

**Final Small Business
Economic Impact Statement**

**Rules addressing Minimum Wage Act exemptions for
executive, administrative, professional, computer
professional, and outside salespersons - Chapter 296-128
WAC, Minimum wages**

Date: December 10, 2019

1. Describe the adopted rule, including: a brief history of the issue; an explanation of why the adopted rule is needed; and a brief description of the amendments in this proposal that would impose new or additional costs on affected businesses, including small businesses.

Washington’s Minimum Wage Act (MWA) is designed to set minimum standards for wages in order to protect employees from substandard wages, provide for the “health, safety and welfare” of Washington citizens, and to encourage Washington employment opportunities.¹ It has been repeatedly amended by both legislative action and citizen initiative to “establish and enforce modern fair labor standards,” including updates to establish fair minimum wages, establishing the forty-hour workweek and the right to overtime pay, and the right to paid sick leave to protect public health and allow workers to care for the health of themselves and their families.² The MWA was patterned after the federal Fair Standards Act (FLSA), 29 U.S.C. § 201 et seq., which was similarly enacted by Congress in 1938 in order to guarantee basic pay and overtime wage standards for employees engaged in interstate commerce. Both Acts are intended to protect employees, and where federal and state wage standards differ, the standard most beneficial to the employee applies.³

The overtime protections under the MWA and FLSA serve two purposes: to reduce overwork and its detrimental effect on the health and well-being of workers, and to spread employment by incentivizing employers to hire more employees rather than requiring existing employees to work longer hours.⁴ As Congress did in the FLSA, Washington’s Legislature included an exemption from the MWA for persons employed in a “bona fide executive, administrative or professional capacity.”⁵ The exemptions for executive, administrative, and professional (EAP) workers are premised on the belief that these kinds of workers, often referred to as “white collar” workers, typically earn salaries well above the minimum wage and enjoy other privileges, including above-average fringe benefits, greater job security, and better opportunities for advancement, that set them apart from workers entitled to the protections of the MWA.⁶ These workers are expected to have sufficient economic and bargaining power to protect themselves from insufficient compensation for hours worked.

L&I promulgated its rules on the executive, administrative, and professional (EAP) exemptions in 1976, and until now, has not substantially updated the rules since that time. The 1976 rules required most workers to meet a duties test and be paid a minimum salary between \$155 and \$250 per week to qualify for these exemptions, which equates to a minimum yearly salary of \$13,000. Following the U.S. Department of Labor’s (USDOL) 2004 rules changes addressing EAP exemptions, which increased the minimum salary to \$455 per week, L&I did not update its rules. Employers are required to comply with both state and federal overtime regulations, but where differences exist between Washington State and the 2004 federal overtime regulations, employers are required to follow the regulation that is most favorable to the worker.

Following the adoption of the 2004 USDOL rules, L&I updated its policies for EAP exemptions to indicate where the federal rules were more favorable. However, continued increases in the state’s minimum wage not only exceeded the state’s salary level of \$250 per week, but the current federal \$455 per week salary threshold set in 2004 as well. On September 24, 2019, the USDOL issued new, final rules, which have an effective date of January 1, 2020.⁷ The salary

¹ RCW 49.46.005, *Bostain v. Food Express, Inc.*, 159 Wn.2d 700, 711, 153 P.3d 846 (2007).

² RCW 49.46.005

³ RCW 49.46.120; 29 U.S.C. § 218(a); *see, e.g., Pac. Merch. Shipping Ass’n v. Aubry*, 918 F.2d 1409, 1425 (9th Cir. 1990), cert. denied, 504 U.S. 979 (1992).

⁴ *See, e.g.*, 84 Fed. Reg. at 10,916; RCW 49.46.005

⁵ RCW 49.46.010(5)(c). The MWA included this language from the time of its adoption in 1959.

⁶ 81 FR 32,392; 81 FR 32,394-95, citing the Report of the Minimum Wage Study Commission, Volume IV, pp. 236 and 240 (June 1981).

