

# POLICY *focus*

RECIPES FOR RATIONAL GOVERNMENT

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## Overtime Pay

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### Introduction

The current U.S. labor market is near full employment, and the economy boasts over 7 million unfilled jobs. Competition for workers is driving wages higher. Families at every income level also enjoy bigger paychecks thanks to the recent federal tax cuts.

Some policymakers desire to increase take-home pay further and propose expanding overtime pay to more workers. However, not all workers desire more pay; increasingly, American workers want greater job flexibility and will make the tradeoff in pay for flexible arrangements.

In 2018, the Trump Administration proposed updating the threshold at which salaried workers become eligible to receive overtime from \$23,660 to \$35,308 annually. This is a more modest increase than the \$47,000-per-year salary threshold proposed by the Obama Administration in 2015, but it would still expand overtime pay to 1.3 million U.S. workers and transfer over \$400 million each year from employers to workers.

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Advocates believe expanding overtime will fairly compensate salaried workers who clock long hours without increased wages, spur hiring, and increase hours for part-time workers. However, as with other regulations that raise labor, compliance, and litigation costs, employers will likely respond in ways that ultimately reduce pay and benefits and phase out the flexible work arrangements that workers value.

Workers want to negotiate the salaries and schedules that meet their needs. Policymakers should be mindful that raising the overtime threshold could reduce the flexibility that workers demand, and should consider other avenues to boost wages for hard work.

## Why We Care

We all want workers to be compensated fairly. However, it's important to understand how government regulations of compensation practices can backfire on workers. Increasing the number of workers covered by overtime pay rules could lead to:

- **Reduced pay** as employers lower hourly pay rates to account for overtime. One **study** finds that employers covered as much as 80 percent of overtime costs by lowering wages.
- **Fewer benefits.** Workers who are reclassified as non-exempt from overtime pay may lose other benefits such as health, dental, and vision coverage; life insurance; and disability benefits.
- **Fewer hours and greater stress.** As employers try to limit overtime hours, workers could be forced to complete the same workload in less time.
- **Less flexible work arrangements.** If employers are required to track and pay overtime for everything employees do outside of the office, such as responding to emails and conducting phone calls, they will likely end telework and remote work options.
- **Increased litigation** by employees who are not paid overtime for activities done while working remotely.

Instead of expanding the pool of workers subject to government red tape, policymakers should update labor laws to meet an evolving workplace. Today's workforce wants greater work-life balance and more flexibility.

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## Overtime Overview

Under the 80-year-old Fair Labor Standards Act (FLSA), hourly workers who log over 40 hours each week must receive overtime pay at a rate of at least one and a half times their regular pay. In 2017, there were **80.4 million** hourly workers age 16 and older in the United States, and women comprised half them. The FLSA exempts many employees from overtime though, such as executives, managers, professionals, and sales people.

Salaried employees, who earn below a salary threshold of \$23,660 per year (or \$455 per week), or whose work duties do not primarily involve executive, administrative or professional duties, also qualify for overtime pay. The current threshold has been in place since 2004 when it was increased from \$8,060.

During the Barack Obama administration, the Department of Labor (DOL) sought to double the threshold to \$47,476 per year (\$913 per week) to reflect inflation. This would have expanded overtime coverage to an additional 4.6 million workers and provided automatic threshold increases in the future.



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In August 2017, following a temporary **injunction** from the year prior, a federal judge permanently **blocked** the proposed Obama rule from taking effect because the high salary level might sweep up management workers who should be exempt. This left it to the next administration to determine any changes to overtime pay.

In 2018, the DOL under President Donald Trump **proposed** increasing the salary threshold to \$35,308 per year (\$679 per week). Although by less than the Obama proposal, the Trump rule would significantly expand eligibility for overtime pay—to an additional **1.3 million** workers.

