 percent of salaried workers were classified as exempt by their employer although they did not meet the criteria for being so.” This survey was conducted when the salary level was \$455. The exact percentage may no longer be applicable, but the concern that in some instances the duties test may be misapplied remains.

<sup>400</sup> Akerlof, G.A. (1982). Labor Contracts as Partial Gift Exchange. *The Quarterly Journal of Economics*, 97(4), 543–569.

<sup>401</sup> Another model of efficiency wages, which is less applicable here, is the adverse selection model in which higher wages raise the quality of the pool of applicants.

<sup>402</sup> Kim, H.S., & Jang, S. (2019). Minimum Wage Increase and Firm Productivity: Evidence from the Restaurant Industry. *Tourism Management* 71, 378–388. <https://doi.org/10.1016/j.tourman.2018.10.029>.

<sup>403</sup> 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. IRL Working Paper #149–13.

<sup>404</sup> 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.

supervision and training.<sup>405</sup> Reduced turnover could 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 because the higher wages may be offset by increased productivity and reduced hiring costs for firms.

Third, this rulemaking could result in an increase in personal time for some workers. Due to the increase in marginal cost for overtime hours for newly overtime-eligible workers, employers could demand fewer hours from some of the workers affected by this rulemaking. If these workers’ pay remains the same, they could benefit from increased personal time and improved work-life balance. Empirical evidence shows that workers in the United States typically work more than workers in other comparatively wealthy countries.<sup>406</sup> Although estimates of the actual level of overwork vary considerably, workers in executive, administrative, and professional occupations tend to work longer hours.<sup>407</sup> They also have the highest percentage of workers who would prefer to work fewer hours compared to other occupational categories.<sup>408</sup> Therefore, the Department believes that this proposed rule may result in reduced time spent working for a group of workers, some of whom may prefer such an outcome.

## 6. Sensitivity Analysis of Transfer Payments

Because the Department cannot predict employers’ precise reactions to the proposed rule, the Department calculated bounds on the size of the estimated transfers from employers to workers, relative to the primary estimates in this RIA. For the upper bound, the Department assumed that the

<sup>405</sup> 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.

<sup>406</sup> For more information, see OECD series, average annual hours actually worked per worker, available at: <http://stats.oecd.org/index.aspx?DataSetCode=ANHRS>.

<sup>407</sup> Boushey, H. and Ansel, B. (2016). Overworked America, The economic causes and consequences of long work hours. Washington Center for Equitable Growth. <https://equitablegrowth.org/research-paper/overworked-america/?longform=true>.

<sup>408</sup> 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).

full overtime premium model is more likely to occur than in the primary model. For the lower bound, the Department assumed that the complete fixed-job model is more likely to occur than in the primary model. Based on these assumptions, estimated transfers may range from \$557.3 million to \$2.4 billion, with the primary estimate equal to \$1.2 billion.

For a reasonable 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 will work the same number of hours but be paid

1.5 times their implicit initial hourly wage for all overtime hours) (Table 20). The full overtime premium model is a special case of the fixed-wage model where there is no change in hours. For the other half of regular overtime workers, the Department assumed in the upper-bound method that they would have their implicit hourly wage adjusted as predicted by the incomplete fixed-job model (wage rates fall and hours are reduced but total earnings continue to increase, as in the primary method). In the primary model, the Department assumed that only 50 percent of occasional overtime workers and no

regular overtime workers would receive the full overtime premium.

The plausible lower bound on transfer payments 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 assumed the employees' wages would fully adjust as predicted by the fixed-job model.<sup>409</sup> For the other half of employees with occasional overtime hours, the lower bound assumes they would be paid one and one-half times their implicit hourly wage for overtime hours worked (full overtime premium).

TABLE 20—SUMMARY OF THE ASSUMPTIONS USED TO CALCULATE THE LOWER ESTIMATE, PRIMARY ESTIMATE, AND UPPER ESTIMATE OF TRANSFERS

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

\* Full overtime premium model: Regular rate of pay equals the implicit hourly wage prior to the regulation (with no adjustments); workers are paid 1.5 times this base wage for the same number of overtime hours worked prior to the regulation.

\* Fixed-job model: Base wages are set at the higher of: (1) a rate such that total earnings and hours remain the same before and after the regulation; thus the base wage falls, and workers are paid 1.5 times the new base wage for overtime hours (the fixed-job model) or (2) the minimum wage.

\* Incomplete fixed-job model: Regular rates of pay are partially adjusted to the wage implied by the fixed-job model.

## 7. Effects by Regions and Industries

This section compares the number of affected workers, costs, and transfers across regions and industries. Although impacts would be more pronounced in some regions or industries, the Department has concluded that in no region or industry are the costs overly burdensome. The proportion of total costs and transfers in each region would be fairly consistent with the proportion of total workers in each region. Affected workers are overrepresented in some industries, but costs and transfers would still be manageable as a share of payroll and of total revenue (*See* Table 24 for regions and Table 27 for industries).

The Department also compared costs and transfers relative to total payrolls and revenues. This provides a common method of assessing the relative effects of the rule on different regions or

industries, and the magnitude of adjustments the rule may require on the part of enterprises in each region or 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 a region or industry because they benchmark against the cost category directly associated with the labor force. Average estimated costs and transfers from this proposed rule are very small relative to current payroll or current revenue—less than a tenth of a percent of payroll and of revenue in each region and in each industry.

Salaries vary across the U.S. geographically. To ensure the proposed standard salary level would not be too high in any region of the country, the Department has used only wages in the lowest-wage region, the South, to set the salary level. However, because wages

are lower in the South and the Midwest than the Northeast and the West, impacts may be larger in these two lower-wage regions. This section considers impacts across the four Census regions to ensure the impacts in the lower-wage regions would be manageable. The South has by far the most affected workers (1.5 million), though it also has the most workers of any Census region (Table 21). As a share of potentially affected workers in the region, the South would have somewhat more affected workers relative to other regions (15.2 percent are affected compared with 10.3 to 13.7 percent in other regions). However, as a share of all workers in the region, the South would not be particularly affected relative to other regions (2.9 percent are affected compared with 2.1 to 2.6 percent in other regions).

<sup>409</sup> The straight-time wage adjusts to a level that keeps weekly earnings constant when overtime

hours are paid at 1.5 times the straight-time wage. In cases where adjusting the straight-time wage

results in a wage less than the minimum wage, the straight-time wage is set to the minimum wage.

TABLE 21—POTENTIALLY AFFECTED AND AFFECTED WORKERS, BY REGION, YEAR 1

Region	Workers subject to FLSA (millions)	Potentially affected workers (millions) <sup>a</sup>	Affected workers (millions) <sup>b</sup>	Affected workers as a percent of potentially affected workers %	Affected workers as a percent of all workers %
All .....	139.4	28.4	3.6	12.9	2.6
Northeast .....	24.8	5.7	0.6	11.1	2.6
Midwest .....	30.4	5.9	0.8	13.7	2.6
South .....	51.4	9.9	1.5	15.2	2.9
West .....	32.8	6.9	0.7	10.3	2.1

**Note:** Pooled CPS data for 2020–2022 adjusted to reflect 2022.

<sup>a</sup> EAP exempt workers who are white-collar, salaried, not eligible for another (non-EAP) overtime exemption, and not in a named occupation.

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

Total transfers in the first year were estimated to be \$1.2 billion (Table 22). As expected, the transfers in the South would be the largest portion because the

largest number of affected workers would be in the South. However, transfers per affected worker would be on the low-end in the South. Annual

transfers per worker would be \$328 in the South, and between \$332 and \$357 in other regions.

TABLE 22—ANNUAL TRANSFERS BY REGION, YEAR 1

Region	Total annual change in earnings (millions)	Annual transfer per affected worker	Annual transfers per entity	Percent of total transfers by region (%)
All .....	\$1,234.2	\$338	\$153	100.0
Northeast .....	211.2	332	143	17.1
Midwest .....	279.1	347	166	22.6
South .....	492.8	328	169	39.9
West .....	251.1	357	125	20.3

**Note:** Pooled CPS data for 2020–2022 adjusted to reflect 2022.

TABLE 23—ANNUAL COSTS BY REGION, YEAR 1

Region	Total direct costs (millions)	Total direct costs per entity	Percent of total direct costs by region (%)
All .....	\$1,202.8	\$149	100.0
Northeast .....	202.8	137	16.9
Midwest .....	278.5	165	23.2
South .....	470.5	161	39.1
West .....	251.1	125	20.9

**Note:** Pooled CPS data for 2020–2022 adjusted to reflect 2022.

Direct employer costs are composed of regulatory familiarization costs, adjustment costs, and managerial costs. The Department estimates that total direct employer costs would be the highest in the South (\$470.5 million) and lowest in the Northeast (\$202.8 million). Transfers and direct employer costs in each region, as a percentage of the total transfers and direct costs, would range from 17.0 percent in the Northeast to 39.5 percent in the South.

These proportions are almost the same as the proportions of the total workforce in each region: 17.8 percent in the Northeast and 36.9 percent in the South. Costs and transfers per establishment would be slightly higher in the South (\$330) than on average, but still small (Table 24).

Another way to compare the relative effects of this proposed rule by region is to consider the transfers and costs as a proportion of payroll and revenues

(Table 24).<sup>410</sup> Nationally, employer costs and transfers would be approximately 0.027 percent of payroll. By region, direct employer costs and transfers as a percent of payroll would be approximately the same (between 0.021 and 0.032 percent of payroll). Employer costs and transfers as a percent of revenue would be 0.005 percent nationally and range between 0.004 and 0.006 percent in each region.

<sup>410</sup> The Department uses 2017 data here because although payroll data are available for 2021, the most recent revenue data are for 2017.

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

Region	Transfers and costs per entity	Payroll (billions) <sup>a</sup>	Revenue (billions) <sup>a</sup>	Costs and transfers	
				As percent of payroll (%)	As percent of revenue (%)
All .....	\$301	\$9,141	\$48,894	0.027	0.005
Northeast .....	279	1,940	9,557	0.021	0.004
Midwest .....	331	1,879	10,884	0.030	0.005
South .....	330	3,028	17,193	0.032	0.006
West .....	250	2,295	11,260	0.022	0.004

<sup>a</sup> Payroll and revenue data exclude the Federal Government.

Sources: Costs and transfers based on pooled CPS data for 2020–2022 adjusted to reflect 2022. Private sector payroll and revenue data from 2017 SUBS. State and local payroll and revenue data from State and Local Government Finances 2020. Inflated to \$2022 using GDP deflator.

Impacts may be more pronounced in some industries. In particular, lower-wage industries where more workers may earn between \$684 and the proposed new salary level may be impacted more. Additionally, industries where EAP workers are more prevalent may experience larger impacts. To gauge the effect of the proposed rule on industries, the Department estimated affected workers, costs, and transfers for

the 13 major industry groups. The Department also compared estimates of combined costs and transfers as a percent of payroll and revenue across industries.

Table 25 presents the number of affected workers by industry. The industry with the most affected workers is professional and business services (687,400). The industry with the largest share of workers affected is financial

activities (4.9 percent). This is because the financial activities industry is heavily composed of salaried white-collar workers. As a share of potentially affected workers, the industry with the highest share affected is agriculture, forestry, fishing, & hunting (22.1 percent), followed by leisure and hospitality (21.1 percent).

TABLE 25—POTENTIALLY AFFECTED AND AFFECTED WORKERS, BY INDUSTRY, YEAR 1

Industry	Workers subject to FLSA (1,000s)	Potentially affected workers (1,000s) <sup>a</sup>	Affected workers (1,000s) <sup>b</sup>	Affected workers as a percent of potentially affected workers (%)	Affected workers as a percent of all workers (%)
All .....	139,397.0	28,359.5	3,648.3	12.9	2.6
Agriculture, forestry, fishing, & hunting .....	1,331.5	55.6	12.3	22.1	0.9
Mining .....	619.5	171.1	12.5	7.3	2.0
Construction .....	8,914.6	1,188.4	154.4	13.0	1.7
Manufacturing .....	15,129.2	3,900.8	317.1	8.1	2.1
Wholesale trade .....	3,226.4	850.5	103.9	12.2	3.2
Retail trade .....	15,381.2	1,853.1	308.7	16.7	2.0
Transportation & utilities .....	8,507.1	1,033.5	118.9	11.5	1.4
Information .....	2,559.2	962.4	118.6	12.3	4.6
Financial activities .....	9,851.4	4,250.7	480.7	11.3	4.9
Professional & business services .....	16,784.2	6,754.2	687.4	10.2	4.1
Education .....	14,017.6	1,121.0	201.8	18.0	1.4
Healthcare & social services .....	20,534.6	3,599.7	626.9	17.4	3.1
Leisure & hospitality .....	11,597.6	869.1	183.5	21.1	1.6
Other services .....	5,314.5	736.5	139.2	18.9	2.6
Public administration .....	5,628.3	1,012.9	182.4	18.0	3.2

**Note:** Pooled CPS data for 2020–2022 adjusted to reflect 2022.

<sup>a</sup> EAP exempt workers who are white-collar, salaried, not eligible for another (non-EAP) overtime exemption, and not in a named occupation.

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

Both transfers and costs would be the largest in the professional and business services industry because this industry is large and heavily composed of salaried white-collar workers (Table 26). Combined, in Year 1, these total \$471.7

million and represent 19.4 percent of nationwide transfers and costs. Transfers and costs are also large in the healthcare and social services industry, at least partially due to the large size of this industry. However, transfers per

affected worker would be relatively low in this industry, \$251 in the first year compared with \$338 nationally. A third industry with relatively large total transfers and costs is the financial activities industry.



TABLE 26—ANNUAL TRANSFERS AND COSTS BY INDUSTRY, YEAR 1

Industry	Transfers (millions)	Transfer per affected worker	Direct costs (millions) <sup>a</sup>	Transfers and costs (millions)	Percent of total transfers and costs by industry (%)
All .....	\$1,234.2	\$338	\$1,202.1	\$2,436.3	100.0
Agriculture, forestry, fishing, & hunting .....	4.2	341	3.2	7.4	0.3
Mining .....	2.9	234	2.6	5.6	0.2
Construction .....	49.1	318	74.0	123.2	5.1
Manufacturing .....	114.0	360	91.9	205.9	8.5
Wholesale trade .....	42.9	413	46.3	89.2	3.7
Retail trade .....	148.8	482	138.7	287.6	11.8
Transportation & utilities .....	46.3	389	37.0	83.3	3.4
Information .....	34.5	290	32.3	66.7	2.7
Financial activities .....	144.3	300	143.2	287.5	11.8
Professional & business services .....	250.7	365	221.0	471.7	19.4
Education .....	54.3	269	42.2	96.5	4.0
Healthcare & social services .....	157.5	251	164.0	321.5	13.2
Leisure & hospitality .....	86.8	473	99.2	186.1	7.6
Other services .....	35.6	256	69.5	105.1	4.3
Public administration .....	62.2	341	37.0	99.2	4.1

Sources: Pooled CPS data for 2020–2022 adjusted to reflect 2022.

<sup>a</sup> Regulatory familiarization costs exclude 13,981 establishments whose industry is “not classified.”

To measure the impact on businesses, a comparison of transfers and costs to payroll, revenue, or profit is more helpful than looking at the absolute size of transfers and costs per industry. As a percent of payroll, transfers and costs would be highest in agriculture, forestry, fishing, and hunting; education; and retail trade (Table 27). However, the magnitude of the relative shares would be small, representing less than 0.1 percent of payroll costs in all industries. The Department’s estimates of transfers and costs as a percent of revenue by industry also indicated a very small effect of less than 0.02 percent of revenues in any industry. The

industries with the largest transfers and costs as a percent of revenue would be education; agriculture, forestry, fishing, and hunting; and professional and business services. Table 27 illustrates that the differences in costs and transfers relative to revenues would be quite small across industry groupings.