⁷ 84 FR 51,230 (Sept. 27, 2019).

level provided in the final rules issued by the USDOL will be \$684 per week (\$35,568 annually).⁸ While the department has strived for consistency with the federal rules in many areas, the department determined based on stakeholder feedback and cost-benefit analysis that some differences from the federal standards were necessary to uphold important protections for employees in Washington State.

The department engaged in this rulemaking to ensure that the regulations in Washington State effectively distinguish between employees to whom the Legislature intended to provide MWA protections and bona fide EAP workers who it intended to exempt. L&I recognizes that when the definitions become outdated, the protections intended by the MWA erode, and employees who the Washington State Legislature intended to protect do not receive the protections of the MWA or the higher salaries, above-average benefits, and greater job security and advancement opportunities expected for *bona fide* EAP and outside sales employees, which justify the exemption from the MWA's protections.

Additionally, employers do not have an efficient and reliable means of identifying which workers are, or are not, entitled to these protections. With these adopted rules, L&I intends to restore protections so that employees who should receive minimum wage, overtime, tips and service charges, paid sick leave, and protection from retaliation will do so, and to implement a mechanism to ensure that the test for exemption remains up-to-date so future workers will not be denied the protections that the Legislature intended to afford them.

Amendments to the duties tests for executives (WAC 296-128-510), administrative employees (WAC 296-128-520), professional employees (WAC 296-128-530), computer professionals (WAC 296-128-535), and outside salespersons (WAC 296-128-540) will impose additional administrative costs for implementation because employers will need to learn and adapt to the new rules and will have costs for reexamining and adjusting exemption statuses. In addition, employers will need to schedule and monitor additional employee work hours.

Amendments to the salary thresholds in WAC 296-128-545, which apply to executives, administrative employees, and professionals, and in WAC 296-128-535 for hourly computer professionals, will also have costs associated with learning and adapting to the new rules, reexamining and adjusting exemption statuses (particularly during the phase-in periods for the salary thresholds), and costs associated with scheduling and monitoring employees' work hours. The changes resulting from the updated salary thresholds will also likely have transfer payments from employers to workers as employers choose to pay overtime and other costs associated with compliance with the Minimum Wage Act, or to pay a higher salary so the employee may remain exempt. These costs and transfer payments will affect business of all sizes who employ EAP workers.

Some small businesses may face higher costs because of this rulemaking, but there is no data indicating the magnitude of this cost. Most, if not all, small businesses, like larger businesses, employ a mix of exempt and Minimum Wage Act-eligible workers. As such, employers already have policies and systems in place for scheduling workers, monitoring overtime hours worked and providing the corresponding overtime premium pay, and providing paid sick leave. L&I recognizes that the rule amendments will result in the reclassification of some workers of small businesses from exempt to nonexempt, and expects that employers will modify their existing policies and systems to accommodate this change.

2. Identify which businesses are required to comply with the adopted rule using the North American Industry Classification System (NAICS).

This rulemaking applies to all businesses in Washington State that employ workers that are classified as exempt from the protections of the Minimum Wage Act. This includes any business that employs an executive, administrative,

⁸ *Id.*

professional, computer professional, or outside sales employee. Table 1 below shows the total number of establishments and employment by each industry.

Table 1: Establishments and employment by industry (excluding nonemployers)

2-digit NAICS	Industry sectors	Total number of establishments	Total employment
	Total	251,695	3,568,014
11	Agriculture, forestry, fishing and hunting	7,678	122,097
21	Mining	178	2,486
22	Utilities	612	4,844
23	Construction	25,920	200,897
31	Manufacturing	7,971	289,553
42	Wholesale trade	14,702	137,035
44	Retail trade	21,278	389,298
48	Transportation and warehousing	5,833	115,148
51	Information	4,598	134,870
52	Finance and insurance	9,200	99,019
53	Real estate and rental and leasing	8,640	55,764
54	Professional and technical services	26,564	213,504
55	Management of companies and enterprises	741	45,650
56	Administrative and waste services	12,945	177,580
61	Educational services	3,979	344,931
62	Healthcare and social assistance	57,301	461,412
71	Arts, entertainment and recreation	3,214	71,768
72	Accommodation and food services	17,700	295,556
81	Other services, except public administration	20,438	131,729
99	Public administration	2,204	274,874

