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Old OT Rule Method Would Burden Cos. In Low-Wage States

By **Stephen Bronars** (July 8, 2021, 4:47 PM EDT)


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In May 2016 the U.S. Department of Labor enacted a salary threshold for the white collar Fair Labor Standards Act overtime exemption of $913 per week or $47,476 per year, with automatic increases every three years. This regulation would have prevented employees earning less than $47,476 per year from being exempt from the overtime provisions of the FLSA, regardless of their job duties.

The regulation was challenged in federal court and eventually overturned.

The current salary threshold for the white collar exemption of $684 per week or $35,568 per year became effective Jan. 1, 2020. Employees who earn less than $684 per week must be paid overtime for hours exceeding 40 in a week even if they are classified as a manager or professional.

In the past few weeks Secretary of Labor Marty Walsh indicated that the DOL is studying an increase in this salary threshold because he believes it is too low.

In this article, I show that if the Biden administration uses the same methodology for determining the salary threshold as the Obama administration, the new threshold for the white collar FLSA overtime exemption will be about $56,000 per year. This threshold is about 18% higher than what was enacted five years ago and is more than 57% higher than the current threshold.

I also explain that a single $56,000 nationwide salary threshold would likely result in the reclassification of many managers and professionals in low-wage states, while having much less impact in high-wage states and metropolitan areas.

Salary Threshold for White Collar Exemption in the 2016 Final Rule

The May 2016 final rule set the salary threshold for the white collar FLSA overtime exemption at the 40th percentile of weekly earnings of full-time workers not paid by the hour — that is, salaried workers — in the lowest-wage census region (the South) in the fourth quarter of 2015.[1]

Had the rule gone into effect, the first automatic update to the salary threshold would have occurred on Jan. 1, 2020.[2]

If the Biden administration uses the same methodology as the May 2016 final rule, it will set the salary threshold for the white collar FLSA exemption at the current 40th percentile of the weekly earnings of full-time salaried workers in the South region.

Unfortunately, the U.S. Bureau of Labor Statistics has not published the results of the research series used to calculate this 40th percentile since the end of 2017.[3]

While tabulations of the BLS' research series are no longer published, public use microdata from the BLS and the U.S. Census Bureau can approximate the official calculation of the 40th percentile.

To illustrate the accuracy of these approximations, Table 1 compares the salary thresholds in the May 2016 final rule to the 40th percentile of the weekly earnings distribution of salaried workers by census region based on the public use microdata from the fourth quarter of 2015.[4]

Each weekly salary amount is within $10 (about 1%) of the percentiles reported by the DOL in the 2016 final rule.[5]

Table 1: 40th Percentile of Earnings for Full-Time Workers not Paid by the Hour by Census Region 2015

Census Region	40th Percentile of Full-Time Workers not Paid by Hour (in 4th quarter 2015) as Reported in May 2016 DOL Final Rule	Calculated from Public Use Current Population Survey Microdata (in 4th quarter 2015)
South	$913	$923
Midwest	$994	$1000
Northeast	$1036	$1038
West	$1050	$1057
All Census Regions	$972	$962

A New Possible Salary Threshold for the Exemption

On June 9, while testifying before the House Education and Labor Committee, Secretary of Labor Marty Walsh said that the DOL is currently studying an increase in the salary threshold for the white collar exemption because he believes the current threshold is "definitely" too low.

He also indicated that the DOL is studying possible automatic increases to the threshold.[6]

Table 2 presents the 40th percentile of the weekly earnings of full-time salaried workers by census region based on public use microdata for the fourth quarter of 2020.

The most recent 40th percentile in the South region is $1,077 per month, or $56,004 per year. This threshold is about 57.5% higher than the current salary threshold and about 18% above the threshold that the Obama administration enacted in 2016.

The earnings of salaried workers, especially for lower-paid salaried workers, increased substantially between 2017 and 2020; the 40th percentile across all census regions increased by 15.4%.

There are several possible explanations for the recent increase in pay among lower-paid salaried workers, including the pandemic and the possible reclassification of lower-paid salaried employees to hourly positions.