The overall magnitude of costs and transfers as a percentage of profits represents less than 1.0 percent of overall profits in each industry.<sup>411 412</sup> By industry, the value of total costs and transfers as a percent of profits ranges from a low of .02 percent (wholesale trade) to a high of 0.71 percent (agriculture, forestry, fishing, and

hunting). Benchmarking against profits is potentially helpful in the sense that it provides a measure of the proposed 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 profit impacts reflecting cross-industry variation in market structure.<sup>413</sup>

TABLE 27—ANNUAL TRANSFERS, TOTAL COSTS, AND TRANSFERS AND COSTS AS PERCENT OF PAYROLL, REVENUE, AND PROFIT BY INDUSTRY, YEAR 1

Industry	Costs and transfers per entity	Payroll (billions) <sup>a</sup>	Revenue (billions) <sup>a</sup>	Costs and transfers as percent of:		
				Payroll <sup>a</sup>	Revenue <sup>a</sup>	Profit <sup>a</sup>
All .....	\$301.7	\$9,140.5	\$48,894.1	0.027	0.005	0.052
Agriculture, forestry, fishing, & hunting .....	323.5	8.3	41.0	0.089	0.018	0.709
Mining .....	233.0	59.7	476.5	0.009	0.001	<sup>b</sup>
Construction .....	163.5	471.2	2,346.7	0.026	0.005	0.090
Manufacturing .....	726.1	805.8	6,522.0	0.026	0.003	0.030
Wholesale trade .....	228.1	512.7	10,287.6	0.017	0.001	0.020
Retail trade .....	277.4	524.6	5,773.6	0.055	0.005	0.154
Transportation & utilities .....	300.4	369.0	1,719.9	0.023	0.005	0.257
Information .....	414.6	421.2	1,860.4	0.016	0.004	0.022

<sup>411</sup> Internal Revenue Service. (2023). SOI Tax Stats—Corporation Income Tax Returns Complete Report (Publication 16). Available at: <https://www.irs.gov/statistics/soi-tax-stats-corporation-income-tax-returns-complete-report-publication-16>.

<sup>412</sup> Table 1 of the IRS report provides total receipts, net income, and deficits by industry. For each industry, the Department calculated the profit-to-revenue ratio as net income (column (7)) less any

deficit (column (8)) divided by total receipts (column (3)). Profits were then calculated as revenues multiplied by profit-to-revenue ratios. Profits could not be used directly because they are limited to only active corporations.

<sup>413</sup> In particular, a basic model of competitive product markets would predict that highly competitive industries with lower rates of return would adjust to increases in the marginal cost of

labor arising from the rule through an overall, industry-level increase in prices and a reduction in quantity demanded based on the relative elasticities of supply and demand. Alternatively, more concentrated markets with higher rates of return would be more likely to adjust through some combination of price increases and profit reductions based on elasticities as well as interfirm pricing responses.

TABLE 27—ANNUAL TRANSFERS, TOTAL COSTS, AND TRANSFERS AND COSTS AS PERCENT OF PAYROLL, REVENUE, AND PROFIT BY INDUSTRY, YEAR 1—Continued

Industry	Costs and transfers per entity	Payroll (billions) <sup>a</sup>	Revenue (billions) <sup>a</sup>	Costs and transfers as percent of:		
				Payroll <sup>a</sup>	Revenue <sup>a</sup>	Profit <sup>a</sup>
Financial activities .....	314.4	896.4	5,881.0	0.032	0.005	0.023
Professional & business services .....	330.6	1,888.7	3,451.6	0.025	0.014	0.122
Education .....	876.2	168.8	484.3	0.057	0.020	0.310
Healthcare & social services .....	346.4	1,175.4	2,986.5	0.027	0.011	0.144
Leisure & hospitality .....	210.1	423.4	1,429.5	0.044	0.013	0.158
Other services .....	136.3	213.5	850.6	0.049	0.012	0.183
Public administration .....	1,100.1	1,201.8	4,782.8	0.008	0.002	<sup>c</sup>

Sources: Pooled CPS data for 2020–2022 adjusted to reflect 2022. Private sector payroll and revenue data from 2017 SUSB. State and local payroll and revenue data from State and Local Government Finances 2020 are used for the Public Administration industry. Profit-to-revenue data from the Internal Revenue Service 2019. Inflated to \$2022 using GDP deflator.

<sup>a</sup> Payroll and revenue data exclude the Federal Government. Profit-to-revenue data limited to active corporations. Regulatory familiarization costs, payrolls, and revenues exclude 13,981 establishments whose industry is “not classified.” Because transfer payments include all workers, the estimates of costs and transfers as a share of payroll or revenue are slightly overestimated.

<sup>b</sup> Profits were negative in this industry in this year.

<sup>c</sup> Profit is not applicable for public administration.

## 8. Regulatory Alternatives

The Department considered a range of alternatives before selecting its methods for updating the standard salary level and the HCE compensation level (see section IV.A.5). As seen in Table 28, the Department has calculated the salary/compensation levels, the number of affected workers, and the associated costs and transfers for these alternative levels.

The Department proposes to update the standard salary level using earnings for the 35th percentile of full-time salaried workers in the South Census region, \$1,059 per week. The alternative methods considered for setting the standard salary level are:

- Alternative 1: 2004/2019 method—\$822 per week—20th percentile of earnings of nonhourly full-time workers in the South Census region and in the retail industry nationally.

- Alternative 2: Kantor long test method—\$925 per week—10th percentile of earnings of likely exempt workers.

- Alternative 3: 2016 method—\$1,145 per week—40th percentile of earnings of nonhourly full-time workers in the South Census region

- Alternative 4: Kantor short test method—\$1,378 per week—Kantor long test level multiplied by 149 percent (the historical average relationship between the long and short test levels).

The Department considered using the 2004 methodology (the 20th percentile of full-time salaried white-collar workers in the lowest-wage Census region (currently the South) and in retail nationally), which is currently \$822 per week (\$42,744 per year). This is also the methodology that the Department used in the 2019 rule.<sup>414</sup> However, the salary

level produced by the 2004 methodology is below the current equivalent long test salary level (\$925 per week), which the Department considers to be the lower boundary for an appropriate salary level.

The Department also considered setting the standard salary level at the long test level (\$925 per week or \$48,100 per year). Doing so would ensure the initial screening function of the salary level by restoring overtime protections to those employees who were consistently excluded from the EAP exemption under each iteration of the regulations prior to 2019, either by the long test salary level itself, or under the 2004 rule salary level, which was set equivalent to the long test salary level.<sup>415</sup> However, as explained above, setting the standard salary level at the long test level would perpetuate the problems that have become evident under the 2004 and 2019 rules.

The Department also considered setting the standard salary level at the 40th earnings percentile of salaried white-collar workers in the lowest-wage Census Region (currently the South) (\$1,145 per week or \$59,540 per year). This salary level is roughly the midpoint between the long and short test salary level alternatives (\$925 per week and \$1,378 per week, respectively). However, the Department is concerned that this approach could be seen by courts as making salary level determinative of exemption status for too large a portion of employees, as this salary level would make the salary paid by the employer determinative of exemption status for roughly half (47%) of white-collar employees who earn between the long and short test salary levels. The Department is also

concerned that this approach would generate the same concerns that led to the district court decision invalidating the 2016 rule (which adopted the same methodology).

Finally, the Department considered setting the standard salary level at the current equivalent of the short test salary level (\$1,378 per week or \$71,656 per year).<sup>416</sup> This would ensure that all employees who earn between the long and short test salary levels and perform substantial amounts of nonexempt work would be entitled to overtime compensation. However, by making exemption status for all employees who earn between the long and short test levels depend on the salary paid by the employer, this approach would prevent employers from being able to use the EAP exemption for employees earning between these salary levels who do not perform substantial amounts of nonexempt work and thus were historically exempt under the long test.

As described above, the Department proposes to update the HCE compensation level using earnings for the 85th percentile of all full-time salaried workers nationally, \$143,988 per year. The Department also evaluated the following alternative methods to set the HCE compensation levels:

- HCE alternative 1: 2019 method <sup>417</sup>—\$125,268 annually—80th percentile of earnings of nonhourly full-time workers nationally.

- HCE alternative 2: 2016 method <sup>418</sup>—\$172,796 annually—90th percentile of earnings of nonhourly full-time workers nationally.

The Department believes that HCE alternative 1 would not produce a

<sup>416</sup> See *id.*

<sup>417</sup> See 81 FR 32429.

<sup>418</sup> See 84 FR 51250.

<sup>414</sup> 84 FR 51260.

<sup>415</sup> See section IV.A.1.

threshold high enough to reserve the HCE test for employees at the top of today's economic ladder and ensure that the HCE threshold continues to appropriately complement the minimal HCE duties test. The Department also considered setting the HCE threshold at the 90th percentile; however, the

Department is concerned that the resulting level (\$172,796) would restrict the use of the HCE exemption for employers in low-wage regions and industries. The Department believes its proposal to adjust the HCE total annual compensation threshold to reflect the 85th percentile of earnings of nonhourly

full-time workers nationally strikes the appropriate balance and ensures that the HCE test continues to serve its intended function as a streamlined alternative for employees who are highly likely to pass the standard duties test.

TABLE 28—UPDATED STANDARD SALARY AND HCE COMPENSATION LEVELS AND ALTERNATIVES, AFFECTED EAP WORKERS, COSTS, AND TRANSFERS, YEAR 1

Alternative	Salary level	Affected EAP workers (1,000s)	Year 1 effects (millions)	
			Adj. & mana- gerial costs	Transfers
Standard Salary Level (Weekly)				
Alt. #1: 2004/2019 method <sup>a</sup> .....	\$822	825	\$159.0	\$170.8
Alt #2: Kantor long test <sup>b</sup> .....	925	1,773	367.4	456.8
Proposed rule: 35th percentile South <sup>c</sup> .....	1,059	3,399	709.8	980.7
Alt. #3: 2016 method—40th percentile South <sup>c</sup> .....	1,145	4,312	955.2	1,415.9
Alt. #4: Kantor short test <sup>d</sup> .....	1,378	7,640	1,728.3	3,136.6
HCE Compensation Level (Annually)				
HCE alt. #1: 2019 method—80th percentile <sup>e</sup> .....	125,268	166	43.1	151.6
Proposed rule: 85th percentile <sup>e</sup> .....	143,988	249	65.9	253.5
HCE alt. #2: 2016 method—90th percentile <sup>e</sup> .....	172,796	295	84.0	330.0

**Note:** Regulatory familiarization costs are excluded because they do not vary based on the selected values of the salary levels. Additionally, they cannot be disaggregated by exemption type (*i.e.*, standard versus HCE). The Department requests comment on how to refine familiarization cost estimates in a manner that distinguishes among regulatory alternatives.

<sup>a</sup> 20th percentile earnings of nonhourly full-time workers in the South Census region and retail industry (excludes workers not subject to the FLSA, not subject to the salary level test, and in agriculture or transportation). Pooled CPS data for 2020–2022 adjusted to reflect 2022.

<sup>b</sup> 10th percentile earnings of likely exempt workers. Pooled CPS data for 2020–2022 adjusted to reflect 2022.

<sup>c</sup> Designated percentile of earnings of nonhourly full-time workers in the South Census region (excludes workers not subject to the FLSA, not subject to the salary level test, and in agriculture or transportation). CPS 2022 data.

<sup>d</sup> Kantor short test is set as the long test level multiplied by 149 percent. This is the historical average relationship between the two levels.

<sup>e</sup> Designated percentile of earnings of nonhourly full-time workers nationally (excludes workers not subject to the FLSA, not subject to the salary level test, and in agriculture or transportation). CPS 2022 data.

## 9. Automatic Updates

Between updates to the standard salary and HCE compensation levels, 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 salary and compensation levels allows these thresholds to keep pace with changes in earnings and continue to serve as an effective dividing line between potentially exempt and nonexempt workers. Furthermore, automatically updating the salary and compensation levels will provide employers more certainty in knowing that these levels will change by smaller amounts on a regular basis, rather than the more disruptive increases caused by much larger changes after longer, uncertain increments of time. This would allow

firms to better predict short- and long-term costs and employment needs.

The Department is including in this proposed rule a mechanism for automatically updating the salary and compensation levels every 3 years to reflect current earnings. For purposes of this analysis, the Department assumes that the standard salary would be updated using the same methodology that the Department proposes to use to set the standard salary level: the 35th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region (currently the South). Likewise, the Department assumes that the HCE annual compensation level would be updated using the same methodology the Department proposes to use to set this earnings threshold: the 85th percentile of weekly earnings of full-time salaried workers nationally.

As previously discussed, future automatic updates will set the earnings thresholds using the most recent 12 months of CPS data preceding the Department's notice to automatically update the thresholds. To estimate

future thresholds in years when the salary and compensation levels will be updated, the Department used the historic geometric growth rate between 2011 and 2021 in (1) the 35th earnings percentile of full-time salaried workers in the South for the standard salary level and (2) the 85th earnings percentile of full-time salaried workers nationally for the HCE compensation level. For example, between 2011 and 2021, the annual growth rate in the 35th percentile of full-time salaried workers in the South has increased by 2.72 percent. To estimate the first automatic update salary level of \$1,148, the Department multiplied \$1,059 by 1.0272 to the power of three. Figure 5 shows the projected automatic update levels for the first 10 years. Note that these projections are illustrative estimates based on past wage growth; the actual level at the time of the update will depend on the wage growth that occurs between now and the update date. Figure 6 shows the standard salary levels in both nominal and 2022 dollars.

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Figure 5: Projected Future Salary and Compensation Levels, Nominal Dollars

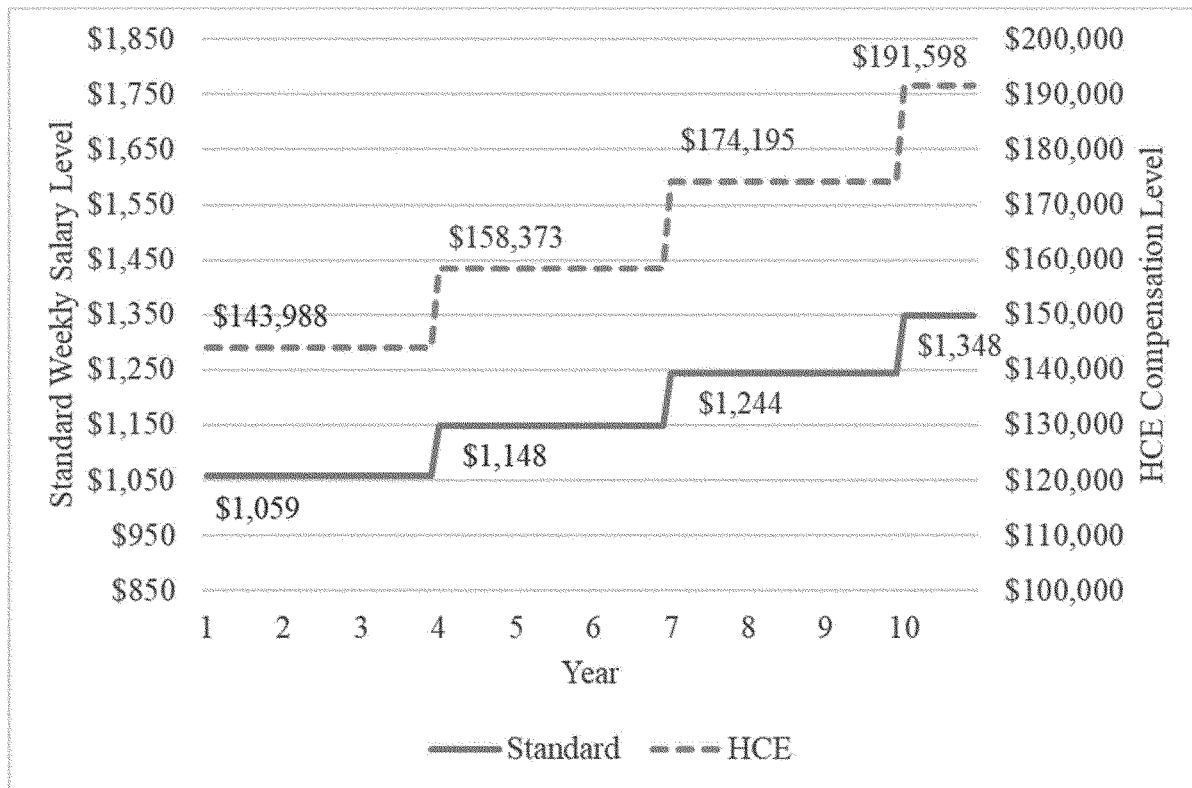
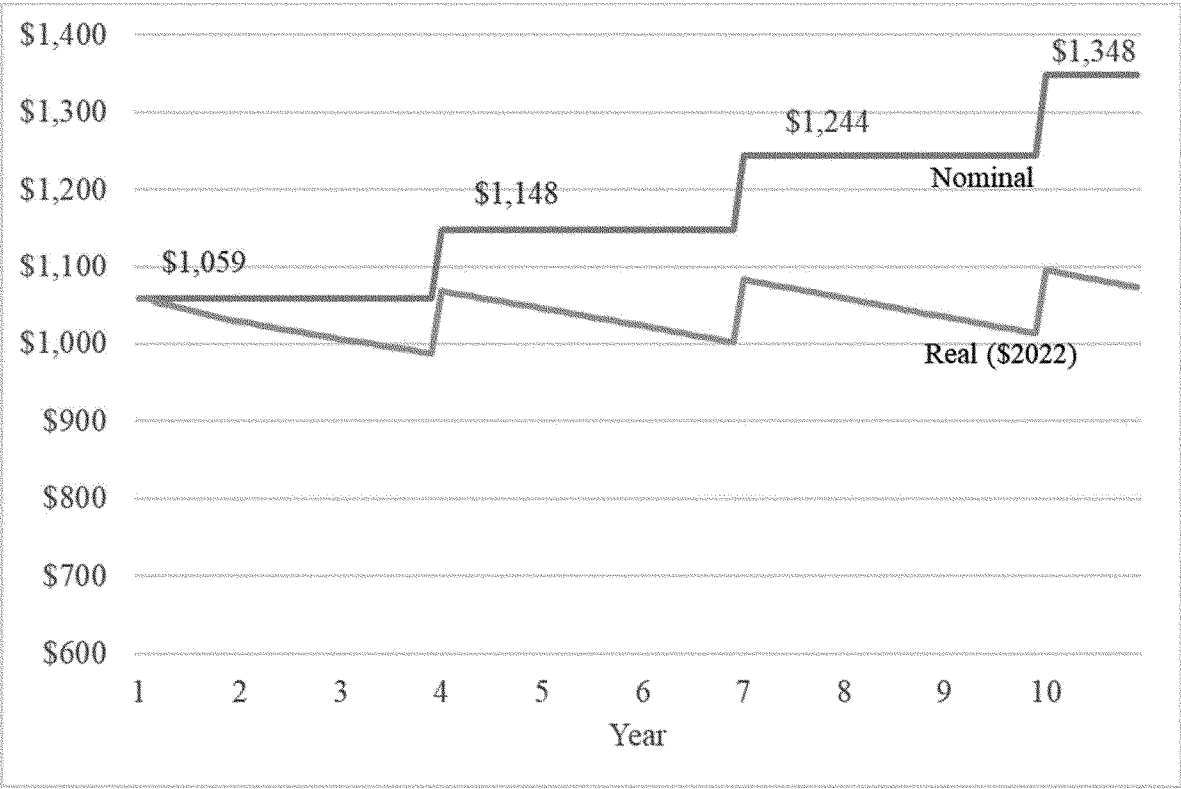


