



441 G St. N.W.  
Washington, DC 20548

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June 7, 2016

The Honorable Lamar Alexander  
Chairman  
The Honorable Patty Murray  
Ranking Member  
Committee on Health, Education, Labor, and Pensions  
United States Senate

The Honorable John Kline  
Chairman  
The Honorable Robert "Bobby" Scott  
Ranking Member  
Committee on Education and the Workforce  
House of Representatives

Subject: *Department of Labor, Wage and Hour Division: Defining and Delimiting the Exemptions for Executive, Administrative, Professional, Outside Sales and Computer Employees*

Pursuant to section 801(a)(2)(A) of title 5, United States Code, this is our report on a major rule promulgated by the Department of Labor, Wage and Hour Division (Labor) entitled "Defining and Delimiting the Exemptions for Executive, Administrative, Professional, Outside Sales and Computer Employees" (RIN:1235-AA11). We received the rule on May 23, 2016. It was published in the *Federal Register* as a final rule on May 23, 2016. 81 Fed. Reg. 32,391.

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

In this final rule, Labor updates the standard salary level and total annual compensation requirements to more effectively distinguish between overtime-eligible white collar employees and those who may be exempt, thereby making the exemption easier for employers and employees to understand and ensuring that FLSA's intended overtime protections are fully implemented. Labor sets the standard salary level for exempt EAP employees at the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region. Labor also permits employers to satisfy up to 10 percent of the standard salary requirement with nondiscretionary bonuses, incentive payments, and commissions, provided these forms of

compensation are paid at least quarterly. Labor sets the total annual compensation requirement for an exempt Highly Compensated Employee (HCE) equal to the annualized weekly earnings of the 90th percentile of full-time salaried workers nationally. Labor also adds a provision to the regulations that automatically updates the standard salary level and HCE compensation requirements every 3 years by maintaining the earnings percentiles set in the final rule to prevent these thresholds from becoming outdated. Finally, Labor has not made any changes in this final rule to the duties tests for the EAP exemption.

Enclosed is our assessment of Labor's compliance with the procedural steps required by section 801(a)(1)(B)(i) through (iv) of title 5 with respect to the rule. Our review of the procedural steps taken indicates that Labor complied with the applicable requirements.

If you have any questions about this report or wish to contact GAO officials responsible for the evaluation work relating to the subject matter of the rule, please contact Shirley A. Jones, Assistant General Counsel, at (202) 512-8156.

signed

Robert J. Cramer  
Managing Associate General Counsel

Enclosure

cc: Mary Ziegler  
Assistant Administrator for Policy  
Department of Labor

REPORT UNDER 5 U.S.C. § 801(a)(2)(A) ON A MAJOR RULE  
ISSUED BY THE  
DEPARTMENT OF LABOR  
WAGE AND HOUR DIVISION  
ENTITLED  
“DEFINING AND DELIMITING THE EXEMPTIONS FOR  
EXECUTIVE, ADMINISTRATIVE, PROFESSIONAL,  
OUTSIDE SALES AND COMPUTER EMPLOYEES”  
(RIN: 1235-AA11)

(i) Cost-benefit analysis

The Department of Labor (Labor) included a cost-benefit analysis in the final rule. Based on the economic impact analysis of the final rule, Labor determined that the final rule will result in year 1 costs for state and local governments totaling \$115.1 million, of which \$38.8 million are direct employer costs and \$76.3 million are payroll increases. Additionally, the final rule will lead to \$0.3 million in dead weight loss (DWL). In subsequent years, Labor estimated that state and local governments may experience payroll increases of as much as \$85.4 million in a year when the salary level is automatically updated. Labor determined that the final rule will result in year 1 costs to the private sector of approximately \$1.8 billion, of which \$637.7 million are direct employer costs and \$1.2 billion are payroll increases. Additionally, the final rule will result in \$6.0 million in DWL. In subsequent years, Labor estimated that the private sector may experience a payroll increase of as much as \$1.5 billion per year.

According to Labor, the largest estimated impact to workers is likely the transfer of income to workers from some combination of employers, end consumers, and other workers; but, to the extent that the utility derived by workers outweighs the disutility experienced by employers and other entities experiencing the negative side of transfers, there may be a societal welfare increase due to this transfer. According to Labor, the channels through which societal welfare may change, and other secondary benefits, transfers and costs may occur, include: decreased litigation costs due to fewer workers subject to the duties test, the multiplier effect of the transfer, changes in productivity, potentially reduced dependence on social assistance, and a potential increase in time off and its associated benefits to the social welfare of some workers (for instance, those who work so many hours that the overtime requirement renders their current combination of pay and hours worked non-compliant with the minimum wage). Additionally, Labor states that because of the increased salary level, overtime protection will be strengthened for 5.7 million salaried white collar workers and 3.2 million salaried blue collar workers who do not meet the duties requirements for the executive, administrative, professional, outside sales, and computer employees (EAP) exemption, but who earn between the current minimum salary level of \$455 per week and the updated salary level, because their right to minimum wage and overtime protection will be clear rather than depend upon an analysis of their duties.