3. Identify and analyze the probable costs to comply with the adopted rule.

Costs to be estimated (administrative):

- Costs of learning and adapting to the new rules.
- Costs of reexamining and adjusting exemption statuses.
- Costs of scheduling and monitoring employee’s work hours.

As detailed in Chapter 2 of L&I’s cost-benefit analysis, the following is the summary of the annualized costs of the rules amendments.

Table 2: Summary of annualized total administrative costs.

Costs of learning and adapting to the new rules	\$1.87 million
Costs of reexamining and adjusting the exemption status	\$1.95 million
Costs of scheduling and monitoring employees’ work hours	\$9.83 million
Annualized total	\$13.65 million

The department also analyzed the costs associated with transfer payments. The increases in salary and hourly (for computer professionals) threshold levels by these rules may result in higher payroll costs from either the overtime premiums paid to the newly eligible workers, the increased salaries for workers to remain in exemption status, or the hire of additional employees to spread the workload. For the purposes of the SBEIS, the department is considering the cost of payroll as a cost to the employer.

Employers may also incur payroll costs if some of their affected workers are currently paid less than the state minimum wage. In addition, employers may incur payroll costs transferred to the newly nonexempt employees and their replacement workers to cover the hours their newly eligible employees take as paid sick leave. All of these payroll impacts essentially represent the redistributed income from employers to workers and, unlike administrative costs, the costs to employers are equally-valued benefits to workers, so they cancel out. In addition, they do not create new social values. Therefore, they are considered transfer payments and are analyzed separately from administrative costs.

As detailed in Chapter 4 of L&I’s cost-benefit analysis, the following is the summary of the transfer payments associated with the rule amendments in 2020

Table 3: Summary of total transfer payments (2020).

Due to overtime coverage	\$20.21 million
Due to minimum wage coverage	\$10.78 million
Due to paid sick leave coverage	\$5.31 million
Total	\$36.30 million

For more information, please see the cost-benefit analysis, which includes our cost-impact analysis for the adopted rules.

The cost-benefit analysis is available on the L&I website, or it may be obtained by:

Email: EAPRules@Lni.wa.gov
Phone: (360) 902-4597

4. Determine whether the adopted rule may impose a disproportionate impact on small businesses compared to the 10 percent of businesses that are the largest businesses required to comply with the adopted rule.

For informational purposes, the department computed the minor cost threshold defined as 1 percent of average annual payroll per business for each sector based on the Quarterly Census of Employment and Wages. The department also calculated per-employer cost for all employers across sectors and for each sector individually, based on the assumption that the sectoral cost is proportional to the share of affected workers by each sector. The average per employer cost in 2020 is smaller than the minor cost threshold for employers in any affected sector (see table in Appendix A). However, we cannot confirm this assumption, nor do we have data to determine whether or not this average cost is larger than the minor cost at a more detailed level (for example, 4-digit NAICS level). Therefore, the department assumes these rules will impose more than minor costs.

In addition, there is insufficient data to determine the size of the cost impact between large and small employers to calculate disproportionate impacts. As required by RCW 19.85.030, in the absence of this data, the department identified cost-mitigation measures, where legal and feasible, as described below.

5. If the adopted rule is likely to impose a disproportionate impact on small businesses, identify the steps taken to reduce the costs of the rule on small businesses.