Figure 6: Projected Future Standard Salary Levels, Nominal and Real (Constant 2022 Dollars)



10. Projections

The Department estimated that in Year 1, 3.6 million EAP workers would be affected, with about 248,900 of these attributable to the revised HCE compensation level (Table 29). In Year 10, the number of affected EAP workers was estimated to equal 5.1 million with 768,700 attributable to the updated HCE

compensation level. Average annualized costs are \$664 million and transfers are \$1.3 billion using a 7 percent real discount rate. These projections involved several steps.

1. Use past growth in the earnings distribution to estimate future salary and compensation levels (*see* section VII.C.9).

- 2. Predict workers’ earnings, absent a change in the salary levels.
- 3. Compare workers’ predicted earnings to the predicted salary and compensation levels to estimate affected workers.
- 4. Project future employment levels.
- 5. Estimate employer adjustments to hours and pay.
- 6. Calculate costs and transfers.

Figure 7: 10-Year Projected Number of Affected Workers

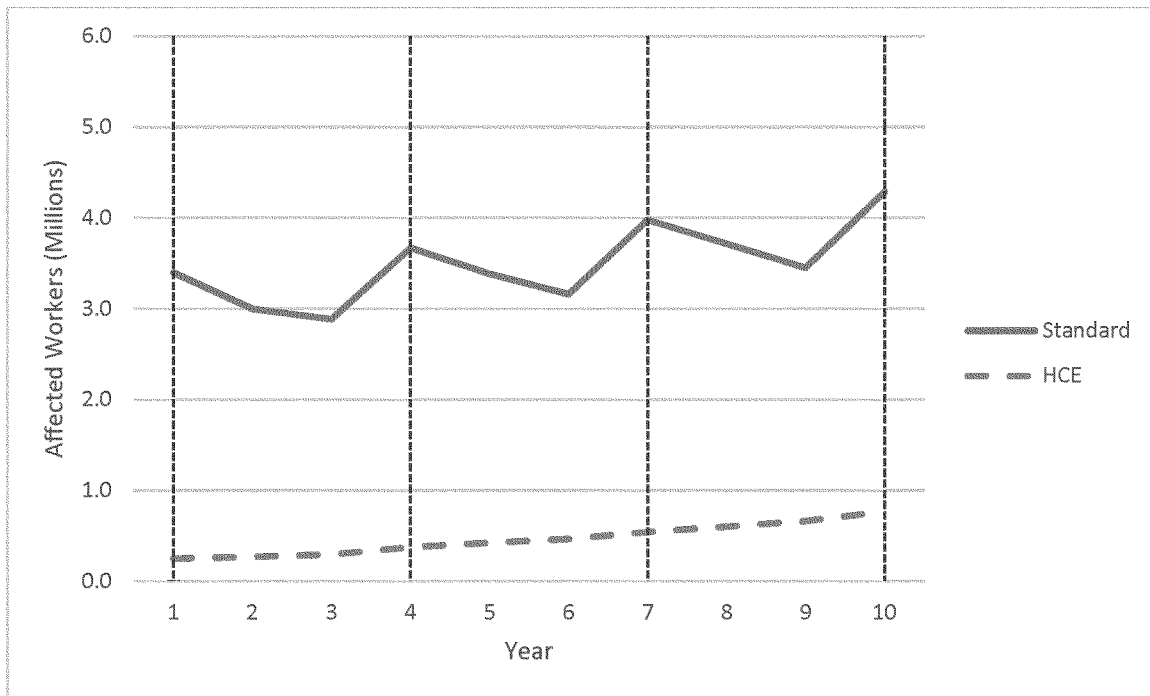


Figure 8: 10-Year Projected Costs and Transfers (Millions \$2022)

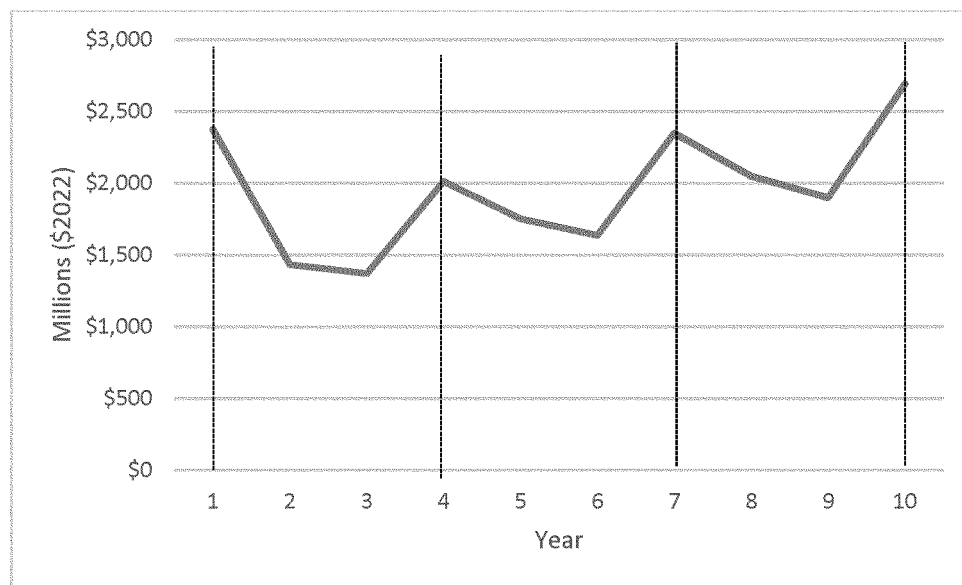


TABLE 29—PROJECTED COSTS AND TRANSFERS, STANDARD SALARY AND HCE COMPENSATION LEVELS

Year	Affected EAP workers (millions)	Costs (millions \$2022)				Transfers (millions \$2022)		
		Regulatory familiarization <sup>a</sup>	Adjustment <sup>a</sup>	Managerial	Total	Due to MW	Due to OT	Total
Year 1 .....	3.6	\$427.2	\$240.8	\$534.9	\$1,202.8	\$48.6	\$1,185.6	\$1,234.2
Year 2 .....	3.3	0.0	8.1	500.2	508.3	27.1	921.8	949.0
Year 3 .....	3.2	0.0	7.7	470.5	478.2	23.6	891.5	915.1
Year 4 .....	4.0	69.1	11.1	561.5	641.6	20.5	1,382.0	1,402.5
Year 5 .....	3.8	0.0	8.2	534.0	542.2	23.2	1,212.2	1,235.4
Year 6 .....	3.6	0.0	7.2	524.6	531.8	23.0	1,107.3	1,130.3
Year 7 .....	4.5	67.1	12.2	620.1	699.3	23.6	1,661.2	1,684.8
Year 8 .....	4.3	0.0	7.1	583.1	590.2	19.8	1,467.4	1,487.2
Year 9 .....	4.1	0.0	7.9	566.5	574.4	20.1	1,332.6	1,352.8
Year 10 .....	5.1	65.1	15.0	667.9	748.0	17.2	1,963.9	1,981.2
Annualized (3% real discount rate) .....		67.9	35.7	552.8	656.4	25.2	1,292.9	1,318.1
Annualized (7% real discount rate) .....		75.0	40.0	548.5	663.6	25.9	1,268.5	1,294.3

<sup>a</sup> Regulatory familiarization costs occur in years when the salary and compensation levels are updated. Adjustment costs occur in all years when there are newly affected workers.

The Department calculated workers' earnings in future years by applying the historical wage growth rate in the workers' industry-occupation to current earnings. The wage growth rate was calculated as the geometric growth rate in median wages using CPS MORG data for occupation-industry categories from 2010–2022.<sup>419</sup> The geometric growth rate is 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 rate only depends on the wage values in the first and last year.<sup>420</sup>

The geometric wage growth rates per industry-occupation combination were also calculated from the BLS' Occupational Employment and Wage Statistics (OEWS) survey. 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 OEWS data.<sup>421</sup> Any remaining occupation-industry combinations without sufficient data in either data source were assigned the median of the growth rates in median wages from the CPS MORG data.

The Department 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 absent the rule change (*e.g.*, would earn at least \$684 if exempt under standard salary level) but have projected earnings in the future year that are less than the relevant salary level. The projected number of affected workers also includes workers who were not EAP exempt in the base year but would have become exempt in the absence of this proposed rule in Years 2 through 10. For example, a worker who passes the standard duties test may earn less than \$684 in Year 1 but between \$684 and the new salary level in subsequent years; such a worker will be counted as an affected worker in those subsequent years. Additionally, the number of affected workers is not limited to newly affected workers.

Workers who are affected in a given year may remain affected in subsequent years (*e.g.*, because they earn between \$684 and \$1,059 in years 1, 2, and 3), and continue to be counted as affected.

The projected number of affected workers also accounts for anticipated employment growth. Employment

growth was estimated as the geometric annual growth rate based on the 10-year employment projection from BLS' National Employment Matrix (NEM) for 2021 to 2031 within an occupation-industry category.<sup>422 423</sup> The Department applied these growth rates to the sample weights of the workers to estimate increased employment levels over time. This is because the Department cannot introduce new observations to the CPS MORG data to represent the newly employed.

For workers newly affected in Year 2 through Year 10, employers' wage and hour adjustments due to the rulemaking are generally estimated as described in section VII.C.4. The only difference is the hours adjustment now uses a long-run elasticity of labor demand of –0.4.<sup>424</sup> 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).

The Department quantified three types of direct employer costs in the 10-

<sup>422</sup> Bureau of Labor Statistics, Employment Projections Program. 2021–31 National Employment Matrix. <https://www.bls.gov/emp/ind-occ-matrix/matrix.xlsx>.

<sup>423</sup> An alternative method is to spread the total change in the level of employment over the ten years evenly (constant change in the number 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).

<sup>424</sup> Based on the Department's analysis of the following paper:

Lichter, A., Peichl, A. & Sieglösch, A. (2014). The Own-Wage Elasticity of Labor Demand: A Meta-Regression Analysis. IZA DP No. 7958.

<sup>419</sup> To maximize the number of observations used in calculating the median wage for each occupation-industry category, 3 years of data were pooled for each of the endpoint years. Specifically, data from 2010, 2011, and 2012 (converted to 2011 dollars) were used to calculate the 2011 median wage and data from 2020, 2021, and 2022 (converted to 2021 dollars) were used to calculate the 2021 median wage.

<sup>420</sup> The geometric growth rate may be a flawed measure if either or both of the endpoint 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.

<sup>421</sup> 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.

year projections: (1) regulatory familiarization costs; (2) adjustment costs; and (3) managerial costs. Section VII.C.3. provides details on the methodology for estimating these costs. This section only discusses the aspects specific to projections. Projected costs and transfers were deflated to 2022 dollars using the Congressional Budget Office's projections for the CPI-U.<sup>425</sup>

Regulatory familiarization costs occur in years when the salary and compensation levels are updated. Thus, in addition to Year 1, some regulatory familiarization costs are expected to occur in Year 4, Year 7, and Year 10. The Department assumed 10 minutes per establishment for time to access and read the published notice in the **Federal Register** with the updated standard salary level and HCE compensation level. This time estimate is low because the majority of establishments will not have newly affected workers. The time estimate has been increased from 5 minutes in the 2016 rulemaking. In each of these 3 years regulatory familiarization costs are between \$65 and \$70 million. Although start-up firms must become familiar with the FLSA, the difference between the time necessary for familiarization with the current part 541 exemptions and those exemptions as modified by this rulemaking is essentially zero. Therefore, projected regulatory familiarization costs for new entrants over the next 9 years are zero (although these new entrants will incur regulatory familiarization costs in years when the

salary and compensation levels are updated).

Adjustment costs are a function of the number of newly affected EAP workers and would occur in any year in which workers are newly affected. Adjustment costs would be largest in Year 1, of moderate size in automatic update years, and smaller in other years. Management costs would recur each year for all affected EAP workers whose hours are adjusted. Therefore, managerial costs increase in automatic update years and then modestly decrease between updates since earnings growth will cause some workers to no longer be affected in those years.

The Department projected transfers from employers to employees due to the minimum wage provision and the overtime pay provision. Transfers to workers from employers due to the minimum wage provision would decline from \$48.6 million in Year 1 to \$17.2 million in Year 10 as increased earnings over time move workers' regular rates of pay above the minimum wage.<sup>426</sup> Transfers due to overtime pay should grow slightly over time because the number of affected workers would increase, although transfers fall in years between automatic updates. Transfers to workers from employers due to the overtime pay provision would increase from \$1.2 billion in Year 1 to \$2.0 billion in Year 10.

<sup>426</sup> State minimum wages above the Federal level as of January 1, 2022 were incorporated and used for projected years. Increases in minimum wages were not projected. If state or Federal minimum wages increase over the next 10 years, then estimated projected minimum wage transfers would be underestimated.

The Department compared projected impacts with and without automatic updating (Table 30). Projections without automatic updating are shown so impacts of the initial increase and subsequent increases can be disaggregated. With triennial automatic updating, the number of affected EAP workers would increase from 3.6 million to 5.1 million over 10 years. Conversely, in the absence of automatic updating, the number of affected EAP workers is projected to decline from 3.6 million in Year 1 to 2.3 million in Year 10. As shown in Figure 9, the number of affected workers decreases from year to year between automatic updates as the real value of the salary and compensation levels decrease, and then increases in update years.