## The Benefits of Overtime Expansion

Raising the salary threshold for overtime to \$35,308 would increase the earnings of over one million workers. The new rule would transfer **\$430 million** from employers to workers over the next decade. Additional workers could also benefit from employers increasing their salaries above the new threshold to avoid paying overtime costs.

Left-leaning groups support overtime changes because they claim employers often intentionally “misclassify” salaried workers as exempt from overtime pay. They view these benefits as important to combat income inequality, wealth inequality, and stagnant wages for workers who clock long hours without additional pay.

Other advocates believe that these changes will spur hiring and increase hours for part-time employees. The Retail Federation **estimates** that over 117,000 jobs would have been created by the Obama overtime rule. Of course, if employers responded to the new rules by hiring more workers, this would reduce the effect of higher take-home pay for existing workers as their overtime work opportunities would simply be re-bundled into new jobs.

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## How Overtime Changes Hamper Workers

The Department of Labor estimates that expanding overtime to over one million workers will lead to approximately **\$120.5 million** per year in direct employer costs over the first ten years.

Economic research tells us that employers will respond to the increased costs from the expanded overtime rules in ways that overall harm workers, like reducing earnings and hours worked. There are two economic models that explain how employers view compensation in light of mandatory overtime regulations: labor-demand or employment-contract models.

Under the labor-demand model, any hours above 40 hours each week are considered more expensive to employers. Overtime changes mean workers in labor-demand arrangements will get more pay unless their employers implement labor-saving solutions such as capital investments in automation, leaving them with fewer hours or no job at all.

With the employment-contract model, employers and employees negotiate a total number of hours and total pay. Employers factor overtime pay into total earnings and will adjust pay rates

to meet the negotiated total pay. Workers in employment-contract models maintain their salaries, but at lower pay rates.

Here are ways that workers may suffer under expanded overtime changes:

- **Reclassification**—To keep costs in check, employers may simply reclassify newly non-exempt employees as exempt from overtime pay. This is likely for employees who do not work much beyond 40 hours per week.
- **Lower pay**—Employers generally know the value workers provide to the company. They may set the hourly rate for newly non-exempt workers at a level that results in the same number of hours worked and the same total pay even including overtime. While the workers' overall compensation remains the same, the lower base pay may weigh them down in pay negotiations for future jobs. One **study** finds that employers covered as much as 80 percent of overtime costs by lowering wages.
- **Fewer benefits**—Some employers use exempt/non-exempt classifications to determine which employees earn additional benefits. Workers who are reclassified as non-exempt from overtime, may then lose **fringe benefits** that they previously enjoyed as exempt workers such as health, dental and vision coverage, paid time off, and life and disability benefits.
- **Fewer hours**—To limit the amount of overtime reclassified employees may incur, employers will more closely monitor their hours and cap their time at 40 hours. Those employees may be forced to complete the same workload, but in less time. Because of this, an estimated **11 percent** of the 2.2 million retail and restaurant workers would have had their hours reduced because of the Obama overtime rule, resulting in a loss of \$2.3 billion to managers and supervisors.
- **More Part-time Jobs**—Employers may opt to hire more part-time workers to fill their business needs rather than full-time employees (because full-time workers are more likely to incur overtime costs).
- **Automation**—In the long-term, employers may forgo new hiring and substitute non-exempt workers with labor-saving capital investments such as automation.
- **Loss of responsibilities**—Employers may reassign tasks from newly reclassified workers to those who remain exempt from overtime. That could be demoralizing if you have worked hard to gain skills and experience to do your job.
- **Less flexibility**—Expanded overtime rules would restrict or eliminate flexible work arrangements for many workers. An estimated **3.9 million** U.S. employees (2.9 percent of the workforce) work remotely at least half of the time. Many others telecommute on an ad hoc basis or work non-traditional hours. These arrangements allow them to take time off as needed or to structure their days around other priorities such as taking children to the doctor, as long as they get their job done. Under the new rules, employers would have to track when employees respond to emails, conduct phone calls, or do other work-related tasks and pay them overtime. Rather than do all this tracking, employers are likely to respond by limiting flexible work opportunities.