L&I reviewed the list of methods for reducing the impact on small businesses under RCW 19.85.030, and is taking the following steps to reduce the costs of the rules on small businesses:

- Delayed implementation/phase-in of the salary thresholds.
 - The proposed rules contained a delayed-implementation/phase-in of the salary thresholds based on employer-size. In response to feedback from stakeholders including small businesses, the department extended the phase-in schedule to provide employers additional time to adjust to and comply with the updated salary thresholds for their salaried, exempt employees. For those EAP workers subject to salary threshold requirements, the adopted rules extended the phase-in implementation from six years to eight years, with the most gradual phase-in applying to small businesses. The salary threshold will reach a final threshold of 2.5 times the state minimum wage for a 40-hour workweek for all employers at the end of that period.
 - Beginning July 1, 2020, all businesses are subject to an initial change to 1.25 times the state minimum wage for a 40-hour workweek. Following the initial increase to 1.25 times the state minimum wage in 2020:
 - Businesses with more than 50 employees will increase to 1.75 times the state minimum wage for a 40-hour workweek beginning January 1, 2021, and must implement the final statewide threshold of 2.5 times the state minimum wage for a 40-hour workweek on January 1, 2027.
 - Businesses with one to 50 employees will increase to 1.5 times the state minimum wage for a 40-hour workweek beginning January 1, 2021, and must implement the final statewide threshold of 2.5 times the state minimum wage for a 40-hour workweek on January 1, 2028.

- For hourly computer professionals, the adopted rules phase-in implementation over three years, with a more gradual phase-in for small businesses.
- More closely aligning with the federal duties tests for all executive, administrative, professional, computer professional, and outside sales employees. The department determined that moving to a standard test that more closely aligns with the tests employers are already required to comply with under federal law reduces regulatory requirements and compliance costs for employers.
- Developing and implementing a robust outreach and education program to ensure that small businesses are informed about what they need to know to comply with the law.
- Considering other mitigation techniques, including those suggested by small businesses or small business advocates.

L&I has considered the other methods of reducing costs under RCW 19.85.030 and found them inapplicable or infeasible:

- These rules do not directly impose any recordkeeping or reporting requirements. Indirectly, they may affect the number of employees for whom certain recordkeeping requirements are imposed under the statute or other rules. L&I cannot reduce the requirements set by statute in the Minimum Wage Act through these rules.
- These rules do not require inspections and present no opportunity to reduce the frequency of inspections.
- These rules does not impose fine schedules for noncompliance and present no opportunity to reduce fine schedules.

6. Describe how small businesses were involved in the development of the adopted rules.

Department staff initiated the rule development process with an informational kickoff meeting in April 2018. The department held subsequent meetings to discuss scope and content of the rulemaking: two meetings to present stakeholder-requested data on state wages and economic characteristics and an additional meeting to discuss draft concepts for the rule updates.

Stakeholders were able to participate in person, by phone, and through the Employment Standards Rulemaking & Policy Development engagement website, which the department provided to enhance public participation and transparency in the rulemaking process. The engagement site provides stakeholders with a single location for providing feedback and reviewing feedback submitted by other stakeholders on draft proposed versions of the rules; for locating pertinent documents, such as the most updated version of the draft rule language and stakeholder meeting agendas; and for viewing a timeline that outlines the steps in the rulemaking process.

Utilizing input contributed by stakeholders during the process, the department prepared an initial pre-draft version of proposed rule language and circulated it for stakeholder feedback. The department held several listening sessions throughout the state during the month of October 2018. The well-attended sessions provided yet another opportunity for the public to discuss the draft. After reviewing the comments received on the first pre-draft rules, the department updated the language and issued a second pre-draft version of the rule language for stakeholder feedback. The department held a second round of statewide listening sessions in November. The department accepted comments on both pre-draft versions of the rules through the engagement site, by standard mail, by email, and in person at the listening sessions.