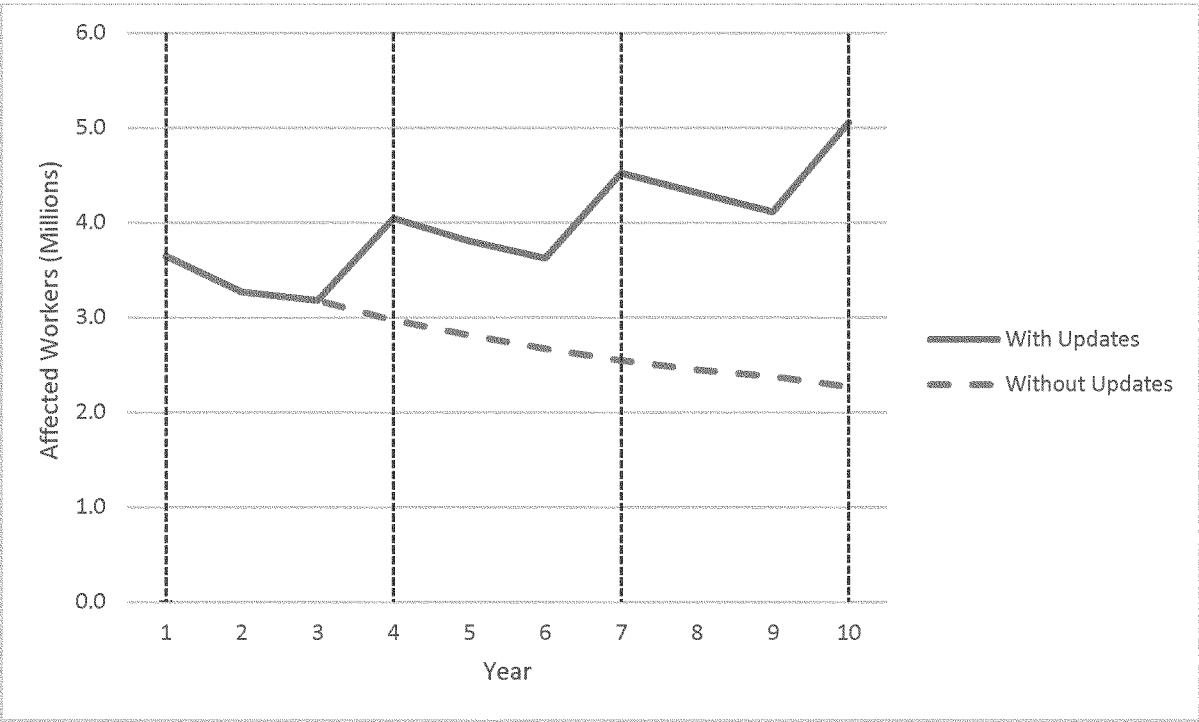
Regarding costs, regulatory familiarization costs are lower without automatic updating because, in the absence of automatic updating, employers would not need to familiarize themselves with updated salary and compensation levels every 3 years. Adjustment costs and managerial costs are a function of the number of affected EAP workers and so will be higher with automatic updating. Average annualized direct costs would be \$663.6 million with automatic updating and \$520.4 million without automatic updating. Transfers are also a function of the number of affected workers and hence are lower without automatic updating. Average annualized transfers would be \$1.3 billion with automatic updating and \$868.2 million without automatic updating. Table 30 shows aggregated costs and transfers over the 10-year horizon.

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<sup>425</sup> Congressional Budget Office. 2023. The Budget and Economic Outlook: 2023 To 2033. See <https://www.cbo.gov/system/files/2023-02/58848-Outlook.pdf>.



Figure 9: 10-Year Projected Number of Affected Workers, with and without Automatic Updating



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TABLE 30—COMPARISON OF PROJECTED COSTS AND TRANSFERS WITH AND WITHOUT AUTOMATIC UPDATING

Year	Affected EAP workers (millions)		Costs (millions \$2022)		Transfers (millions \$2022)	
	With updates	Without updates	With updates	Without updates	With updates	Without updates
Year 1 .....	3.6	3.6	\$1,202.8	\$1,202.8	\$1,234.2	\$1,234.2
Year 2 .....	3.3	3.3	508.3	508.3	949.0	949.0
Year 3 .....	3.2	3.2	478.2	478.2	915.1	915.1
Year 4 .....	4.0	3.0	641.6	442.4	1,402.5	860.7
Year 5 .....	3.8	2.8	542.2	421.7	1,235.4	823.4
Year 6 .....	3.6	2.7	531.8	400.5	1,130.3	800.9
Year 7 .....	4.5	2.5	699.3	374.3	1,684.8	769.9
Year 8 .....	4.3	2.4	590.2	357.6	1,487.2	711.3
Year 9 .....	4.1	2.4	574.4	343.4	1,352.8	677.9
Year 10 .....	5.1	2.3	748.0	322.5	1,981.2	646.8
Annualized (3% real discount rate) .....	.....	.....	656.4	500.2	1,318.1	851.6
Annualized (7% real discount rate) .....	.....	.....	663.6	520.4	1,294.3	868.2

VIII. Initial Regulatory Flexibility Analysis (IRFA)

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 Department has determined that this rulemaking is economically significant. This section (1) provides an overview of the objectives of this proposed rule; (2) estimates the number of affected small entities and employees; (3) discusses reporting, recordkeeping, and other compliance requirements; (4) presents the steps the Department took to minimize the significant economic

impact on small entities; and (5) declares that it is unaware of any relevant Federal rules that may duplicate, overlap, or conflict with this proposed rule.

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

The FLSA requires covered employers to: (1) pay employees who are covered and not exempt from the Act’s requirements not less than the Federal

minimum wage for all hours worked and overtime premium pay at a rate of not less than one and one-half times the employee's regular rate of pay for all hours worked over 40 in a workweek, and (2) make, keep, and preserve records of the persons employed by the employer and of the wages, hours, and other conditions and practices of employment. The FLSA provides exemptions from the Act's minimum wage and overtime pay provisions, including one for bona fide executive, administrative, and professional employees, as those terms are "defined and delimited" by the Department.<sup>427</sup> The Department's regulations implementing this white-collar exemption are codified at 29 CFR part 541.

To qualify for the EAP exemption under the Department's regulations, 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). In 2004, the Department revised its regulations to include a highly compensated employee test with a higher salary threshold and a minimal duties test.<sup>428</sup> The Department has periodically updated the regulations governing the white-collar exemptions since the FLSA's enactment in 1938. Most recently, the 2019 rule updated the standard salary level test to \$684 per week and the HCE compensation level to \$107,432 annually.

The goal of this rulemaking is not only to update the single standard salary level to account for earnings growth since the 2019 rule, but also to build on lessons learned in the Department's most recent rulemakings to more effectively define and delimit employees working in a bona fide EAP capacity. As explained in greater detail in sections III and IV.A., above, setting the standard salary level at or below the long test salary level, as the 2004 and 2019 rules did, results in the exemption of lower-salaried employees who traditionally were entitled to overtime protection under the long test either because of their low salary or because they perform large amounts of nonexempt work, in effect significantly broadening the exemption compared to

the two-test system. Setting the salary level at the lower end of the historic range of short test salary levels, as the 2016 rule did, would have restored overtime protections to those employees who perform substantial amounts of nonexempt work and earned between the long test salary level and the low end of the short test salary range. However, it would also have resulted in denying employers the use of the exemption for lower-salaried employees who traditionally were not entitled to overtime compensation under the long test, which raised concerns that the Department was in effect narrowing the exemption. By setting a salary level above what would currently be the equivalent of the long test salary level, the proposal would restore the right to overtime pay for salaried white-collar employees who prior to the 2019 rule were always considered nonexempt if they earned below the long test (or long test-equivalent) salary level and ensure that fewer lower paid white-collar employees who perform significant amounts of nonexempt work are included in the exemption. At the same time, by setting it below what would currently be the equivalent of the short test salary level, the proposal would allow employers to continue to use the exemption for many lower paid white-collar employees who were made exempt under the 2004 standard duties test. As such, the proposed salary level would also more reasonably distribute between employees and their employers what the Department now understands to be the impact of the shift from a two-test to a one-test system on employees earning between the long and short test salary levels.

As the Department has previously noted, the amount paid to an employee is "a valuable and easily applied index to the 'bona fide' character of the employment for which the exemption is claimed," as well as the "principal[]" "delimiting requirement" "prevent[ing] abuse" of the exemption.<sup>429</sup> Additionally, the salary level test facilitates application of the exemption by saving employees and employers from having to apply the more time-consuming duties analysis to a large group of employees who will not pass it. For these reasons, the salary level test has been a key part of how the Department defines and delimits the EAP exemption since the beginning of its rulemaking on the EAP exemption.<sup>430</sup> At the same time, the salary test's role in defining and delimiting the scope of the EAP

exemption must allow for appropriate examination of employee duties.<sup>431</sup> Under the Department's proposal, duties would continue to determine the exemption status for most salaried white-collar employees, addressing the legal concerns that have been raised about excluding from the EAP exemption too many white-collar employees solely based on their salary level.

The Department also proposes to update the HCE total annual compensation requirement to the annualized weekly earnings for the 85th percentile of full-time salaried workers nationally (\$143,988 in 2022). Though not as high a percentile as the HCE threshold initially adopted in 2004, which covered 93.7 percent of all full-time salaried workers,<sup>432</sup> the Department's proposed increase to the HCE threshold would ensure it continues to serve its intended function, because the HCE total annual compensation level would be high enough to exclude all but those employees at the very top of the economic ladder.

The Department is also proposing to apply the standard salary level to all territories that are subject to the Federal minimum wage, and to update the special salary levels for American Samoa and the motion picture industry in relation to the new standard salary level. Having not increased these levels since 2004, there is a need to increase the salary levels in U.S. territories, particularly for employees in those territories that are subject to the Federal minimum wage.

In its three most recent part 541 rulemakings, the Department has expressed its commitment to keeping the earnings thresholds up to date to ensure that they remain effective in helping differentiate between exempt and nonexempt employees. Long intervals between rulemakings have resulted in eroded earnings thresholds based on outdated earnings data that were ill-equipped to help identify bona fide EAP employees. This rulemaking is motivated in part by the need to keep the part 541 earnings thresholds up to date. Based on its long experience with updating the salary levels, the Department has determined that adopting a regulatory provision for automatically updating the salary levels, with an exception for pausing future updates under certain conditions, is the most viable and efficient way to ensure the EAP exemption earnings thresholds keep pace with changes in employee

<sup>427</sup> 29 U.S.C. 213(a)(1).

<sup>428</sup> § 541.601.

<sup>429</sup> Stein Report at 19, 24; *see also* 81 FR 32422.

<sup>430</sup> *See* 84 FR 51237.

<sup>431</sup> *See id.* at 51238.

<sup>432</sup> *See* 69 FR 22169 (Table 3).

pay and thus remain effective in helping determine exemption status. Accordingly, the Department is including in this proposed rule a mechanism for automatically updating the salary and compensation levels every 3 years to reflect current earnings. As explained in greater detail in section IV.D., employees and employers alike would benefit from the certainty and stability of regularly scheduled updates using a set methodology.

### *B. Number of Affected Small Entities*

#### 1. Definition of Small Entity

The RFA defines a “small entity” as (1) a small not-for-profit organization, (2) a small governmental jurisdiction, or (3) a small business. The Department used the entity size standards defined by SBA and in effect as of 2019, to classify entities as small or large.<sup>433</sup> The most recent size standards were released in 2022 and use the 2022 NAICS. However, because the data used by the Department to estimate the number of small entities uses the 2017 NAICS, the Department used the 2019 standards instead of the 2022 standards.<sup>434</sup>

SBA establishes standards for 6-digit NAICS industry codes, and standard size cutoffs are typically based on either the average number of employees, or average annual receipts. However, some exceptions exist, the most notable being that depository institutions (including credit unions, commercial banks, and non-commercial banks) are classified by total assets and small governmental jurisdictions are defined as areas with populations of less than 50,000.<sup>435</sup>

#### 2. Number of Small Entities and Employees

The primary data source used to estimate the number of small entities

and employment in these entities is the Statistics of U.S. Businesses (SUSB). Alternative sources were used for industries with asset thresholds (credit unions,<sup>436</sup> commercial banks and savings institutions,<sup>437</sup> agriculture<sup>438</sup>), and public administration.<sup>439</sup> The Department used 2017 data, when possible, to align with the use of 2017 SUSB data. Private households are excluded from the analysis due to lack of data.

For each industry, the SUSB 2017 tabulates employment, establishment, and firm counts by both enterprise employment size (e.g., 0–4 employees, 5–9 employees) and receipt size (e.g., less than \$100,000, \$100,000–\$499,999).<sup>440</sup> Although 2020 SUSB data are available, these data do not disaggregate entities by revenue sizes. The Department combined these data with the SBA size standards to estimate the proportion of firms and establishments in each industry that are considered small, and the proportion of workers employed by a small entity. The Department classified all firms and establishments and their employees in categories below the SBA cutoff as small.<sup>441</sup> If a cutoff fell in the middle of a category, the Department assumed a uniform distribution of employees across that bracket to determine what proportion of establishments should be classified as small.<sup>442</sup> The estimated share of establishments that were small in 2017 was applied to the more recent 2020 SUSB data on the number of small establishments to determine the number of small entities.<sup>443</sup>

The Department also estimated the number of small establishments and their employees by employer type (nonprofit, for-profit, government). This calculation is similar to the calculation

of the number of establishments by industry but with different data. Instead of using data by industry, the Department used SUSB data by Legal Form of Organization for nonprofit and for-profit establishments. The estimated share of establishments that were calculated as small with the 2017 data was then applied to the 2020 SUSB counts. For governments, the Department used the number of governments reported in the 2017 Census of Governments.<sup>444</sup>

Table 31 presents the estimated number of establishments/governments and small establishments/governments in the U.S. (hereafter, referred to as “entities”).<sup>445</sup> The numbers in the following tables are for Year 1; projected impacts are considered later. The Department found that of the 8.1 million entities, 80 percent (6.5 million) are small by SBA standards. These small entities employ 53.6 million workers, about 37 percent of workers (excluding self-employed, unpaid workers, and members of the armed forces). They also account for roughly 35 percent of total payroll (\$3.5 trillion of \$10.1 trillion).<sup>446</sup>

Although the Department used 6-digit NAICS to determine the number of small entities and the associated number of employees, the following tables aggregate findings to 27 industry categories. This was the most detailed level available while maintaining adequate sample sizes.<sup>447</sup> The Department started with the 51-industry breakdown and aggregated where necessary to obtain adequate sample sizes.

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. The Department based the analysis on the number of establishments rather than firms for a more conservative estimate (potential overestimate) of the number of small businesses.

<sup>446</sup> Since information is not available on employer size in the CPS MOR, 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.

<sup>447</sup> The Department required at least 15 affected workers (i.e., observations) in small entities in Year 1.

<sup>433</sup> See [https://www.sba.gov/sites/default/files/2019-08/SBA%20Table%20of%20Size%20Standards\\_Effective%20Aug%2019%2C%202019\\_Rev.pdf](https://www.sba.gov/sites/default/files/2019-08/SBA%20Table%20of%20Size%20Standards_Effective%20Aug%2019%2C%202019_Rev.pdf).

<sup>434</sup> The SBA size standard changes in 2022 primarily adjusted the standards to the 2022 NAICS, these changes were not substantive. <https://www.govinfo.gov/content/pkg/FR-2022-09-29/pdf/2022-20513.pdf>.

<sup>435</sup> See <http://www.sba.gov/advocacy/regulatory-flexibility-act> for details.

<sup>436</sup> National Credit Union Association. (2018). 2018 Year End Statistics for Federally Insured Credit Unions. Available at: <https://www.cuna.org/advocacy/credit-union---economic-data/data---statistics/credit-union-profile-reports.html>.

<sup>437</sup> Federal Depository Insurance Corporation. (2018). Quarterly Financial Reports-Statistics On Depository Institutions (SDI). Available at: <https://www.fdic.gov/foia/ris/id-sdi/index.html>. Data are from 12/31/17.

<sup>438</sup> United States Department of Agriculture. (2019). 2017 Census of Agriculture: United States Summary and State Data: Volume 1, Geographic Area Series, Part 51. Available at: [https://www.nass.usda.gov/Publications/AgCensus/2017/Full\\_Report/Volume\\_1\\_Chapter\\_1\\_US/usv1.pdf](https://www.nass.usda.gov/Publications/AgCensus/2017/Full_Report/Volume_1_Chapter_1_US/usv1.pdf).

