

Parsing The Impact Of White Collar FLSA Exemption Proposal

By **Stephen Bronars** (June 13, 2022, 4:05 PM EDT)

The salary threshold for the white collar Fair Labor Standards Act overtime exemption is \$684 per week or \$35,568 per year.

Employees earning less than \$684 per week must be paid an overtime premium of time and a half for hours exceeding 40 hours in a week, regardless of their job duties.

The Congressional Progressive Caucus recently proposed an increase in the salary threshold that they claim will reach \$82,732 by 2026 — \$1,591 per week. The CPC proposal states that "automatic updates to prevent the erosion of the salary threshold over time" should be implemented.[1]



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This article shows that if the CPC proposal were implemented today, the salary threshold would be \$1,500 per week or 119% higher than the current threshold. In addition, the automatic updates proposed by the CPC would cause substantially faster growth in the threshold by 2026 than the 6% increase assumed by the CPC.[2]

The proposed salary threshold increase would cause the reclassification of millions of managers and professionals as hourly employees, especially in low-wage states, and require nearly all retail supervisors to be classified as nonexempt.

Businesses required to accurately record the work hours and accurately calculate regular rates of millions of managers and professionals, many of whom receive bonuses and commissions, are likely to face a considerable increase in compliance costs.

Economic theory suggests that the proposed increase in the salary threshold is questionable public policy because, despite the costs, it is not expected to increase the average compensation of reclassified workers but will likely increase the variability of their compensation from week to week.

Proposed White Collar FLSA Salary Threshold Is Based on the Current Population Survey

The May 2016 U.S. Department of Labor final rule set the white collar salary threshold at the 40th percentile of the earnings distribution of full-time workers not paid by the hour in the South, but that threshold was never implemented.[3]

The proposed CPC threshold is set at the 55th percentile of the earnings distribution of full-time workers not paid by the hour in the entire U.S. The thresholds are based on estimated percentiles from the Current Population Survey.[4]

Although the research series tabulations used for threshold calculations have not been published since 2017, public use microdata can be used to approximate pay distribution percentiles.[5]

The following table presents alternative salary thresholds based on estimated percentiles of the earnings distribution of full-time salaried workers from public use annual microdata for workers in both the South and the entire U.S. from 2015 to 2022.

Alternative White Collar FLSA Minimum Salary Thresholds Based on Percentiles of Salaried Employee Pay Distribution

YEAR	40TH PERCENTILE SOUTH		55TH PERCENTILE U.S.	
	ANNUAL	FIRST QUARTER	ANNUAL	FIRST QUARTER
2015	\$900	\$884	\$1,200	\$1,192
2016	\$923	\$923	\$1,250	\$1,229
2017	\$961	\$961	\$1,250	\$1,250
2018	\$962	\$962	\$1,346	\$1,308
2019	\$1,000	\$969	\$1,350	\$1,346
2020	\$1,058	\$1,019	\$1,442	\$1,385
2021	\$1,058	\$1,058	\$1,442	\$1,442
2022		\$1,115		\$1,500

The most recent data, from the first quarter of 2022, indicate that the 40th percentile in the South is \$1,115 per week — \$57,980 per year — and the 55th percentile for the entire U.S. is \$1500 per week — \$78,000 per year.

The CPC proposed salary threshold is 119.3% higher than the current salary threshold, 64.3% above the May 2016 threshold and 34.5% higher than the threshold obtained by applying the May 2016 final rule methodology to data from 2022.

The Impact of Automatic Increases to the Threshold

The CPC proposal will increase the threshold faster than the inflation rate because the threshold is indexed to a moving target. The proposal requires that only the top 45% of highest-paid salaried employees can be exempt from the overtime provisions of the FLSA.

Reclassification of workers with lower salaries raises the threshold, independent of inflation, as the top 45% is calculated among an increasingly narrow group of higher-paid salaried employees.

For example, if just one of four employees with pay below the 55th percentile is reclassified as hourly, then 13.75% — one-fourth of 55% — of salaried employees earning less than the threshold leave the salaried pay distribution as they become hourly employees. New percentiles calculated for the remaining 86.25% of salaried employees are higher than before.

In this example, using 2022 data, the new 55th percentile is approximately the same as the 61st percentile before workers were reclassified or \$1,634 per week. The reclassification of one-fourth of employees who fail the salary test, with no change in any individual's salary, increases the threshold by about 8.9%.