(ii) Agency actions relevant to the Regulatory Flexibility Act (RFA), 5 U.S.C. §§ 603-605, 607, and 609

Based on its methodology, Labor found that of the 7.5 million establishments relevant to this analysis, more than 80 percent (6.0 million) are small by Small Business Administration standards. These small establishments employ almost 50 million workers, about 37 percent of workers employed by all establishments (excluding self-employed, unpaid workers, and members of the armed forces), and account for roughly a third of total payroll (\$2.3 trillion of \$6.5 trillion). Labor estimates that 1.6 million of the 4.2 million affected workers (37.1 percent) are employed by small entities. This composes about 3.1 percent of the 49.8 million workers employed by small entities. Labor estimated a range of impacts for small entities. Labor estimated that the rule will affect 1.6 million workers who are employed by somewhere between 210,800 and 1.6 million small establishments; this composes from 3.5 percent to 25.9 percent of all small establishments. It also means that from 4.5 million to 5.9 million small establishments incur no more than minimal regulatory familiarization costs. As a result of this rule, Labor

expects total direct employer costs will range from \$157.9 million to \$206.8 million for affected small establishments in the first year after the promulgation of the final rule. An additional \$162.3 million to \$211.5 million in regulatory familiarization costs will be incurred by small establishments that do not employ affected workers.

To determine how small businesses will be affected in future years, Labor projected costs to small business for 9 years after year 1 of the rule. Projected affected employees in small firms follow a similar pattern to affected workers in all establishments. The number decreases gradually in years without automatic updates, but the increases in years with automatic updates offset this fall and result in a net growth over time. There are 1.6 million affected workers in small establishments in year 1 and 2.0 million in year 10. Costs to small establishments decrease in the years following year 1 because regulatory familiarization costs are zero in years without automatic updates, and adjustment costs are significantly smaller in years without automatic updating. However, both direct costs and payrolls increase over time as more workers become affected, leading to higher managerial costs and earnings for affected workers. Therefore, by year 10 additional costs and payrolls to small businesses have increased from \$688.3 in year 1 to \$901.8 in year 10. Despite this increase over the 10-year period, Labor states that even in year 10 costs and payroll increases are a relatively negligible 0.04 percent and 0.01 percent share of payroll and revenue respectively, assuming no growth in real firm payroll or revenues. Labor included a number of tables summarizing the estimated affected employees, industries, and costs.

(iii) Agency actions relevant to sections 202-205 of the Unfunded Mandates Reform Act of 1995 (UMRA), 2 U.S.C. §§ 1532-1535

Labor provided an analysis under UMRA and states that for purposes of UMRA, the rule includes a federal mandate that is expected to result in increased expenditures by the private sector of more than \$156 million in at least one year, but the rule will not result in increased expenditures by state, local, and tribal governments, in the aggregate, of \$156 million or more in any one year.

(iv) Other relevant information or requirements under acts and executive orders

Administrative Procedure Act, 5 U.S.C. §§ 551 *et seq.*

Labor published a Notice of Proposed Rulemaking (NPRM) to propose revisions to the part 541 regulations. 80 Fed. Reg. 38,516 (July 6, 2015). More than 270,000 individuals and organizations timely commented on the NPRM during the 60-day comment period that ended on September 4, 2015. Labor received comments from a broad array of constituencies, including small business owners, Fortune 500 corporations, employer and industry associations, individual workers, worker advocacy groups, unions, non-profit organizations, law firms (representing both employers and employees), educational organizations and representatives, religious organizations, economists, Members of Congress, federal government agencies, state and local governments and representatives, tribal governments and representatives, professional associations, and other interested members of the public. Significant issues raised in the timely received comments were summarized and addressed in the final rule, together with Labor's response to those comments and a topical discussion of the changes that have been made in the final rule and its regulatory text. According to Labor, it also received a number of submissions after the close of the comment period, including some campaign comments, from a range of commenters representing both employers and employees. Late comments were not considered in the development of this final rule and were not discussed in the final rule. In instances where an organization submitted both timely and untimely comments, only the timely comments were considered. Labor also states that it received a number of comments that were beyond the scope of this rule.