Table 2: 40th Percentile of Earnings for Full-Time Workers not Paid by the Hour by Census Region 2020	
Census Region	Calculated from Public Use Current Population Survey Microdata (in 4th quarter 2020)
South	$1077
Midwest	$1153
Northeast	$1211
West	$1250
All Census Regions	$1154

Different Impact on Low-Wage and High-Wage States

The South, in addition to having the lowest average salaries, is the largest census region with 16 states and the District of Columbia, and accounts for almost 40% of the U.S. workforce.

There are more than twice as many salaried workers in the South than in the Midwest or the Northeast regions, and nearly 80% more than in the West region.[7]

The South region contains vastly different labor markets with different average salaries. Average weekly earnings among salaried full-time employees in Maryland, Virginia and the District of Columbia are about 36% higher than in the three lowest wage states in the South — Mississippi, Oklahoma and West Virginia.[8]

If the $56,004 per year threshold was applied to Mississippi, Oklahoma and West Virginia, about 52% of full-time salaried employees would fail the salary test and could not be exempt from overtime.

Only about 29% of full-time salaried employees in Maryland, Virginia and the District of Columbia earn less than the threshold, and fewer employees will be affected by this possible change in the regulation.

The May 2016 final rule methodology, if adopted in 2021, would raise the white collar salary threshold in almost every county in the U.S.

California, New York and Washington are three of the highest paid states in the U.S., and each has adopted a threshold higher than the DOL's current salary test.

The $56,004 threshold, however, is higher than the 2021 salary thresholds for white collar exemptions for all employees in Washington, for employees of small businesses in California, and for most employees in New York.

The threshold for small businesses in Washington is $42,712.80 and for businesses with 25 or more employees it's $49,831.60. The threshold for small businesses in California is $54,080 and for businesses with 25 or more employees it's $58,240.[9]

Average weekly earnings of salaried workers in high-wage states, such as Connecticut and Washington, are about 50% higher than in Mississippi, Oklahoma and West Virginia.

Despite these substantial differences in average salaries across states, the May 2016 final rule methodology imposes the same salary test for overtime exemption in every state.

While over half of salaried employees would fail this salary test and lose their overtime exemption in Mississippi, Oklahoma and West Virginia, fewer than one-quarter of salaried employees in high-wage states would fail this salary test.

Conclusion

The methodology for determining the salary threshold for the overtime exemption in the May 2016 final rule ignores the considerable variation in pay across areas within the South region.

Many less-experienced managers and professionals in lower-wage states, primarily in the South, earn less than $56,000 per year, the 2021 salary threshold based on the 2016 methodology.

With this threshold, many employers in lower-wage states will be required to reclassify salaried managers and professionals as hourly nonexempt employees, not because the workers fail the white collar duties test, but because the business operates in an area with lower average salaries.

The cost and inconvenience of reclassifying managers and professionals will disproportionately affect businesses in lower-wage states because much fewer white collar employees earn less than $56,000 in states with higher average salaries.

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[1] The threshold is based on special "research series" tabulations from the Current Population Survey (CPS) a monthly survey conducted by the Bureau of Labor Statistics and the Census Bureau. 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 nonhourly 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.

[2] Because the May 2016 Final Rule required that the DOL publish the updated threshold by early August 2019, the most recent salary data at that time would likely have been from the first quarter 2019.

[3] At the end of 2017, the 40th percentile of the weekly earnings of full-time salaried workers was $929 per week in the South, or just 1.75% higher than the salary threshold specified in the May 2016 Final Rule.

[4] These public use data files are available at https://www.nber.org/research/data/current-population-

survey-cps-data-nber.

[5] In addition, according to the BLS, the 95% confidence interval for the 40th percentile of the full-time salary distribution in the South in the last quarter of 2015 was $913 plus or minus about $26.

[6] https://news.bloombergtax.com/payroll/overtime-pay-rule-under-review-by-labor-department-walsh-says.

[7] These calculations are based on the same BLS and Census public use microdata used to calculate the 40th percentiles by region.

[8] Id.

[9] The New York salary threshold for the white collar exemption is $48,750 for counties outside the New York City area and $54,600 for suburban New York City counties. New York City has a white collar exemption threshold of $58,500.