**Ways workers may suffer under expanded overtime changes:**

**Reclassification**  
**Lower Pay**  
**Fewer Benefits**  
**Fewer Hours**  
**More Part-time Jobs**  
**Automation**  
**Loss of Responsibilities**  
**Less Flexibility**

Employers also face compliance costs and litigation costs. Trial lawyers have seen a 237 percent **increase** in labor lawsuits over the past decade against employers who failed to compensate overtime-eligible workers for work done while away from the office among other issues. The Trump Administration believes that its overtime proposal would prevent over **200** FLSA lawsuits each year, saving an annual total of \$138.2 million in litigation costs. However, this may underestimate the real costs, especially in industries where virtual offices and telework thrive. The tech start-up industry alone was **estimated** to face between \$317 million and \$4.5 billion in overtime legal fees if the Obama proposal had gone into effect.

## A Case for Greater Flexibility

Rather than focus on changing overtime regulations to make the workplace less flexible, policymakers should consider ways to facilitate innovative new work arrangements that are popular with workers.

Technology is rapidly changing the way we work. The traditional model of checking into a physical office each day and clocking 8 hours at a desk has quickly been replaced by various types of work arrangements. Yet, our labor laws are based upon this outdated model. From 2005 to 2015, the number of U.S. workers who worked remotely at least 50 percent of the time grew **115 percent**.

Flexible work arrangements are on the rise because employees increasingly value work-life balance. In one survey, **36 percent** of workers said they would choose to work from home over taking a pay raise. According to **Gallup**, over half of U.S. employees say they would change jobs for one that offered them flextime, and over a third would take a different job that offered the ability to work remotely at least part of the time.

Analysis of thousands of surveys, reports and articles **finds** that telecommuting increases performance, productivity, and job and life satisfaction. Employees are less stressed, experience improved health and well-being, and are less likely to quit their jobs when flex work is available. Employers benefit from reduced unplanned absenteeism and turnover. They also gain access to a broader pool of workers who live far away.

Workers also benefit from sufficient time off from work. One way to reform overtime regulations and offer workers greater choice would be to allow workers to opt in to receive paid time off for overtime rather than extra pay.

Federal policies that increase workplace flexibility and make it easier for employers to offer alternatives to the 9-to-5 arrangement will move with the workforce rather than lag behind it. Our leaders should explore other ways to encourage workplace flexibility so that workers can negotiate with their employers how to maximize pay or flexibility.

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# What You Can Do

## Get Informed

Learn more about how to help workers maximize pay and flexibility. Visit:

- [Society of Human Resource Management](#)
- [Heritage Foundation](#)
- [Mercatus Center](#)

## Talk to Your Friends

Help your friends and family understand these important issues. Tell them about what's going on and encourage them to join you in getting involved.

## Become a Leader in the Community

Get a group together each month to talk about a political/policy issue (it will be fun!). Write a letter to the editor. Show up at local government meetings and make your opinions known. Go to rallies. Better yet, organize rallies! A few motivated people can change the world.

## Remain Engaged Politically

Too many good citizens see election time as the only time they need to pay attention to politics. We need everyone to pay attention and hold elected officials accountable. Let your Representatives know your opinions. After all, they are supposed to work for you!

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## ABOUT INDEPENDENT WOMEN'S FORUM

Independent Women's Forum (IWF) is dedicated to building support for free markets, limited government, and individual responsibility.

IWF, a non-partisan, 501(c)(3) research and educational institution, seeks to combat the too-common presumption that women want and benefit from big government, and build awareness of the ways that women are better served by greater economic freedom. By aggressively seeking earned media, providing easy-to-read, timely publications and commentary, and reaching out to the public, we seek to cultivate support for these important principles and encourage women to join us in working to return the country to limited, Constitutional government.

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