The CPC expects the minimum salary threshold in 2026 to be \$1,591 per week, only 6% higher than if its proposal was implemented today. This understates the likely effects of the CPC proposal from one year to the next.

The requirement that only the top 45% of highest-paid salaried employees are exempt from the FLSA will result in increasingly higher salary thresholds so that eventually only highly compensated employees will be exempt from the FLSA.[6]

The CPC Proposal Will Have a Disproportionate Affect on Professionals and Managers in Low-Wage States

Although 55% of all salaried employees are expected to fail the white collar salary test proposed by the CPC, the effect is not evenly distributed. In some occupations and labor market areas, more than 55% of salaried employees are expected to fail the salary test, and in other occupations and areas, the expected failure rate is lower than 55%.

The table below shows the percentage of employees in 10 selected occupations that are expected to earn less than the CPC salary threshold, nationwide and in six low-wage states, for which Bureau of Labor Statistics pay data by occupation is available.

For employees to be exempt from the FLSA's overtime requirements and be paid a salary rather than an hourly wage, they must perform specific executive, administrative or professional job duties — the duties test — and their salary must exceed the threshold set by the DOL — the salary test.

Because nearly all employees in the listed occupations perform job duties that satisfy the duties test, whether an employee in one of these occupations is exempt from the FLSA depends almost exclusively on whether their salary is above the salary threshold set by the DOL.[7]

The percentage of employees in the U.S. expected to fail the CPC salary test ranges from 25% for facilities managers to 72% for first-line supervisors of office workers. In low-wage states, a higher proportion of professionals and managers typically earns less than \$1,500 per week and would fail the salary test.

For example, while 47% of accountants in the U.S. are expected to fail the CPC salary test, between 68% and 71% of accountants in these six low-wage states are expected to fail the CPC salary test.

Percentage of Employees Expected to Fail CPC Proposed Salary Test for White Collar FLSA Exemption by Occupation and State

OCCUPATION	U.S.	AL	AR	LA	MS	SC	WV
Accountants and Auditors	47%	68%	69%	68%	71%	68%	67%
Architects	43%		47%	24%	47%	46%	49%
Chemists	44%	46%	59%	47%	54%	67%	56%
Conservation Scientists	66%		55%	67%	85%	62%	83%
Facilities Managers	25%	19%	27%	28%	63%	21%	33%
First-Line Supervisors of Office Workers	72%	87%	88%	87%	88%	85%	88%
Insurance Underwriters	48%	69%	53%	85%	72%	69%	86%
Microbiologists	45%	72%	72%			85%	75%
Statisticians	30%	72%	41%	61%		70%	73%
Zoologists	65%	79%	84%	61%	57%	85%	

For most of the occupations listed in the table above, a substantial majority of employees in low-wage states are expected to fail the proposed CPC salary test despite their managerial and professional duties.

Effect of CPC Proposed Threshold on Retail Trade

In the 2016 final rule, the DOL indicated that a majority — between 50% and 90% — of first-line supervisors of retail sales workers engaged in managerial activities that satisfy the duties test.

Even though the DOL would consider a majority of retail supervisors to be bona fide managers based on their job duties, if the CPC proposal were adopted today, 91% of retail supervisors nationwide would fail the salary test and lose their overtime exemption.

In effect, the CPC proposal would immediately require more than 1 million retail supervisors to be nonexempt from the FLSA overtime provisions, regardless of their job duties.[8]

Economic Theory Suggests That an Increase in Salary Threshold Has Little Impact on Average Compensation

Economic theory argues that employee compensation is determined by worker productivity and supply and demand conditions, and not whether an employee is paid by the hour or the week. According to this theory, increases in the salary threshold will have little, if any, effect on average compensation for employees who earn well above the minimum wage.[9]

Consider, for example, a salaried employee who earns \$1040 per week and typically works 48 hours per week. Economic theory suggests that, if an employer were to convert this worker's position to hourly, the hourly wage rate would be \$20 so that in a typical week the employee would earn \$800 — at \$20 per hour — for the first 40 hours of work and \$240 — at \$30 per hour — for the final eight hours.

Thus, in a typical week the employee is expected to earn \$1040, whether paid a salary or paid by the hour. The only substantive impact of the reclassification to an hourly position is that if overtime hours fluctuate from week to week, the employee's pay will also fluctuate from week to week.