<sup>439</sup> Census of Governments. 2017. Available at: <https://www.census.gov/data/tables/2017/econ/gus/2017-governments.html>.

<sup>440</sup> The SUSB defines employment as of March 12th.

<sup>441</sup> The Department’s estimates of the numbers of affected small entities and affected workers who are employees of small entities includes entities not covered by the FLSA and thus are likely overestimates. The Department had no credible way to estimate which enterprises with annual revenues below \$500,000 also did not engage in interstate commerce and hence are not subject to the FLSA.

<sup>442</sup> The Department assumed that the small entity share of credit card issuing and other depository credit intermediation institutions (which were not separately represented in FDIC asset data), is similar to that of commercial banking and savings institutions.

<sup>443</sup> Statistics of U.S. Businesses 2020, <https://www.census.gov/programs-surveys/susb.html>.

<sup>444</sup> Census of Governments 2017. Available at <https://www.census.gov/programs-surveys/cog.html>.

<sup>445</sup> SUSB reports data by “enterprise” size designations (a business organization consisting of

TABLE 31—NUMBER OF ENTITIES AND EMPLOYEES BY SBA SIZE STANDARDS, BY INDUSTRY AND EMPLOYER TYPE

Industry/employer type	Entities (1,000s)		Workers (1,000s) <sup>a</sup>		Annual payroll (billions)	
	Total	Small	Total	Small business employed	Total	Small
Total .....	8,090.3	6,459.6	143,444.4	53,585.6	\$10,054.5	\$3,535.6
<b>Industry <sup>b</sup></b>						
Agriculture, forestry, fishing, and hunting .....	22.7	18.9	1,364.4	724.4	62.7	34.6
Mining .....	23.9	19.2	620.8	285.4	66.0	30.6
Construction .....	753.3	726.7	8,957.5	5,415.9	608.9	369.2
Manufacturing—durable goods .....	175.2	160.4	9,694.4	4,506.7	785.7	350.4
Manufacturing—non-durable goods .....	108.3	96.4	5,522.6	2,649.3	416.7	187.9
Wholesale trade .....	391.1	301.5	3,231.4	1,354.8	249.6	101.8
Retail trade .....	1,036.8	661.3	15,430.8	4,804.9	769.4	258.8
Transportation and warehousing .....	257.8	203.2	7,152.0	1,746.5	439.5	106.7
Utilities .....	19.5	7.8	1,455.4	310.6	137.3	28.3
Information .....	160.9	93.2	2,570.4	691.7	254.6	67.5
Finance .....	295.5	132.0	4,865.2	902.9	514.9	97.1
Insurance .....	181.3	139.7	2,765.4	585.4	\$245.3	\$51.6
Real estate and rental and leasing .....	437.7	339.0	2,308.4	1,223.1	173.0	92.7
Professional and technical services .....	943.2	841.5	11,575.6	5,104.8	1,291.5	555.8
Management, administrative and waste management services .....	483.5	397.8	5,377.8	2,338.5	284.0	111.6
Educational services .....	110.1	97.6	14,093.6	3,546.7	955.6	223.2
Hospitals .....	7.1	1.4	7,820.6	282.1	632.3	21.2
Health care services, except hospitals .....	736.1	567.4	10,187.6	4,466.2	631.5	271.6
Social assistance .....	185.0	149.8	2,938.8	1,590.5	138.0	71.4
Arts, entertainment, and recreation .....	151.9	138.4	2,381.3	1,185.8	120.8	59.7
Accommodation .....	69.2	58.1	1,048.8	408.3	49.3	19.2
Food services and drinking places .....	664.7	516.6	8,222.4	4,697.9	263.8	151.3
Repair and maintenance .....	216.1	198.6	1,655.6	1,171.9	90.0	63.3
Personal and laundry services .....	248.6	221.5	1,520.5	1,184.7	62.4	47.7
Membership associations and organizations .....	306.6	294.4	2,019.0	1,399.8	138.0	93.6
Public administration <sup>c</sup> .....	90.1	65.7	8,032.3	1,006.6	654.4	68.5
<b>Employer Type</b>						
Nonprofit, private .....	596.3	504.5	10,318.0	3,876.8	741.4	249.6
For profit, private .....	7,403.9	5,874.3	110,919.2	46,388.3	7,688.9	3,072.6
Government (state and local) .....	90.1	65.7	18,041.2	3,320.6	1,241.3	213.3

**Note:** Establishment data are from SUSB 2020; worker and payroll data from pooled CPS MORG data for 2020–2022 adjusted to reflect 2022.

<sup>a</sup> Excludes the self-employed, unpaid workers, and workers in private households.

<sup>b</sup> Summation across industries may not add to the totals reported due to suppressed values and some entities not reporting an industry.

<sup>c</sup> Entity number represents the total number of governments, including state and local. Data from Census of Governments, 2017.

Estimates are not limited to entities subject to the FLSA because the Department cannot estimate which enterprises do not meet the enterprise coverage requirements because of data limitations. Although not excluding such entities and associated workers only affects a small percentage of workers generally, it may have a larger effect (and result in a larger overestimate) for non-profits, because revenue from charitable activities is not included when determining enterprise coverage.

### 3. Number of Affected Small Entities and Employees

The calculation of the number of affected EAP workers was explained in detail in section VII.B. Here, the Department focuses on how these workers were allocated to either small or large entities. To estimate the probability that an exempt EAP worker in the CPS data is employed by a small entity, the Department assumed this probability is equal to the proportion of

all workers employed by small entities in the corresponding industry. That is, if 50 percent of workers in an industry are employed in small entities, then on average small entities are expected to employ one out of every two exempt EAP workers in this industry.<sup>448</sup> The Department applied these probabilities to the population of exempt EAP workers to find the number of workers (total exempt EAP workers and total affected by the rule) that small entities employ. No data are available to determine whether small businesses (or small businesses in specific industries) are more or less likely than non-small businesses to employ exempt EAP workers or affected EAP workers. Therefore, the best assumption available

<sup>448</sup> 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.

is to assign the same rates to all small and non-small businesses.<sup>449 450</sup>

The Department estimated that small entities employ 1.3 million of the 3.6 million affected workers (36.8 percent) (Table 32). This composes 2.5 percent of the 53.6 million workers that small entities employ. The sectors with the highest total number of affected workers employed by small entities are professional and technical services (238,000); health care services, except hospitals (120,000); and retail trade (103,000). The sectors with the largest percent of workers employed by small entities who are affected include:

<sup>449</sup> A strand of literature indicates that small businesses tend to pay lower wages than larger businesses. 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.

<sup>450</sup> Workers are designated as employed in a small business based on their industry of employment. The share of workers considered small in nonprofit, for profit, and government entities is therefore the weighted average of the shares for the industries that compose these categories.

insurance (6.8 percent); finance (5.4 percent); and information (4.9 percent).

TABLE 32—NUMBER OF AFFECTED WORKERS EMPLOYED BY SMALL ENTITIES, BY INDUSTRY AND EMPLOYER TYPE

Industry	Workers (1,000s)		Affected workers (1,000s) <sup>a</sup>	
	Total	Small business employed	Total	Small business employed
Total .....	143,444.4	53,585.6	3,648.3	1,341.1
<b>Industry</b>				
Agriculture, forestry, fishing, and hunting .....	1,364.4	724.4	12.3	6.8
Mining .....	620.8	285.4	12.5	5.1
Construction .....	8,957.5	5,415.9	154.4	93.4
Manufacturing—durable goods .....	9,694.4	4,506.7	203.8	94.0
Manufacturing—non-durable goods .....	5,522.6	2,649.3	113.3	53.6
Wholesale trade .....	3,231.4	1,354.8	103.9	50.4
Retail trade .....	15,430.8	4,804.9	308.7	103.1
Transportation and warehousing .....	7,152.0	1,746.5	87.8	29.1
Utilities .....	1,455.4	310.6	31.1	6.0
Information .....	2,570.4	691.7	118.6	33.9
Finance .....	4,865.2	902.9	241.6	49.1
Insurance .....	2,765.4	585.4	170.7	39.9
Real estate and rental and leasing .....	2,308.4	1,223.1	68.3	34.7
Professional and technical services .....	11,575.6	5,104.8	572.2	238.2
Management, administrative and waste management services .....	5,377.8	2,338.5	115.2	42.1
Educational services .....	14,093.6	3,546.7	201.8	44.2
Hospitals .....	7,820.6	282.1	212.6	5.6
Health care services, except hospitals .....	10,187.6	4,466.2	290.8	120.4
Social assistance .....	2,938.8	1,590.5	123.5	72.3
Arts, entertainment, and recreation .....	2,381.3	1,185.8	92.9	48.6
Accommodation .....	1,048.8	408.3	15.5	6.1
Food services and drinking places .....	8,222.4	4,697.9	75.1	42.4
Repair and maintenance .....	1,655.6	1,171.9	19.8	14.2
Personal and laundry services .....	1,520.5	1,184.7	19.6	12.5
Membership associations and organizations .....	2,019.0	1,399.8	99.4	66.0
Public administration .....	8,032.3	1,006.6	182.4	29.5
<b>Employer Type</b>				
Nonprofit, private .....	10,318.0	3,876.8	381.5	162.1
For profit, private .....	110,919.2	46,388.3	2,868.4	1,119.4
Government (state and local) .....	18,041.2	3,320.6	398.3	59.7

**Note:** Worker data are from pooled CPS MORG data for 2020–2022 adjusted to reflect 2022.

<sup>a</sup> Estimation of affected workers employed by small entities was done at the most detailed industry level available. Therefore, at the more aggregated industry level shown in this table, the ratio of small business employed to total employed does not equal the ratio of affected small business employed to total affected for each industry, nor does it equal the ratio for the national total because relative industry size, employment, and small business employment differs from industry to industry.

Because no information is available on how affected workers would be distributed among small entities, the Department estimated a range of effects. At one end of this range, the Department assumed that each small entity employs no more than one affected worker, meaning that at most 1.3 million of the 6.5 million small entities will employ an affected worker. Thus, these assumptions provide an upper-end estimate of the number of affected small entities. (However, it provides a lower-end estimate of the effect per small entity because costs are spread over a larger number of entities; the impacts experienced by an entity would increase as the share of its workers that are affected increases.) For the purpose of

estimating a lower-range number of affected small entities, the Department used the average size of a small entity as the typical size of an affected small entity, and assumed all workers are affected. This can be considered an approximation of all employees at an entity affected.<sup>451</sup> The average number

<sup>451</sup> This is not the true lower bound estimate of the number of affected entities. Strictly speaking, a true lower bound estimate of the number of affected small entities would be calculated by assuming all employees in the largest small entity are affected. For example, if the SBA standard is that entities with 500 employees are “small,” and 1,350 affected workers are employed by small entities in that industry, then the smallest number of entities that could be affected in that industry (the true lower bound) would be three. However, because such an outcome appears implausible, the Department

of employees in a small entity is the number of workers that small entities employ divided by the total number of small establishments in that industry. The number of affected employees at small businesses is then divided by this average number of employees to calculate 179,700 affected small entities.

Table 33 summarizes the estimated number of affected workers that small entities employ and the expected range for the number of affected small entities by industry. The Department estimated that the rule would affect 1.3 million workers who are employed by somewhere between 179,700 and 1.3

determined a more reasonable lower estimate would be based on average establishment size.

million small entities; this comprises from 2.8 percent to 20.8 percent of all small entities. It also means that from 5.1 million to 6.3 million small entities would incur no more than minimal regulatory familiarization costs (*i.e.*, 6.5 million minus 1.3 million equals 5.1 million; 6.5 million minus 179,700

equals 6.3 million, using rounded values). The table also presents the average number of affected employees per establishment using the method in which all employees at the establishment would be affected. For the other method, by definition, there would always be one affected employee

per establishment. Also displayed is the average payroll per small establishment by industry (based on both affected and non-affected small entities), calculated by dividing total payroll of small businesses by the number of small businesses (Table 31) (applicable to both methods).

TABLE 33—NUMBER OF SMALL AFFECTED ENTITIES AND EMPLOYEES BY INDUSTRY AND EMPLOYER TYPE

Industry	Affected workers in small entities (1,000s)	Number of small affected entities (1,000s) <sup>a</sup>		Per entity	
		One affected employee per entity <sup>b</sup>	All employees at entity affected <sup>c</sup>	Affected employees <sup>a</sup>	Average annual payroll (\$1,000s)
Total .....	1,341.1	1,341.1	179.7	7.5	\$547.3
<b>Industry</b>					
Agriculture, forestry, fishing, and hunting .....	6.8	6.8	0.2	38.4	1,833.6
Mining .....	5.1	5.1	0.3	14.9	1,594.3
Construction .....	93.4	93.4	12.5	7.5	508.1
Manufacturing—durable goods .....	94.0	94.0	3.3	28.1	2,184.4
Manufacturing—non-durable goods .....	53.6	53.6	2.0	27.5	1,949.1
Wholesale trade .....	50.4	50.4	11.2	4.5	337.7
Retail trade .....	103.1	103.1	14.2	7.3	391.3
Transportation and warehousing .....	29.1	29.1	3.4	8.6	525.0
Utilities .....	6.0	6.0	0.2	39.9	3,634.2
Information .....	33.9	33.9	4.6	7.4	723.9
Finance .....	49.1	49.1	7.2	6.8	735.5
Insurance .....	39.9	39.9	9.5	4.2	369.4
Real estate and rental and leasing .....	34.7	34.7	9.6	3.6	273.6
Professional and technical services .....	238.2	238.2	39.3	6.1	660.5
Management, administrative and waste management services .....	42.1	42.1	7.2	5.9	280.5
Educational services .....	44.2	44.2	1.2	36.3	2,286.8
Hospitals .....	5.6	<sup>d</sup> 4.2	0.0	201.6	15,137.3
Health care services, except hospitals .....	120.4	120.4	15.3	7.9	478.7
Social assistance .....	72.3	72.3	6.8	10.6	476.7
Arts, entertainment, and recreation .....	48.6	48.6	5.7	8.6	431.4
Accommodation .....	6.1	6.1	0.9	7.0	330.8
Food services and drinking places .....	42.4	42.4	4.7	9.1	292.9
Repair and maintenance .....	14.2	14.2	2.4	5.9	318.8
Personal and laundry services .....	12.5	12.5	2.3	5.3	215.3
Membership associations and organizations .....	66.0	66.0	13.9	4.8	318.1
Public administration <sup>e</sup> .....	29.5	29.5	1.9	15.3	1,042.9
<b>Employer Type</b>					
Nonprofit, private .....	162.1	162.1	21.1	7.7	494.8
For profit, private .....	1,119.4	1,119.4	141.8	7.9	523.1
Government (state and local) .....	59.7	59.7	1.2	50.5	3,246.6

**Note:** Establishment data are from SUSB 2020; worker and payroll data from pooled CPS MORG data for 2020–2022 adjusted to reflect 2022.

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

<sup>b</sup> This method may overestimate the number of affected entities and therefore the ratio of affected workers to affected entities may be greater than 1-to-1. However, the Department addresses this issue by also calculating effects based on the assumption that 100 percent of workers at an entity are affected.

<sup>c</sup> For example, on average, a small entity in the construction industry employs 7.5 workers (5.4 million employees divided by 726,700 small entities). This method assumes if an entity is affected then all 7.5 workers are affected. Therefore, in the construction industry this method estimates there are 12,500 small affected entities (93,400 affected small entity workers divided by 7.5).

<sup>d</sup> Number of entities is smaller than number of affected employees; thus, total number of entities is reported.

<sup>e</sup> Entity number represents the total number of state and local governments.

#### 4. Impacts to Affected Small Entities

For small entities, the Department estimated various types of effects, including regulatory familiarization

costs, adjustment costs, managerial costs, and payroll increases borne by employers. The Department estimated a range for the number of affected small entities and the impacts they incur.

While the upper and lower bounds are likely over- and under-estimates, respectively, of effects per small entity, the Department believes that this range of costs and payroll increases provides

the most accurate characterization of the effects of the rule on small employers.<sup>452</sup> Furthermore, the smaller estimate of the number of affected entities (*i.e.*, where all employees at each affected employer are assumed to be affected) will result in the largest

costs and payroll increases per entity as a percent of establishment payroll and revenue, and the Department expects that many, if not most, entities will incur smaller costs, payroll increases, and effects relative to entity size.

