



To: The National Retail Federation

From: Oxford Economics

Date: July 17, 2015

Re: Updated impacts of raising the overtime exemption threshold

This letter updates estimates of the number of retail and restaurant workers affected by proposed new overtime regulations and the costs associated with those changes, which Oxford Economics originally calculated in our paper “Rethinking Overtime: How Increasing Overtime Exemption Thresholds will Affect the Retail and Restaurant Industries.” That report, published before the Department of Labor’s Notice of Proposed Rulemaking on this topic,¹ was based on 2013 Occupational Employment Survey data — the most recently available. The report considered three possible new exemption thresholds: \$610, \$808 and \$984 a week. Implicitly, these figures were in 2013 dollars. In the new Notice of Proposed Rulemaking, the DOL proposes to set the new overtime threshold at the 40th percentile of wages for full-time, non-hourly workers, which it forecasts will be approximately \$970 a week in 2016. This 40th percentile wage series has been specially constructed by the Bureau of Labor Statistics for the purposes of this rule, based on data from the Current Population Survey.²

In order to update our cost estimates, we first explore the series that BLS constructs to set the new threshold. We then present our own forecasts of what the overtime threshold will be after two and five years (i.e. in 2018 and 2021) if it’s set to \$970 in 2016 and indexed either to CPI or to the 40th percentile wage series. Following this, we present our new cost impacts for retail and restaurant workers under the new threshold. Finally, we conclude with some observations about using the new BLS series to set and adjust the overtime threshold.

¹ See <http://www.dol.gov/whd/overtime/NPRM2015>.

² See http://www.bls.gov/cps/research_series_earnings_nonhourly_workers.htm.



I. Exploring the BLS’s 40th percentile wage series

As part of this work, Oxford attempted to verify the BLS’s calculations of 40th percentile wages for full-time non-hourly workers using CPS microdata, and to extend their series beyond the time period BLS reports, 2013 through the first quarter of 2015. Ultimately, Oxford was not able to exactly reproduce BLS’s numbers,³ although we have arrived at close results, which are presented in table 1 below.⁴

	2013	2014	2014Q4	2015Q1
BLS value	\$921	\$933	\$942	\$951
Oxford best match 40th percentile wage	\$923	\$941	\$949	\$961

Table 1. BLS 40th percentile wage figures and Oxford’s best match to the BLS procedure, constructed using CPS microdata.

The limited number of data points BLS provides makes it difficult to forecast the series with any reliability. Between 2013 and 2014, the series grew by 1.3%; between the fourth quarter of 2014 and the first quarter of 2015, the series grew at an annualized rate of 3.9%. If the series continued to grow at 1.3% from 2014, it would be \$957 in 2016; if it continued to grow at a 3.9% annualized rate from 2015Q1, it would have an annual average of \$1,002 in 2016.

These results raise concerns about the volatility of the measure DOL has selected to base this rule on. Using Oxford’s best match series, we can construct a monthly series, which is presented in figure 1 below, that better illustrates this volatility.

³ Several technical points deserve mention: BLS says the series is restricted to those who “usually work 35 hours or more per week at their sole or principle job and who are not paid by the hour,” but among those who have more than one job and who report that their usual hours vary at their main job, the CPS only records whether the worker works 35 hours a week total, not 35 hours at their main job. Additionally, two different variables in the CPS can reasonably be used to identify hourly workers: peernhry and peernrt. Finally, BLS has not specified whether its quarterly and annual average series are unweighted averages of monthly values, or percentiles of multi-month samples. Trying several different permutations, Oxford has not been able to exactly reproduce the BLS figures using CPS Public Use Microdata.

⁴ The results presented here are unweighted averages of monthly results, using the restriction that peernrt = 2 to screen for nonhourly workers, and pehrusl ≥ 35 OR (pehrusl = -4 AND pehrftpt = 1) to screen for full-time workers. Responses are weighted by pworwgt, and the small number of respondents under age 16 with wage data are excluded.