After filing the CR-102 proposed rule language on June 4, 2019, the department held seven statewide public hearings. These public hearing yielded 625 attendees, 182 of whom provided testimony. In addition to the comments provided at the public hearings, the department also received 2,266 written comments. Comments were received from individuals as

well as various representatives of business, labor, and nonprofits, and reflected both support for, and concerns about, the proposed rule updates.

Small business employers and organizations representing small businesses were involved throughout all steps in the process, and the Department considered their feedback prior to finalizing the adopted rules.

7. Identify the estimated number of jobs that will be created or lost as the result of compliance with the adopted rule.

The overtime protections under the MWA and FLSA serve two purposes: to reduce overwork and its detrimental effect on the health and well-being of workers; and to spread employment by incentivizing employers to hire more employees rather than requiring existing employees to work longer hours.⁹ It is possible that some employers may choose to eliminate all overtime for affected workers and hire additional workers or spread the work to existing employees to replace the lost hours. The potential for this adjustment is uncertain, and L&I has found no studies that estimate the potential magnitude of this effect. Because of the lack of data, L&I cannot estimate how many jobs will be created due to the adopted rules.

⁹ See, e.g., 84 Fed. Reg. at 10,916; RCW 49.46.005

Appendix A

Table X. Unit Cost Analysis: 2020

2-digit NAICS	Industry sectors	Total number of firms	Affected workers	Affected as % of total affected	Total cost (regulatory plus payroll)	Per-employer cost per year	Annual payroll per business	Minor cost threshold (1% of annual payroll)
Total	Total	225,117	40,343	100.00%	\$46,818,879	\$208	\$1,050,029	\$10,500
11	Agriculture, forestry, fishing and hunting	7,208	71	0.18%	\$82,397	\$11	\$526,158	\$5,262
21	Mining	152	6	0.01%	\$6,963	\$46	\$1,350,870	\$13,509
22	Utilities	223	25	0.06%	\$29,013	\$130	\$2,288,804	\$22,888
23	Construction	25,043	729	1.81%	\$846,019	\$34	\$529,654	\$5,297
31-33	Manufacturing	7,373	2,252	5.58%	\$2,613,492	\$354	\$3,357,824	\$33,578
42	Wholesale trade	13,007	2,089	5.18%	\$2,424,327	\$186	\$900,106	\$9,001
44-45	Retail trade	14,561	5,282	13.09%	\$6,129,869	\$421	\$1,579,591	\$15,796
48-49	Transportation and warehousing	4,575	485	1.20%	\$562,852	\$123	\$1,413,152	\$14,132
51	Information	3,701	4,698	11.65%	\$5,452,125	\$1,473	\$6,787,740	\$67,877
52	Finance and insurance	5,733	3,112	7.71%	\$3,611,540	\$630	\$1,718,781	\$17,188
53	Real estate and rental and leasing	6,773	695	1.72%	\$806,562	\$119	\$447,129	\$4,471
54	Professional and technical services	25,057	6,486	16.08%	\$7,527,136	\$300	\$830,071	\$8,301
55	Management of companies and enterprises	632	1,058	2.62%	\$1,227,831	\$1,943	\$9,067,576	\$90,676
56	Administrative and waste services	12,010	2,121	5.26%	\$2,461,464	\$205	\$774,582	\$7,746
61	Educational services	3,230	2,231	5.53%	\$2,589,121	\$802	\$583,167	\$5,832
62	Healthcare and social assistance	50,312	3,264	8.09%	\$3,787,939	\$75	\$479,890	\$4,799
71	Arts, entertainment and recreation	2,791	1,161	2.88%	\$1,347,364	\$483	\$678,532	\$6,785
72	Accommodation and food services	14,309	524	1.30%	\$608,113	\$42	\$504,872	\$5,049
81	Other services, except public administration	18,611	1,253	3.11%	\$1,454,132	\$78	\$235,235	\$2,352
92	Public administration	2,118	2,801	6.94%	\$3,250,618	\$1,535	\$18,563,092	\$185,631