Parameters that are used in the small business cost analysis for Year 1 are provided in Table 34, along with summary data of the impacts. See section C.3 of the Regulatory Impact Analysis for a more fulsome discussion on these costs.

**TABLE 34—OVERVIEW OF PARAMETERS USED FOR COSTS TO SMALL BUSINESSES AND THE IMPACTS ON SMALL BUSINESSES**

Small business costs	Cost
<b>Direct and Payroll Costs</b>	
Average total cost per affected entity <sup>a</sup> .....	\$4,323.
Range of total costs per affected entity <sup>a</sup> .....	\$1,833–\$146,781.
Average percent of revenue per affected entity .....	0.16%.
Average percent of payroll per affected entity .....	0.79%.
<b>Direct Costs</b>	
Regulatory familiarization:	
Time (first year) .....	1 hour per entity.
Time (update years) .....	10 minutes per entity.
Hourly wage .....	\$52.80.
Adjustment:	
Time (first year affected) .....	75 minutes per newly affected worker.
Hourly wage .....	\$52.80.
Managerial:	
Time (weekly) .....	10 minutes per affected worker whose hours change.
Hourly wage .....	\$83.63.
<b>Payroll Increases</b>	
Average payroll increase per affected entity <sup>a</sup> .....	\$2,638.
Range of payroll increases per affected entity <sup>a</sup> .....	\$769–\$103,871.

<sup>a</sup> 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.

The Department expects total direct employer costs would range from \$294.6 million to \$356.0 million for affected small entities (*i.e.*, those with affected employees) in the first year (an average cost of between \$265 to \$1,640 per entity) (Table 35). Small entities that do not employ affected workers would incur \$270.2 million to \$331.6 million

in regulatory familiarization costs (an average cost of \$52.80 per entity). The three industries with the highest costs (professional and technical services; health care services, except hospitals; and retail trade) account for about 35 percent of the costs. Hospitals are expected to incur the largest cost per establishment (\$42,900 using the

method where all employees are affected), although the costs are not expected to exceed 0.3 percent of payroll. The food services and drinking places industry is expected to experience the largest effect as a share of payroll (estimated direct costs compose 0.68 percent of average entity payroll).

**TABLE 35—YEAR 1 SMALL ESTABLISHMENT DIRECT COSTS, TOTAL AND PER ESTABLISHMENT, BY INDUSTRY AND EMPLOYER TYPE**

Industry	Direct cost to small entities in year 1 <sup>a</sup>					
	One affected employee			All employees affected		
	Total (millions) <sup>a</sup>	Cost per affected entity	Percent of annual payroll	Total (millions) <sup>b</sup>	Cost per affected entity	Percent of annual payroll
Total .....	\$356.0	\$265	0.05	\$294.6	\$1,640	0.30
<b>Industry</b>						
Agriculture, forestry, fishing, and hunting .....	1.8	265	0.01	1.5	8,221	0.45
Mining .....	1.4	265	0.02	1.1	3,219	0.20
Construction .....	24.8	265	0.05	20.5	1,637	0.32
Manufacturing—durable goods .....	25.0	265	0.01	20.2	6,025	0.28
Manufacturing—non-durable goods .....	14.2	265	0.01	11.5	5,895	0.30
Wholesale trade .....	13.4	265	0.08	11.3	1,008	0.30
Retail trade .....	27.4	265	0.07	22.7	1,598	0.41
Transportation and warehousing .....	7.7	265	0.05	6.4	1,880	0.36

<sup>452</sup> As noted previously, these are not the true lower and upper bounds. The values presented are

the highest and lowest estimates the Department believes are plausible.

TABLE 35—YEAR 1 SMALL ESTABLISHMENT DIRECT COSTS, TOTAL AND PER ESTABLISHMENT, BY INDUSTRY AND EMPLOYER TYPE—Continued

Industry	Direct cost to small entities in year 1 <sup>a</sup>					
	One affected employee			All employees affected		
	Total (millions) <sup>a</sup>	Cost per affected entity	Percent of annual payroll	Total (millions) <sup>b</sup>	Cost per affected entity	Percent of annual payroll
Utilities .....	1.6	265	0.01	1.3	8,527	0.23
Information .....	9.0	265	0.04	7.4	1,630	0.23
Finance .....	13.0	265	0.04	10.8	1,507	0.20
Insurance .....	10.6	265	0.07	9.0	943	0.26
Real estate and rental and leasing .....	9.2	265	0.10	7.9	820	0.30
Professional and technical services .....	63.2	265	0.04	52.7	1,343	0.20
Management, administrative and waste management services .....	11.2	265	0.10	9.3	1,303	0.46
Educational services .....	11.7	265	0.01	9.5	7,777	0.34
Hospitals .....	1.5	265	0.00	1.2	42,910	0.28
Health care services, except hospitals .....	32.0	265	0.06	26.4	1,726	0.36
Social assistance .....	19.2	265	0.06	15.7	2,311	0.48
Arts, entertainment, and recreation .....	12.9	265	0.06	10.6	1,874	0.43
Accommodation .....	1.6	265	0.08	1.3	1,547	0.47
Food services and drinking places .....	11.2	265	0.09	9.3	1,986	0.68
Repair and maintenance .....	3.8	265	0.08	3.1	1,307	0.41
Personal and laundry services .....	3.3	265	0.13	2.8	1,190	0.55
Membership associations and organizations .....	17.5	265	0.08	14.8	1,064	0.33
Public administration .....	7.8	265	0.03	6.4	3,311	0.32
<b>Employer Type</b>						
Nonprofit, private .....	42.6	263	0.05	35.2	1,669	0.34
For profit, private .....	344.8	308	0.06	293.1	2,068	0.40
Government (state and local) .....	16.2	272	0.01	13.1	11,119	0.34

**Note:** Pooled CPS data for 2020–2022 adjusted to reflect 2022.

<sup>a</sup> Direct costs include regulatory familiarization, adjustment, and managerial costs.

<sup>b</sup> The range of costs per entity depends on the number of affected entities. The minimum assumes that each affected entity has one affected worker (therefore, the number of affected entities 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 entities that are affected.

It is possible that the costs of the proposed rule may be disproportionately large for small entities, especially because small entities often have limited human resources personnel on staff. However, the Department expects that small entities would rely on compliance assistance materials provided by the Department or industry associations to become familiar with the final rule once issued. Additionally, the Department notes that the proposed rule is quite limited in scope because the changes all relate to the salary component of the part 541 regulations. Finally, the Department believes that most entities

have at least some nonexempt employees and, therefore, already have policies and systems in place for monitoring and recording their hours. The Department believes that applying those same policies and systems to the workers whose exemption status changes would not be an unreasonable burden on small businesses.

Average weekly earnings for affected EAP workers in small entities are expected to increase by about \$6.91 per week per affected worker, using the incomplete fixed-job model <sup>453</sup> described in section VII.C.4.iii. <sup>454</sup> This would lead to \$482.2 million in additional annual wage payments to

employees in small entities (less than 0.5 percent of aggregate affected establishment payroll; Table 36). The largest payroll increases per establishment are expected in hospitals (up to \$103,900 per entity); utilities (up to \$20,900 per entity); and non-durable goods manufacturing (up to \$11,700 per entity). However, average payroll increases per entity would exceed one percent of average annual payroll in only three sectors: food services and drinking places (2.5 percent); management, administrative and waste management services (1.2 percent); and transportation and warehousing (1.1 percent).

TABLE 36—YEAR 1 SMALL ESTABLISHMENT PAYROLL INCREASES, TOTAL AND PER ESTABLISHMENT, BY INDUSTRY AND EMPLOYER TYPE

Industry	Increased payroll for small entities in year 1 <sup>a</sup>				
	Total (millions)	One affected employee		All employees affected	
		Per entity	Percent of annual payroll	Per entity	Percent of annual payroll
Total .....	\$482.2	\$360	0.07%	\$2,683	0.49%

<sup>453</sup> The incomplete fixed-job model reflects the Department's determination that an appropriate estimate of the impact on the implicit hourly rate of pay for regular overtime workers should be determined using the average of Barkume's and Trejo's two estimates of the incomplete fixed-job

model adjustments: a wage change that is 40 percent of the adjustment toward the amount predicted by the fixed-job model, assuming an initial zero overtime pay premium, and a wage change that is 80 percent of the adjustment

assuming an initial 28 percent overtime pay premium.

<sup>454</sup> This is an average increase for all affected workers (both standard test and HCE), and reconciles to the weighted average of individual salary changes discussed in the Transfers section.



TABLE 36—YEAR 1 SMALL ESTABLISHMENT PAYROLL INCREASES, TOTAL AND PER ESTABLISHMENT, BY INDUSTRY AND EMPLOYER TYPE—Continued

Industry	Increased payroll for small entities in year 1 <sup>a</sup>				
	Total (millions)	One affected employee		All employees affected	
		Per entity	Percent of annual payroll	Per entity	Percent of annual payroll
Industry					
Agriculture, forestry, fishing, and hunting .....	0.9	126	0.01	4,837	0.26
Mining .....	1.7	330	0.02	4,918	0.31
Construction .....	30.0	321	0.07	2,391	0.47
Manufacturing—durable goods .....	31.5	335	0.02	9,423	0.43
Manufacturing—non-durable goods .....	22.8	426	0.02	11,707	0.60
Wholesale trade .....	24.7	491	0.15	2,206	0.65
Retail trade .....	51.3	497	0.13	3,613	0.92
Transportation and warehousing .....	20.0	687	0.14	5,907	1.13
Utilities .....	3.1	524	0.01	20,888	0.57
Information .....	12.0	353	0.05	2,622	0.36
Finance .....	15.9	324	0.04	2,214	0.30
Insurance .....	11.8	297	0.08	1,244	0.34
Real estate and rental and leasing .....	15.8	456	0.17	1,646	0.60
Professional and technical services .....	77.5	326	0.05	1,975	0.30
Management, administrative and waste management services .....	24.4	580	0.21	3,407	1.21
Educational services .....	9.0	204	0.01	7,417	0.32
Hospitals .....	2.9	515	0.00	103,871	0.69
Health care services, except hospitals .....	38.3	318	0.07	2,502	0.52
Social assistance .....	10.5	145	0.03	1,539	0.32
Arts, entertainment, and recreation .....	14.3	295	0.07	2,523	0.58
Accommodation .....	1.7	279	0.09	1,959	0.59
Food services and drinking places .....	34.2	808	0.28	7,345	2.51
Repair and maintenance .....	7.0	490	0.16	2,893	0.91
Personal and laundry services .....	2.8	221	0.11	1,183	0.55
Membership associations and organizations .....	10.7	162	0.05	769	0.24
Public administration .....	7.3	249	0.02	3,810	0.37
Employer Type					
Nonprofit, private .....	49.3	304	0.06	2,336	0.47
For profit, private .....	421.3	376	0.07	2,972	0.57
Government (state and local) .....	11.6	194	0.01	9,816	0.30

**Note:** Pooled CPS data for 2020–2022 adjusted to reflect 2022.

<sup>a</sup>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.

Table 37 presents estimated first year direct costs and payroll increases combined per entity and the costs and payroll increases as a percent of average entity payroll. The Department presents only the results for the upper bound scenario where all workers employed by the entity are affected. Combined costs and payroll increases per establishment range from \$1,800 in membership associations to \$146,800 in hospitals.

Combined costs and payroll increases compose more than two percent of average annual payroll in one sector, food services and drinking places (3.2 percent).

However, comparing costs and payroll increases to payrolls overstates the effects on entities because payroll represents only a fraction of the financial resources available to an establishment. The Department approximated revenue per affected

small establishment by calculating the ratio of small business revenues to payroll by industry from the 2017 SUSB data then multiplying that ratio by average small entity payroll.<sup>455</sup> Using this approximation of annual revenues as a benchmark, only one sector would have costs and payroll increases amounting to close to one percent of revenues, food services and drinking places (1.0 percent).

<sup>455</sup> The Department used this estimate of revenue, instead of small business revenue reported directly from the 2017 SUSB so revenue aligned with payrolls in 2022.

TABLE 37—YEAR 1 SMALL ESTABLISHMENT DIRECT COSTS AND PAYROLL INCREASES, TOTAL AND PER ENTITY, BY INDUSTRY AND EMPLOYER TYPE, USING ALL EMPLOYEES IN ENTITY AFFECTED METHOD

Industry	Costs and payroll increases for small affected entities, all employees affected			
	Total (millions)	Per entity <sup>a</sup>	Percent of annual payroll	Percent of estimated revenues <sup>b</sup>
Total .....	\$776.8	\$4,323	0.79%	0.16%
<b>Industry</b>				
Agriculture, forestry, fishing, and hunting .....	2.3	13,058	0.71	0.14
Mining .....	2.8	8,136	0.51	0.07
Construction .....	50.5	4,028	0.79	0.18
Manufacturing—durable goods .....	51.7	15,448	0.71	0.15
Manufacturing—non-durable goods .....	34.3	17,601	0.90	0.12
Wholesale trade .....	36.1	3,214	0.95	0.07
Retail trade .....	73.9	5,210	1.33	0.13
Transportation and warehousing .....	26.4	7,786	1.48	0.35
Utilities .....	4.4	29,415	0.81	0.06
Information .....	19.4	4,252	0.59	0.17
Finance .....	26.7	3,721	0.51	0.15
Insurance .....	20.8	2,187	0.59	0.13
Real estate and rental and leasing .....	23.7	2,466	0.90	0.20
Professional and technical services .....	130.2	3,317	0.50	0.20
Management, administrative and waste management services .....	33.7	4,710	1.68	0.68
Educational services .....	18.5	15,194	0.66	0.27
Hospitals .....	4.1	146,781	0.97	0.41
Health care services, except hospitals .....	64.7	4,228	0.88	0.37
Social assistance .....	26.2	3,850	0.81	0.38
Arts, entertainment, and recreation .....	24.9	4,397	1.02	0.33
Accommodation .....	3.0	3,506	1.06	0.26
Food services and drinking places .....	43.5	9,332	3.19	1.00
Repair and maintenance .....	10.1	4,200	1.32	0.37
Personal and laundry services .....	5.5	2,373	1.10	0.39
Membership associations and organizations .....	25.4	1,833	0.58	0.14
Public administration .....	13.7	7,122	0.68	0.17
<b>Employer Type</b>				
Nonprofit, private .....	94.40	3,570	1.00	0.30
For profit, private .....	585.30	3,532	1.00	0.20
Government (state and local) .....	12.20	9,264	0.60	0.20

**Note:** Pooled CPS data for 2020–2022 adjusted to reflect 2022.

<sup>a</sup> Total direct costs and transfers for small entities in which all employees are affected. Impacts to small entities in which one employee is affected will be a fraction of the impacts presented in this table.

<sup>b</sup> Revenues estimated by calculating the ratio of estimated small business revenues to payroll from the 2017 SUSB, and multiplying by payroll per small entity. For the public administration sector, the ratio was calculated using revenues and payroll from the 2017 Census of Governments.

#### 5. Projected Effects to Affected Small Entities in Year 2 Through Year 10

To determine how small businesses would be affected in future years, the Department projected costs to small businesses for 9 years after Year 1 of the

rule. Projected employment and earnings were calculated using the same methodology described in section VII.B.3. Affected employees in small firms follow a similar pattern to affected workers in all entities: the number

decreases gradually between automatic update years, and then increases. There are 1.3 million affected workers in small entities in Year 1 and 1.9 million in Year 10. Table 38 reports affected workers in these 2 years only.