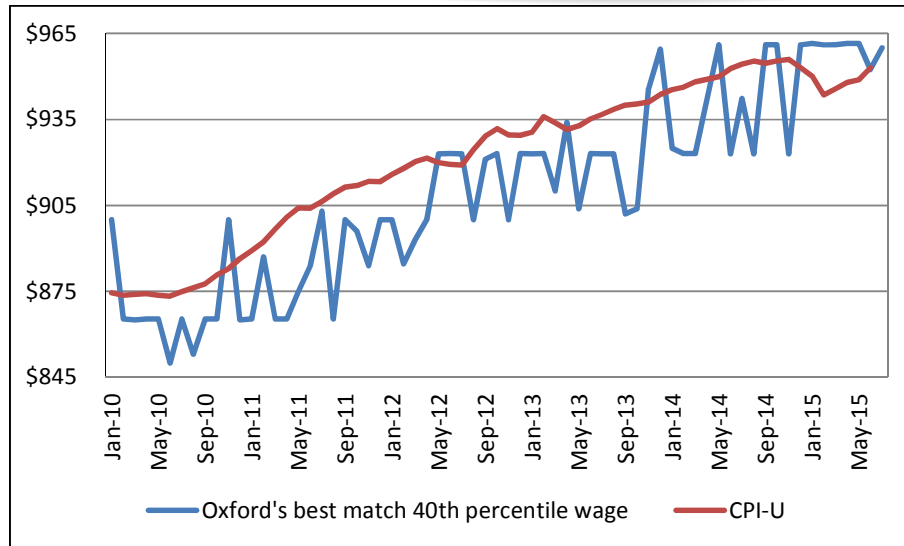


Figure 1. Oxford's monthly series of 40th percentile wage against CPI. Note that CPI is scaled to have the same zero as the other series.

Notwithstanding these concerns about volatility, the 40th percentile wage series, overall, has increased at a rate very similar to CPI-U inflation over the 2010-2014 period. Considering annual averages, CPI increased at a 2.1% annual rate from 2010 to 2014, while Oxford's best match 40th percentile series increased at a 2.0% annual rate.



II. Forecasting the overtime threshold

Oxford is a global leader in macroeconomic forecasting,⁵ and routinely forecasts CPI for the United States. According to our most recent forecast, if the overtime threshold were set at \$970 in 2016 and indexed to CPI-U inflation, it would be **\$1,013 in 2018** and **\$1,081 in 2021**.

Given the limited data available from the BLS on their new series, and the fact that it cannot be replicated exactly, it is difficult to forecast precisely what the overtime threshold would be if it were indexed to 40th percentile full-time non-hourly wages from the CPS. However, the results presented in figure 1 indicate that, over the past four years, this series has closely followed CPI. Assuming that this trend were to continue over the short to medium run (i.e. over the five-year timescale being considered), we would expect the overtime threshold indexed to a 40th percentile wage series to be quite similar to what it would be if indexed to CPI.

Over a longer time scale, economic theory would suggest that a wage-based index would grow faster than a price-based index like CPI. Figure 2 plots an annual version of the Oxford best match 40th percentile wage series from 2000-2014, along with annual CPI. Over this time period, CPI grew at a 2.3% annual rate, while the 40th percentile wage series grew at a 2.5% annual rate. Notably, changes in (the rate of growth of) the 40th percentile series seem to lag those in CPI.

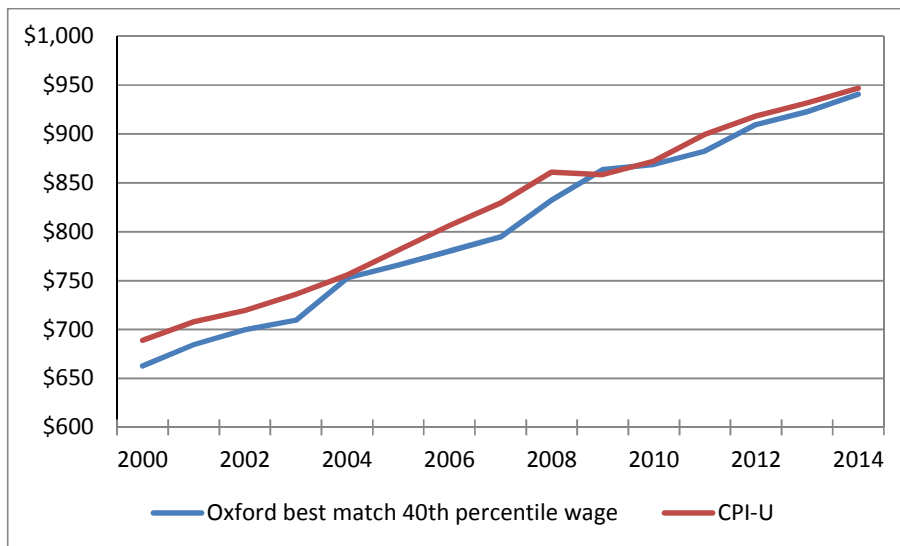


Figure 2. Annualized series over a longer time scale. CPI is scaled to have the same zero as the other series.

If the 40th percentile wage series were to grow as much faster than CPI as it did over the 2000-2014 period, and it were used to index an overtime threshold set to \$970 in 2016, then this threshold would be **\$1,017 in 2018**, and **\$1,093 in 2021**.

⁵ See <http://www.oxfordeconomics.com/macro-service/overview>.