Paperwork Reduction Act (PRA), 44 U.S.C. §§ 3501-3520

According to Labor, the final rule does not impose new information collection requirements; rather, burdens under existing requirements are expected to increase as more employees receive minimum wage and overtime protections due to the proposed increase in the salary level requirement. The Office of Management and Budget (OMB) has assigned control number 1235-0018 to the Fair Labor Standards

Act (FLSA) information collections. OMB has assigned control number 1235-0021 to Employment Information Form collections, which Labor uses to obtain information from complainants regarding FLSA violations. In accordance with PRA, Labor solicited comments on the FLSA information collections and the Employment Information Form collections in the NPRM published July 6, 2015, as the NPRM was expected to impact these collections. 44 U.S.C. 3506(c)(2). Labor states that it also submitted a contemporaneous request for OMB review of the proposed revisions to the FLSA information collections, in accordance with 44 U.S.C. 3507(d). Labor has promulgated regulations at part 516 to establish the basic FLSA recordkeeping requirements, which are approved under OMB control number 1235-0018. The information collection approved under OMB control number 1235-0021 provides a method for the Wage and Hour Division (WHD) of Labor to obtain information from complainants regarding alleged violations of the labor standards the agency administers and enforces. This final rule revises the existing information collections previously approved under OMB control number 1235-0018 (Records to be Kept by Employers—Fair Labor Standards Act) and OMB control number 1235-0021 (Employment Information Form). An agency may not conduct an information collection unless it has a currently valid OMB approval, and Labor has submitted the identified information collection contained in the proposed rule to OMB for review under PRA under the Control Numbers 1235-0018 and 1235-0021. See 44 U.S.C. 3507(d); 5 C.F.R. 1320.11. Labor states that it has resubmitted the revised FLSA information collections to OMB for approval, and intends to publish a notice announcing OMB's decision regarding this information collection request.

Although, according to Labor, the final rule does not impose new information collection requirements, the changes adopted in the final rule may cause an increase in burden on the regulated community because employers will have additional employees to whom certain long-established recordkeeping requirements apply (e.g., maintaining daily records of hours worked by employees who are not exempt from the both minimum wage and overtime provisions). Additionally, the changes adopted in this final rule may cause an initial increase in burden if more employees file a complaint with WHD to collect back wages under the overtime pay requirements.

Under OMB Control Number 1235-0018, Labor summarized:

- Affected Public: Businesses or other for-profit, farms, not-for-profit institutions, state, local, and tribal governments, and individuals or households
- Total Respondents: 5,511,960 (2,506,666 affected by the final rule)
- Total Annual Responses: 46,057,855 (2,552,656 from the final rule)
- Estimated Burden Hours: 3,489,585 (2,506,666 from the final rule)
- Estimated Time per Response: Various
- Frequency: Various
- Total Burden Cost (capital/startup): 0
- Total Burden Costs (operation/maintenance): \$126,392,768 (\$90,791,443 from the final rule)

Under OMB Control Number 1235-0021, Labor summarized:

- Affected Public: Businesses or other for-profit, farms, not-for-profit institutions, state, local, and tribal governments, and individuals or households
- Total Respondents: 37,367 (2,017 added by this rulemaking)
- Estimated Number of Responses: 37,367 (2,017 added by this rulemaking)
- Estimated Burden Hours: 12,456 (672 hours added by this rulemaking)
- Estimated Time per Response: 20 minutes (unaffected by this rulemaking)
- Frequency: Once
- Other Burden Cost: 0

#### Statutory authorization for the rule

Labor promulgated the rule under authority of the 29 U.S.C. 213, specifically, section 13(a)(1) of FLSA, 29 U.S.C. 213(a)(1); Pub. L. No. 101-583, 104 Stat. 2871; Reorganization Plan No. 6 of 1950 (3 C.F.R., 1945-53 Comp., p. 1004); and Secretary's Order 01-2014 (Dec. 19, 2014), 79 Fed. Reg. 77,527 (Dec. 24, 2014). Labor further states that section 3(e) of FLSA, 29 U.S.C. 203(e), defines "employee" to include most individuals employed by a state, political subdivision of a state, or interstate governmental agency, and that section 3(x) of FLSA, 29 U.S.C. 203(x), also defines public agencies to include the government of a state or political subdivision thereof, or any interstate governmental agency.

#### Executive Order No. 12,866 (Regulatory Planning and Review)

Labor states that under Executive Order 12,866, OMB must determine whether a regulatory action is a "significant regulatory action," which includes an action that has an annual effect of \$100 million or more on the economy. Significant regulatory actions are subject to review by OMB. Labor states that the final rule is economically significant. Therefore, Labor has prepared a Regulatory Impact Analysis in connection with this final rule as required under section 6(a)(3) of Executive Order 12,866, and OMB has reviewed the rule.

#### Executive Order No. 13,132 (Federalism)

Labor determined that the final rule does not have federalism implications. Labor states that the final rule will not have substantial direct effects on the states, on the relationship between the national government and the states, or on the distribution of power and responsibilities among the various levels of government.