TABLE 38—PROJECTED NUMBER OF AFFECTED WORKERS IN SMALL ENTITIES, BY INDUSTRY

Industry	Affected workers in small entities (1,000s)	
	Year 1	Year 10
Total .....	1,341.1	1,872.1
Agriculture, forestry, fishing, and hunting .....	6.8	7.6
Mining .....	5.1	7.1
Construction .....	93.4	127.3
Manufacturing—durable goods .....	94.0	125.3
Manufacturing—non-durable goods .....	53.6	78.5

TABLE 38—PROJECTED NUMBER OF AFFECTED WORKERS IN SMALL ENTITIES, BY INDUSTRY—Continued

Industry	Affected workers in small entities (1,000s)	
	Year 1	Year 10
Wholesale trade .....	50.4	73.3
Retail trade .....	103.1	125.6
Transportation and warehousing .....	29.1	40.2
Utilities .....	6.0	7.2
Information .....	33.9	39.6
Finance .....	49.1	59.2
Insurance .....	39.9	60.2
Real estate and rental and leasing .....	34.7	55.4
Professional and technical services .....	238.2	342.6
Management, administrative and waste management services .....	42.1	56.3
Educational services .....	44.2	62.1
Hospitals .....	5.6	8.8
Health care services, except hospitals .....	120.4	172.0
Social assistance .....	72.3	118.6
Arts, entertainment, and recreation .....	48.6	78.9
Accommodation .....	6.1	10.6
Food services and drinking places .....	42.4	56.4
Repair and maintenance .....	14.2	21.2
Personal and laundry services .....	12.5	15.1
Membership associations and organizations .....	66.0	80.8
Public administration .....	29.5	42.4

**Note:** Worker data are from Pooled CPS data for 2020–2022 adjusted to reflect 2022.

Direct costs and payroll increases for small entities vary by year but generally decrease between automatic updates as the real value of the salary and compensation levels decrease and the

number of affected workers consequently decreases. In automatic updating years, costs would increase due to newly affected workers and some regulatory familiarization costs. Direct

costs and payroll increases for small businesses would be fairly close in Year 10 (an automatic update year) and Year 1, \$0.8 billion in Year 1 and \$1.0 billion in Year 10 (Table 39 and Figure 10).

TABLE 39—PROJECTED DIRECT COSTS AND PAYROLL INCREASES FOR AFFECTED SMALL ENTITIES, BY INDUSTRY, USING ALL EMPLOYEES IN ENTITY AFFECTED METHOD

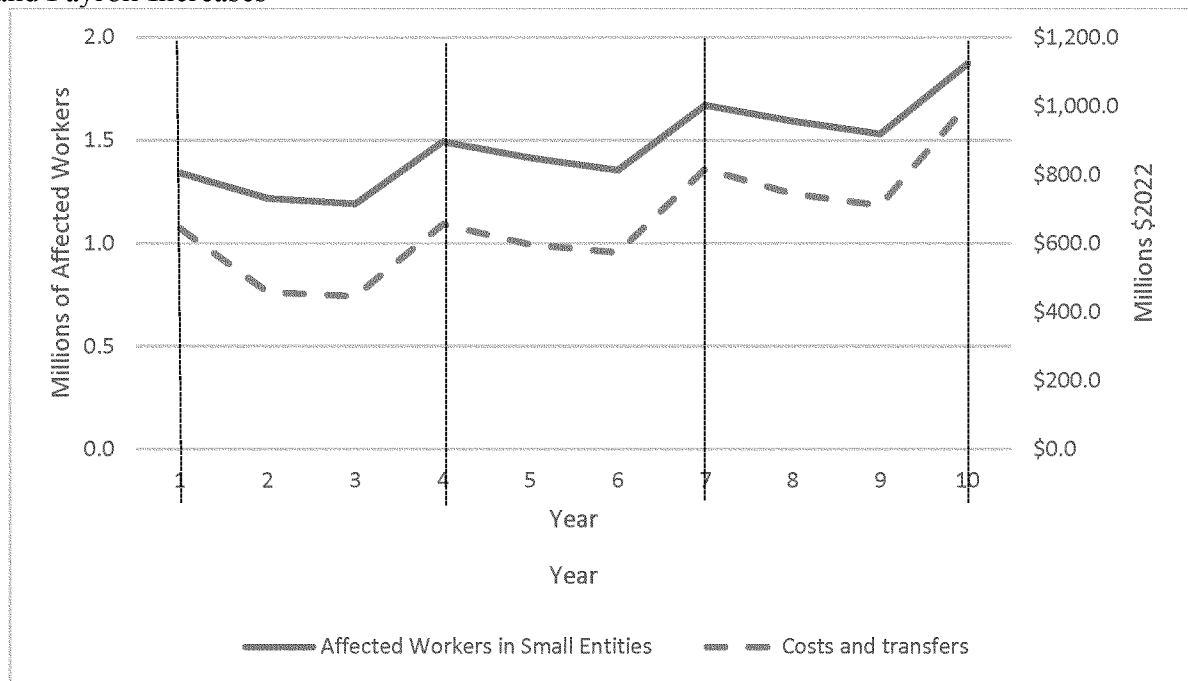
Industry	Costs and payroll increases for small affected entities, all employees affected (millions \$2022)	
	Year 1	Year 10
Total .....	\$776.8	\$1,015.9
Agriculture, forestry, fishing, and hunting .....	2.3	5.6
Mining .....	2.8	3.3
Construction .....	50.5	65.1
Manufacturing—durable goods .....	51.7	64.3
Manufacturing—non-durable goods .....	34.3	43.8
Wholesale trade .....	36.1	62.7
Retail trade .....	73.9	74.6
Transportation and warehousing .....	26.4	70.4
Utilities .....	4.4	3.7
Information .....	19.4	15.9
Finance .....	26.7	33.0
Insurance .....	20.8	25.1
Real estate and rental and leasing .....	23.7	29.7
Professional and technical services .....	130.2	166.8
Management, administrative and waste management services .....	33.7	29.0
Educational services .....	18.5	24.3
Hospitals .....	4.1	15.7
Health care services, except hospitals .....	64.7	70.4
Social assistance .....	26.2	37.3
Arts, entertainment, and recreation .....	24.9	39.7
Accommodation .....	3.0	5.0
Food services and drinking places .....	43.5	51.3
Repair and maintenance .....	10.1	17.4
Personal and laundry services .....	5.5	2.3

TABLE 39—PROJECTED DIRECT COSTS AND PAYROLL INCREASES FOR AFFECTED SMALL ENTITIES, BY INDUSTRY, USING ALL EMPLOYEES IN ENTITY AFFECTED METHOD—Continued

Industry	Costs and payroll increases for small affected entities, all employees affected (millions \$2022)	
	Year 1	Year 10
Membership associations and organizations .....	25.4	28.0
Public administration .....	13.7	31.4

**Note:** Pooled CPS data for 2020–2022 adjusted to reflect 2022.

Figure 10: 10-Year Projected Number of Affected Workers in Small Entities, and Associated Costs and Payroll Increases



### C. Projected Reporting, Recordkeeping, and Other Compliance Requirements of the Proposed Rule

The FLSA sets minimum wage, overtime pay, and recordkeeping requirements for employment subject to its provisions. Unless exempt, covered employees must be paid at least the minimum wage and not less than one and one-half times their regular rates of pay for overtime hours worked.

Pursuant to section 11(c) of the FLSA, the Department's regulations at part 516 require covered employers to maintain certain records about their employees. Bona fide EAP workers are subject to some of these recordkeeping requirements but exempt from others related to pay and worktime.<sup>456</sup> Thus, although this rulemaking would not

introduce any new recordkeeping requirements, employers would need to keep some additional records for affected employees who become newly nonexempt if they do not presently record such information. As indicated in this analysis, this proposed rule expands minimum wage and overtime pay coverage to 3.6 million affected EAP workers, of which 1.3 million are employed by a small entity. This would result in an increase in employer burden and was estimated in the PRA portion (section VI) of this proposed rule. Note that the burdens reported for the PRA section of this proposed rule include the entire information collection and not merely the additional burden estimated as a result of this proposed rule.

### D. Steps the Agency Has Taken To Minimize the Significant Economic Impact on Small Entities

This section describes the steps the agency has taken to minimize the economic impact on small entities, consistent with the stated objectives of the FLSA. It includes a statement of the factual, policy, and legal reasons for the selected standard and HCE levels adopted in the proposed rule and why alternatives were rejected.

In this proposed rule, the Department sets the standard salary level equal to the 35th percentile of earnings of full-time salaried workers in the lowest-wage Census Region (currently the South). Based on 2022 data, this results in a salary level of \$1,059 per week. By setting a salary level above the long test salary level, the proposal would ensure that fewer lower paid white-collar employees who perform significant amounts of nonexempt work are

<sup>456</sup> See 29 CFR 516.3 (providing that employers need not maintain the records required by 29 CFR 516.2(a)(6) through (10) for their EAP workers).

included in the exemption. At the same time, by setting it below the short test salary level, the proposal would allow employers to continue to use the exemption for many lower paid white-collar employees who were made exempt under the 2004 standard duties test. Thus, the Department believes that the proposed salary level would also more reasonably distribute between employees and their employers the impact of the shift from a two-test to a one-test system on employees earning between the long and short test salary levels. As in prior rulemakings, the Department has not proposed to establish multiple salary levels based on region, industry, employer size, or any other factor, which stakeholders have generally agreed would significantly complicate the regulations.<sup>457</sup> Instead, the Department has again proposed to set the standard salary level using earnings data from the lowest-income Census Region, in part to accommodate small employers and employers in low-income industries.<sup>458</sup>

The Department has proposed to set the HCE total annual compensation level equal to the 85th percentile of earnings of full-time salaried workers nationally (\$143,988 annually based on 2022 data). The Department believes that this level avoids costs associated with evaluating, under the standard duties test, the exemption statuses of large numbers of highly-paid white-collar employees, many of whom would have remained exempt even under that test, while providing a meaningful and appropriate complement to the more lenient HCE duties test. While the proposed threshold is higher than the HCE level adopted in the 2019 rule (which was set equal to the 80th percentile of earnings for salaried workers nationwide), the proposed HCE threshold in this rule would be lower than the HCE percentile adopted in the 2004 and 2016 rules, which covered 93.7 and 90 percent of salaried workers nationwide, respectively. The Department further believes that nearly all of the highly-paid white-collar workers earning above this threshold “would satisfy any duties test.”<sup>459</sup>

#### 1. Differing Compliance and Reporting Requirements for Small Entities

This proposed rule provides no differing compliance requirements and reporting requirements for small entities. The Department has strived to minimize respondent recordkeeping burden by requiring no specific form or

order of records under the FLSA and its corresponding regulations. Moreover, employers would normally maintain the records under usual or customary business practices.

#### 2. Least Burdensome Option or Explanation Required

The Department believes it has chosen the most effective option that updates and clarifies the rule and results in the least burden. Among the options considered by the Department, the least restrictive option was using the 2004 methodology (the 20th percentile of weekly earnings of full-time nonhourly workers in the lowest-wage Census region, currently the South, and in retail nationally) to set the standard salary level, which was also the methodology used in the 2019 rule. As noted above, however, the salary level produced by the 2004 methodology is below the long test salary level, which the Department considers to be the lower boundary for an appropriate salary level in a one-test system using the current standard duties test. Using the 2004 methodology thus does not address the Department’s concerns discussed above under Objectives of, and Need for, the Proposed Rule.

Pursuant to section 603(c) of the RFA, the following alternatives are to be addressed:

##### i. 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. The Department makes available a variety of resources to employers for understanding their obligations and achieving compliance. Therefore, the Department has not proposed differing compliance or reporting requirements for small businesses.

##### ii. The Clarification, Consolidation, or Simplification of Compliance and Reporting Requirements for Small Entities

This proposed rule imposes no new reporting requirements. The Department makes available a variety of resources to employers for understanding their obligations and achieving compliance.

##### iii. The Use of Performance Rather Than Design Standards

Under this proposed rule, employers may achieve compliance through a

variety of means. Employers may elect to continue to claim the EAP exemption for affected employees by adjusting salary levels, hiring additional workers or spreading overtime hours to other employees, or compensating employees for overtime hours worked. The Department makes available a variety of resources to employers for understanding their obligations and achieving compliance.

#### iv. An Exemption From Coverage of the Rule, or Any Part Thereof, for Such Small Entities

Creating an exemption from coverage of this rulemaking for businesses with as many as 500 employees, those defined as small businesses under SBA’s size standards, is inconsistent with the FLSA, which applies to all employers that satisfy the enterprise coverage threshold or employ individually covered employees, regardless of employer size.<sup>460</sup>

#### *E. Identification, to the Extent Practicable, of All Relevant Federal Rules That May Duplicate, Overlap, or Conflict With the Proposed Rule*

The Department is not aware of any Federal rules that duplicate, overlap, or conflict with this proposed rule.

### IX. Unfunded Mandates Reform Act Analysis

The Unfunded Mandates Reform Act of 1995 (UMRA),<sup>461</sup> requires agencies to prepare a written statement for proposed rulemaking that includes any Federal mandate that may result in increased expenditures by state, local, and tribal governments, in the aggregate, or by the private sector, of \$192 million (\$100 million in 1995 dollars adjusted for inflation to 2022) 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, present 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 proposed rule is issued pursuant to section 13(a)(1) of the Fair Labor Standards Act (FLSA or Act), 29 U.S.C. 213(a)(1). The section exempts from the FLSA’s minimum wage and overtime

<sup>457</sup> See 84 FR 51239; 81 FR 32411; 69 FR 22171.

<sup>458</sup> See 84 FR 51238; 81 FR 32527; 69 FR 22237.

<sup>459</sup> 84 FR 51250 (internal citation omitted).

<sup>460</sup> See 29 U.S.C. 203(s).

<sup>461</sup> 2 U.S.C. 1501 *et seq.*

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] . . .).”<sup>462</sup> The requirements of the exemption are contained in part 541 of the Department’s regulations. Section 3(e) of the FLSA<sup>463</sup> 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<sup>464</sup> also defines public agencies to include the government of a state or political subdivision thereof, or any interstate governmental agency.

#### *B. Costs and Benefits*

For purposes of the UMRA, this proposed rule includes a Federal mandate that is expected to result in increased expenditures by the private sector of more than \$192 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 \$192 million or more in any one year.

Based on the economic impact analysis of this proposed rule, the

Department determined that Year 1 costs for state and local governments would total \$184.1 million, of which \$74.0 million are direct employer costs and \$110.1 million are payroll increases (Table 40). In subsequent years, state and local governments may experience payroll increases of as much as \$192.5 million per year.

The proposed rule would result in Year 1 costs to the private sector of approximately \$2.2 billion, of which \$1.1 billion are direct employer costs and \$1.1 billion are payroll increases. In subsequent years, the Department estimated that the private sector may experience a payroll increase of as much as \$1.8 billion per year.

TABLE 40—SUMMARY OF YEAR 1 IMPACTS BY TYPE OF EMPLOYER

Impact	Total	Private	Government <sup>a</sup>
<b>Affected EAP Workers (1,000s)</b>			
Number .....	3,648	3,250	392
<b>Direct Employer Costs (Millions)</b>			
Regulatory familiarization .....	\$427.2	\$422.4	\$4.8
Adjustment .....	240.8	214.5	25.9
Managerial .....	534.9	490.0	43.3
Total direct costs .....	1,202.8	1,126.8	74.0
<b>Payroll Increases (Millions)</b>			
From employers to workers .....	\$1,234.2	\$1,121.4	\$110.1
<b>Direct Employer Costs &amp; Payroll Increases (Millions)</b>			
From employers .....	\$2,437.0	\$2,248.2	\$184.1

<sup>a</sup> Includes only state, local, and tribal governments.

UMRA requires agencies to estimate the effect of a regulation on the national economy if, at its discretion, such estimates are reasonably feasible and the effect is relevant and material.<sup>465</sup> However, OMB guidance on this requirement notes that such macroeconomic effects tend to be measurable in nationwide econometric models only if the economic effect of the regulation reaches 0.25 percent to 0.5 percent of GDP, or in the range of \$63.7 billion to \$127.3 billion (using 2022 GDP). A regulation with a smaller aggregate effect is not likely to have a measurable effect in macro-economic terms unless it is highly focused on a particular geographic region or

economic sector, which is not the case with this proposed rule.

The Department’s RIA estimates that the total first-year costs (direct employer costs and payroll increases from employers to workers) of the proposed rule would be approximately \$2.2 billion for private employers and \$184.1 million for state and local governments. Given OMB’s guidance, the Department has determined that a full macro-economic analysis is not likely to show any measurable effect on the economy. Therefore, these costs are compared to payroll costs and revenue to demonstrate the feasibility of adapting to these new rules.