III. Updated impacts and costs

This section follows the same methodology as the “Rethinking Overtime” report, and updates the results presented there based on the proposed new rule from DOL and newly available 2014 data. As much as possible in the following updated findings, Oxford Economics adopts the same language as in the original report for comparability. For reference, please consult the original report and appendices.

“Rethinking Overtime” used 2013 OES data to estimate that 3,324,400 of 25,431,500 retail and restaurant workers (13.1%) were exempt from Fair Labor Standards Act overtime rules under the Executive, Administrative and Professional exemption. Using 2014 OES data and the same methodology, an estimated 3,417,000 of 26,068,900 retail and restaurant workers (still 13.1%) were EAP exempt in 2014. We use this adjusted baseline for our 2016 calculations below.⁶

A. Number of affected workers

If the overtime threshold were set to \$970 in 2016, we estimate that approximately 2,189,600 exempt retail and restaurant workers would be affected, roughly 64.1% of the total exempt workers in the industry (3,417,000).

B. Passive costs

Under the passive model, it is assumed that businesses do not change behavior in response to higher costs, and so the cost to businesses of the new rules would be enormous. If the overtime threshold were set to \$970 in 2016, the passive cost would be \$8.40 billion.

C. More realistic response

If the threshold had been set to \$970 in 2016, approximately 2,189,600 workers would be affected, of whom 798,900 work more than 40 hours per week.

- An estimated 104,400 workers who are closest to this new threshold would likely see an increase in their base salaries by a total of nearly \$159 million, over \$1,500 per worker. This group, however, would also suffer an equivalent decrease in their benefits and bonuses. (Measure 1)
- About 463,000 workers would be converted to hourly non-exempt status from exempt salaried status and become eligible for approximately \$5.36 billion in overtime earnings, about \$11,600 per worker. However this group would also see their hourly rates decreased by an equal amount, leaving their total annual earnings unchanged. (Measure 2)
- Approximately 231,500 workers would be converted from exempt salary to non-exempt hourly and have their hours reduced to 38 hours per week. This change would cost these workers about \$2.32 billion in earnings, but would cause employers to hire an estimated 117,100 part-time workers to fill their labor needs.

⁶ Specifically, since our data are from 2014, we use the DOL’s 40th percentile wage value of \$933 in 2014 as a proxy for imposing a \$970 overtime threshold in 2016. This allows us to calculate the number of affected workers, as well as cost estimates for 2014. The cost estimates are then scaled from 2014 to 2016 dollars using Oxford’s current forecast for GDP deflator — an average of 1.8% annual inflation over the two years.



D. Additional transition costs to employers

The original report also described various transition costs, which it quantified. Using the same methods, we estimate that these expenses would equal an additional \$745 million in employer costs if the threshold were set to \$970 in 2016.



IV. Concluding remarks on using the BLS 40th percentile wage series to set and update the overtime threshold

Given the results presented here, we have several observations and comments about using the BLS research series on 40th percentile wages of full-time non-salary workers as a basis to set and update the overtime exemption threshold:

- BLS's current description of methodology does not allow their numbers to be reproduced, and the validity of the calculations checked. This reflects that some fairly arbitrary choices have been made in constructing the series, and sensitivity checks should be run on these arbitrary choices.
- Our results suggest that the series as currently defined can be quite volatile, changing by as much as \$42, or almost 5%, from one month to the next.
- The meaning of (a worker identifying as) being non-hourly in the CPS survey is unclear. Workers are asked, irrespective of how it's easiest to report their pay, whether or not they "are paid at an hourly rate." It is not obvious how a non-exempt worker generally paid a fixed salary when working under 40 hours per week, but eligible for overtime when exceeding 40 hours, should or would respond to this question. It is thus uncertain whether the series accurately reflects what DOL is attempting to measure.
- Importantly, the change in overtime rules itself is likely to change how survey respondents answer the salary/non-salary question, presumably by causing more (relatively lower-wage) workers to report that they do have an hourly rate of pay, and thus driving up the wage distribution for salaried workers. For example, the series presented in figure 2 increases by 6.1% in 2004, when the overtime threshold was last raised, which was the highest rate of increase over the 2000-2014 period. This presents the possibility of a vicious cycle in which the regulation influences the very metric by which it's set.
- It's generally unclear what other economic factors are influencing this series. For example, the second-highest one-year change in the series over the 2000-2014 period was in 2008, when it increased by 4.7%. This may reflect higher salaries that year; however it may also have been influenced by job losses that year falling disproportionately at the lower end of the distribution of salaried workers. It seems questionable that overtime threshold to be increased in such circumstances.
- Using CPS data in this way potentially creates an incentive for survey respondents to respond strategically, potentially undermining the reliability of CPS data.