Conclusion

The CPC proposal for more than doubling the salary threshold for the white collar FLSA exemption will substantially increase the number of white collar employees who are nonexempt from the FLSA, especially in low-wage states in the South. The automatic indexation of the salary threshold to a fixed percentile of the pay distribution among salaried employees will cause growth in the salary threshold that is much faster than inflation.

The policy changes proposed by the CPC will increase wage and hour compliance costs by requiring employers to accurately record the work hours and accurately calculate regular rates of millions of managers and professionals, many of whom receive bonuses and commissions in addition to their salaries.

Economic theory suggests that the benefits to white collar workers who are reclassified as hourly are likely to be small. There is no reason to expect a white collar worker's weekly compensation to increase simply because pay is by the hour, instead of weekly.

An expected consequence of a shift of millions of white collar workers from salaried to hourly positions is an increase in the variability of weekly paychecks for these workers. Higher variability in weekly pay, without an increase in the typical weekly paycheck, is problematic for employees facing mortgage payments, car payments and other financial obligations.

The Biden administration should reject the CPC proposal because it will increase the variability in weekly pay, cause employer costs to rise, and increase the likelihood of future FLSA litigation, without increasing the average pay of affected employees.

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[1] The CPC proposes "Executive Action" which would involve the DOL changing the FLSA salary threshold in a way similar to what was attempted in 2016. https://progressives.house.gov/_cache/files/6/8/68a45450-d818-4c0c-a564-cd85ea395d47/C7DC22A98A6BE5D74603B59C3FAE856F.final-cpc-recommendations-for-executive-action-3-17-22-1-.pdf.

[2] The \$82,732 threshold in 2026 referenced by the CPC is 6% higher than the \$78,000 threshold that would apply today.

[3] The May 2016 salary threshold of \$913 per week, based on the 40th percentile of the earnings distribution of salaried employees in the South region, would have more than doubled the previous threshold and was blocked by a preliminary injunction (*Nevada et al. v. U.S. Department of Labor et al.*, No. 4:16-CV-00731). The \$684 per week threshold became effective in January 2020.

[4] The CPS is conducted by the Bureau of Labor Statistics (BLS). Percentile estimates are from a special CPS "research series." For simplicity I refer to workers not paid by the hour as salaried employees although they include workers paid in other ways as well. The BLS states "These research data are tabulated for workers who do not report being paid an hourly rate. The CPS does not include questions on whether workers are covered by the federal Fair Labor Standards Act (FLSA) or any other federal, state, or local statute. While non-hourly workers typically receive a salary, commissions, tips, or pay in kind from a private employer or from a government unit, the survey does not specifically identify salaried workers." https://www.bls.gov/cps/research_series_earnings_nonhourly_workers.htm.

[5] <https://www.law360.com/employment-authority/labor/articles/1400879/old-ot-rule-method-would-burden-cos-in-low-wage-states>.

[6] Employees earning \$107,432 or more annually are exempt from the FLSA because they are "highly compensated employees." The "highly compensated" FLSA exemption is the only reason why the continued increases in the minimum threshold proposed by the CPC will allow some white collar employees to be classified as exempt. The CPC did not specify an alternative highly compensated threshold.

[7] For an employee to legally be exempt from the FLSA overtime provisions (i.e. be a salaried employee) the employee must hold a "bona fide" executive, administrative or professional (EAP) position. To qualify for the EAP overtime exemption, employees must meet certain test regarding their job duties. See https://www.dol.gov/sites/dolgov/files/WHD/legacy/files/fs17b_executive.pdf, https://www.dol.gov/sites/dolgov/files/WHD/legacy/files/fs17c_administrative.pdf, or https://www.dol.gov/sites/dolgov/files/WHD/legacy/files/fs17d_professional.pdf. The 2015 and 2016 DOL proposals to increase the salary threshold classified occupations into based on the probability of passing the EAP duties test. The occupations in the Table have the highest (at least 90%) probability of passing the EAP duties test.

[8] According to the BLS there are about 1.14 million employees in the First-Line Supervisor of Retail Sales Workers occupation code, and about 1.04 million (91%) earn less than \$1,500 per week.

[9] Stephen J. Trejo, "The Effects of Overtime Pay Regulation on Worker Compensation," *The American Economic Review*, Vol. 91, No. 4, September 1991, pp. 719-740.