Total first-year state and local government costs compose 0.02 percent

of state and local government payrolls.<sup>466</sup> First-year state and local government costs compose 0.004 percent of state and local government revenues (projected 2022 revenues were estimated to be \$4.8 trillion).<sup>467</sup> Effects of this magnitude will not result in significant disruptions to typical state and local governments. The \$184.1 million in state and local government costs constitutes an average of approximately \$2,000 for each of the approximately 90,126 state and local entities. The Department considers these costs to be quite small both in absolute terms and in relation to payroll and revenue.

Total first-year private sector costs compose 0.029 percent of private sector

<sup>462</sup> 29 U.S.C. 213(a)(1).

<sup>463</sup> 29 U.S.C. 203(e).

<sup>464</sup> 29 U.S.C. 203(x).

<sup>465</sup> 2 U.S.C. 1532(a)(4).

<sup>466</sup> 2020 state and local government payrolls were \$1.1 trillion, inflated to 2022 payroll costs of \$1.2 trillion using the GDP deflator. State and Local Government Finances 2020. Available at <https://www.census.gov/data/datasets/2020/econ/local/public-use-datasets.html>.

<sup>467</sup> 2020 state and local revenues were \$4.3 trillion, inflated to 2022 dollars using the GDP deflator. State and Local Government Finances 2020. Available at <https://www.census.gov/data/datasets/2020/econ/local/public-use-datasets.html>.

payrolls nationwide.<sup>468</sup> Total private sector first-year costs compose 0.005 percent of national private sector revenues (revenues in 2022 are projected to be \$43.7 trillion).<sup>469</sup> The Department concludes that effects of this magnitude are affordable and will not result in significant disruptions to typical firms in any of the major industry categories.

### *C. Summary of State, Local, and Tribal Government Input*

The Department held a series of stakeholder listening sessions between March 8, 2022 and June 3, 2022 to gather input on its part 541 regulations. Stakeholders invited to participate in these listening sessions included representatives from labor unions; worker advocate groups; industry associations; small business associations; state and local governments; tribal governments; non-profits; and representatives from specific industries such as K–12 education, higher education, healthcare, retail, restaurant, manufacturing, and wholesale. Stakeholders were invited to share their input on issues including the appropriate EAP salary level, the costs and benefits of increasing the salary level to employers and employees, the methodology for updating the salary level and frequency of updates, and whether changes to the duties test are warranted. A listening session was held specifically for state and local governments on April 1, 2022, and a session for tribal governments was held on May 12, 2022. The input received at these listening sessions aided the Department in drafting its proposed rule.

### *D. Least Burdensome Option or Explanation Required*

This proposed rule has described the Department's consideration of various options throughout the preamble (*see* section IV.A.5) and economic impact analysis (*see* section VII.C.8). The Department believes that it has chosen the least burdensome but still cost-effective methodology to update the salary level consistent with the Department's statutory obligation to define and delimit the scope of the EAP exemption. Although some alternative options considered would set the

standard salary level at a rate lower than the proposed level, that outcome would not necessarily be the most cost-effective or least-burdensome. A salary level equal to or below the long test level would result in the exemption of lower-salaried employees who traditionally were entitled to overtime protection under the long test either because of their low salary or because they perform large amounts of nonexempt work, effectively placing the impact of the move from a two-test system to a one-test system on employees.

Selecting a standard salary level in a one-test system inevitably affects the risk and cost of providing overtime protection to employees paid between the long and short test salary levels. Too low of a salary level shifts the impact of the move to a one-test system to employees by exempting lower-salaried employees who perform large amounts of nonexempt work. However, too high a salary level shifts the impact of the move to a one-test system to employers by denying them the use of the exemption for lower-salaried employees who traditionally were exempt under the long duties test, thereby increasing their labor costs. The Department determined that setting the standard salary level equivalent to the earnings of the 35th percentile of full-time salaried workers in the lowest-wage Census region and automatically updating it every three years to reflect current earnings appropriately accounts for the shift from a two-test to a one-test system for determining exemption status, protecting lower-paid white-collar employees who traditionally have been entitled to overtime protection, while allowing employers to use the exemption for EAP employees earning less than the short test salary level.

The Department believes that the proposed rule could reduce burden on employers of nonexempt workers who earn between the current and proposed standard salary level. Currently, employers must rely on the duties test to determine the exemption status of these workers. But if this proposal is finalized, the exemption status of these workers will be determined based on the simpler salary level test.

### **X. Executive Order 13132, Federalism**

The Department has reviewed this proposed rule in accordance with Executive Order 13132 regarding federalism and determined that it does not have federalism implications. The proposed rule would 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.

### **XI. Executive Order 13175, Indian Tribal Governments**

This proposed rule will not have tribal implications under Executive Order 13175 that would require a tribal summary impact statement. The proposed rule would not have substantial direct effects on one or more Indian tribes, on the relationship between the Federal Government and Indian tribes, or on the distribution of power and responsibilities between the Federal Government and Indian tribes.

### **List of Subjects in 29 CFR Part 541**

Labor, Minimum wages, Overtime pay, Salaries, Teachers, Wages.

For the reasons set out in the preamble, the Wage and Hour Division, Department, of Labor proposes to amend 29 CFR part 541 as follows:

### **PART 541—DEFINING AND DELIMITING THE EXEMPTIONS FOR EXECUTIVE, ADMINISTRATIVE, PROFESSIONAL, COMPUTER, AND OUTSIDE SALES EMPLOYEES**

- 1. The authority citation for part 541 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. Add § 541.5 to read as follows:

#### **§ 541.5 Severability.**

If any provision of this part is held to be invalid or unenforceable by its terms, or as applied to any person or circumstance, or stayed pending further agency action, the provision must be construed so as to continue to give the maximum effect to the provision permitted by law, unless such holding be one of utter invalidity or unenforceability, in which event the provision will be severable from part 541 and will not affect the remainder thereof.

- 3. Amend § 541.100, by revising paragraph (a)(1) to read as follows:

#### **§ 541.100 General rule for executive employees.**

(a) \* \* \*

(1) Compensated on a salary basis at not less than the level set forth in § 541.600;

\* \* \* \* \*

- 4. Amend § 541.200, by revising paragraph (a)(1) to read as follows:

<sup>468</sup> Private sector payroll costs are projected to be \$7.8 trillion in 2022 based on private sector payroll costs of \$6.6 trillion in 2017, inflated to 2022 dollars using the GDP deflator. 2017 Economic Census of the United States.

<sup>469</sup> Private sector revenues in 2017 were \$37.0 trillion using the 2017 Economic Census of the United States. This was inflated to 2022 dollars using the GDP deflator.

**§ 541.200 General rule for administrative employees.**

(a) \* \* \*

(1) Compensated on a salary or fee basis at not less than the level set forth in § 541.600;

\* \* \* \* \*

■ 5. Amend § 541.204, by revising paragraph (a)(1) to read as follows:

**§ 541.204 Educational establishments.**

(a) \* \* \*

(1) Compensated on a salary or fee basis at not less than the level set forth in § 541.600; or on a salary basis which is at least equal to the entrance salary for teachers in the educational establishment by which employed; and

\* \* \* \* \*

■ 6. Amend § 541.300, by revising paragraph (a)(1) to read as follows:

**§ 541.300 General rule for professional employees.**

(a) \* \* \*

(1) Compensated on a salary or fee basis at not less than the level set forth in § 541.600; and

\* \* \* \* \*

■ 7. Amend § 541.400, by revising the first sentence of paragraph (b) to read as follows:

**§ 541.400 General rule for computer employees.**

\* \* \* \* \*

(b) The section 13(a)(1) exemption applies to any computer employee who is compensated on a salary or fee basis at not less than the level set forth in § 541.600. \* \* \*

\* \* \* \* \*

■ 8. Revise § 541.600 to read as follows:

**§ 541.600 Amount of salary required.**

(a) *Standard salary level.* (1) 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 standard salary level (the 35th percentile of weekly earnings of full-time nonhourly workers in the lowest-wage Census Region), unless employed in American Samoa as set forth in paragraph (b) of this section, exclusive of board, lodging, or other facilities. As of [EFFECTIVE DATE OF THE FINAL RULE], and until such time as the standard salary level is updated pursuant to § 541.607, the standard salary level is \$1,059 per week. Administrative and professional employees may also be paid on a fee basis, as defined in § 541.605.

(2) Beginning 3 years from the date the \$1,059 per week salary level takes effect, and every 3 years thereafter, the

Secretary will update the amount of the required standard salary level pursuant to § 541.607.

(b) *American Samoa.* To qualify as an exempt executive, administrative, or professional employee under section 13(a)(1) of the Act, an employee in American Samoa (except if employed by the Federal Government), must be compensated on a salary basis at a rate of not less than 84 percent of the standard salary level applicable under paragraph (a) of this section (e.g., \$890 per week when the standard salary level is \$1,059), exclusive of board, lodging, or other facilities. Provided that 90 days after the highest industry minimum wage for American Samoa equals the minimum wage under section 6(a)(1) of the Act, exempt employees employed in all industries in American Samoa must be paid the full standard salary level set forth in paragraph (a) of this section, subject to the exceptions provided in paragraphs (d) through (f) of this section. Administrative and professional employees may also be paid on a fee basis, as defined in § 541.605.

(c) *Frequency of payment.* The salary level requirement may be translated into equivalent amounts for periods longer than one week. For example, the \$1,059 per week requirement described in paragraph (a) of this section would be met if the employee is compensated biweekly on a salary basis of not less than \$2,118, semimonthly on a salary basis of not less than \$2,295, or monthly on a salary basis of not less than \$4,589. However, the shortest period of payment that will meet this compensation requirement is one week.

(d) *Alternative salary level for academic administrative employees.* In the case of academic administrative employees, the salary level requirement also may be met by compensation on a salary basis at a rate at least equal to the entrance salary for teachers in the educational establishment by which the employee is employed, as provided in § 541.204(a)(1).

(e) *Hourly rate for computer employees.* In the case of computer employees, the compensation requirement also may be met by compensation on an hourly basis at a rate not less than \$27.63 an hour, as provided in § 541.400(b).

(f) *Exceptions to the standard salary criteria.* In the case of professional employees, the compensation requirements in this section shall not apply to employees engaged as teachers (see § 541.303); employees who hold a valid license or certificate permitting the practice of law or medicine or any of their branches and are actually engaged in the practice thereof (see

§ 541.304); or to employees who hold the requisite academic degree for the general practice of medicine and are engaged in an internship or resident program pursuant to the practice of the profession (see § 541.304). In the case of medical occupations, the exception from the salary or fee requirement does not apply to pharmacists, nurses, therapists, technologists, sanitarians, dietitians, social workers, psychologists, psychometrists, or other professions which service the medical profession.

■ 9. Amend § 541.601 by:

■ a. Adding introductory text to paragraph (a);

■ b. Revising paragraph (a)(1);

■ c. Revising paragraph (a)(2);

■ d. Adding paragraph (a)(3);

■ e. Revising the first sentence of paragraph (b)(1); and

■ f. Revising the second, third, and fourth sentences of paragraph (b)(2).

The revisions and additions read as follows:

**§ 541.601 Highly compensated employees.**

(a) An employee shall be exempt under section 13(a)(1) of the Act if:

(1) The employee receives not less than the total annual compensation level (the annualized earnings amount of the 85th percentile of full-time nonhourly workers nationally), and 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. As of [EFFECTIVE DATE OF THE FINAL RULE], and until such time as the total annual compensation level is updated pursuant to § 541.607, such an employee must receive total annual compensation of at least \$143,988.

(2) Beginning 3 years from the date the \$143,988 total annual compensation level takes effect, and every 3 years thereafter, the Secretary will update the required total annual compensation amount pursuant to § 541.607.

(3) Where the annual period covers periods both prior to and after the \$143,988 total annual compensation level takes effect, or the effective date of any future change to the total annual compensation requirement made pursuant to § 541.607, the amount of total annual compensation due will be determined on a proportional basis.

(b)(1) Total annual compensation must include at least a weekly amount equal to that 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) will not apply to highly compensated employees. \* \* \*

(2) \* \* \* For example, for a 52-week period beginning [EFFECTIVE DATE OF



FINAL RULE], an employee may earn \$120,000 in base salary, and the employer may anticipate based upon past sales that the employee also will earn \$25,000 in commissions. However, due to poor sales in the final quarter of the year, the employee only earns \$20,000 in commissions. In this situation, the employer may within one month after the end of the year make a payment of at least \$3,988 to the employee. \* \* \*

\* \* \* \* \*

■ 10. Amend § 541.604 by:

- a. Revising the second, third, and fourth sentences of paragraph (a); and
- b. Revising the third sentence in paragraph (b).

The revisions read as follows:

**§ 541.604 Minimum guarantee plus extras.**

(a) \* \* \* Thus, for example, an exempt employee guaranteed at least \$1,059 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 \$1,059 each week paid on a salary basis. Similarly, the exemption is not lost if an exempt employee who is guaranteed at least \$1,059 each week paid on a salary basis also receives additional compensation based on hours worked for work beyond the normal workweek. \* \* \*

(b) \* \* \* Thus, for example, an exempt employee guaranteed compensation of at least \$1,125 for any week in which the employee performs any work, and who normally works four or five shifts each week, may be paid \$325 per shift without violating the \$1,059 per week salary basis requirement. \* \* \*

- 11. Amend § 541.605 by revising the second sentence of paragraph (b) to read as follows:

**§ 541.605 Fee basis.**

\* \* \* \* \*

(b) \* \* \* Thus, for example, an artist paid \$550 for a picture that took 20 hours to complete meets the \$1,059 minimum salary requirement for exemption since earnings at this rate would yield the artist \$1,100 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.* (1) Beginning 3 years from [EFFECTIVE DATE OF THE FINAL RULE], and every 3 years thereafter, the amount required to be paid to an exempt employee on a salary or fee basis, as applicable, pursuant to § 541.600(a) will be updated to reflect current earnings data.

(2) The Secretary will determine the lowest-wage Census Region for paragraph (a)(1) of this section using the 35th 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.

(b) *Highly compensated employees.* (1) Beginning 3 years from [EFFECTIVE DATE OF THE FINAL RULE], and every 3 years thereafter, the amount required in total annual compensation for an exempt highly compensated employee pursuant to § 541.601 will be updated to reflect current earnings data.

(2) The Secretary will use the 85th percentile of weekly earnings of full-time nonhourly workers nationally based on data from the Current Population Survey as published by the Bureau of Labor Statistics for paragraph (b)(1) of this section.

(c) *Notice.* (1) Not fewer than 150 days before each automatic update of earnings requirements under this section, the Secretary will publish a notice in the **Federal Register** stating the updated amounts required by paragraphs (a) and (b) of this section, which shall be determined by applying the methodologies set forth in those paragraphs to data from the four quarters preceding the notice as published by the Bureau of Labor Statistics.

(2) No later than the effective date of the updated earnings requirements, the Wage and Hour Division will publish on its website the applicable earnings requirements for employees paid pursuant to this part.

(d) *Delay of updates.* An automatic update to the earnings thresholds is delayed from taking effect for a period of 120 days if the Secretary has separately published a notice of proposed rulemaking in the **Federal Register**, not fewer than 150 days before the date the automatic update is set to take effect, proposing changes to the earnings threshold(s) and/or automatic updating mechanism. If the Secretary does not issue a final rule affecting the

scheduled automatic update to the earnings thresholds by the end of the 120-day extension, the updated amounts published in accordance with paragraph (c)(1) of this section will take effect upon the expiration of the 120-day period. The 120-day delay of a scheduled update under this paragraph will not change the effective dates for future automatic updates of the earnings requirements under this section.

- 13. Revise § 541.709 to read as follows:

**§ 541.709 Motion picture producing industry.**

(a) *Base rate.* The requirement that the employee be paid “on a salary basis” does not apply to an employee in the motion picture producing industry who is compensated at a base rate of at least \$1,617 per week (exclusive of board, lodging, or other facilities), except as provided in paragraph (b) of this section. 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:

(1) 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

(2) 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.

(b) *Updating the base rate.* Upon the date of each increase to the standard salary level pursuant to § 541.607, the base rate required to be paid to an exempt motion picture producing employee pursuant to this section will be updated from the previously applicable base rate, adjusted by the same percentage as the updated standard salary set by § 541.607(a), and rounded to the nearest multiple of \$1.00.

**Julie A. Su,**

*Acting Secretary, Department of Labor.*

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