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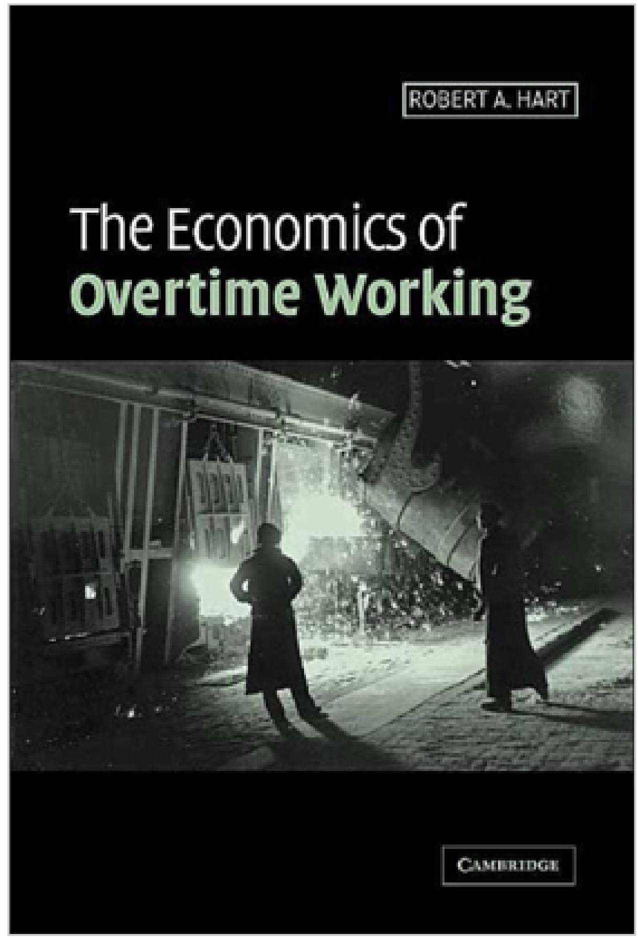
Working overtime: who really benefits?

The Economics of Overtime Working. By Robert A. Hart, New York: Cambridge University Press, 2004, 167 pp., $75.00/hardback.



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In *The Economics of Overtime Working*, Robert Hart, labor economist and professor of economics at the University of Stirling in Scotland, United Kingdom, presents comprehensive theoretic studies on overtime work and how it affects the labor market. Using comparative assessments of labor supply versus labor demand, he showcases a variety of models constructed from evidence collected in the United States, Western Europe, and Japan. The work extends far beyond a mere summary of existing research, to enliven the topic and inform the reader as well as set the stage for debate.

Choosing this book brought back not-so-fond memories of my days working on a farm. My first two jobs were picking cucumbers and cropping tobacco. Many days went beyond the standard work hours, with absolutely no overtime benefits. Sadly, these working conditions still exist.

I must say that I was intrigued by all of the research, studies, collaborations, and debates on the effects of overtime. As I dissected the book, my interest level rose further as I read how economists have viewed overtime as it occurs in a standard nine-to-five job versus how it is perceived on the farm of my younger days. According to the former, anything over 40 hours a week is defined as overtime and if one works on a holiday, one gets paid double time. But that view is by no means universal.

Overtime work is work in excess of standard contractual hours. One example of standard time is a 35-hour workweek consisting of five 7-hour weekdays. Under this standard, an individual who worked a 50-hour week would have accrued 15 hours of overtime. For the vast majority of workers, overtime hours are remunerated at a different rate of pay from standard hours. A premium of time and a half applies to most overtime workers in the United States. For a minority of workers, overtime hours are remunerated at the same rate as standard hours or even at a reduced rate.

Hart cites Brechling as the first to develop in detail the workers–hours demand model, in 1965. Brechling treated output, capital, technology, and factor prices as exogenous to the firm that seeks to minimize its costs. The firm produces output at the lowest cost combination of workers and average hours per worker. For the United States, an economy with mandatory overtime rules, this model concerns the employment effects of a rise in the overtime premium.

Over the years, many scholars have raised strong points regarding working overtime, says Hart. In 1988, Hart and Wilson investigated the issue on the basis of estimated conditional factor demand schedules. The work of DeBeaumont and Singell in 1999 showed that separating industries in the estimation of returns is a fruitful way to proceed. In 1993, Black, Chapman, and Chatterji emphasized the distinction between wage rates and earnings in their evaluation of regional earnings growth in the United Kingdom between 1974 and 1991. By 2000, Hamermesh and Trejo had found yet more support for the work-sharing effects of overtime legislation.

Different attitudes toward work and leisure—prompted by such factors as personal characteristics, family circumstances, and peer group influences—may induce individual suppliers of labor to search for the job length–wage earnings combination that optimizes their utility.

According to Hart, in the literature on the interrelationship among overtime, the demand for it, and production, overtime is treated as one of the firm's most important intensive margin responses. Changes in overtime hours bring production, labor cost, and wage effects. With respect to the last of these, overtime plays a key role in the study of the cyclical behavior of real hourly earnings.

As discussed by Leslie in 1991, changes in the amount of overtime working occur along two main channels. First, average overtime per overtime worker fluctuates. Second, the ratio of overtime to total workers also varies. Therefore, the total change in overtime working would be expected to result mainly, though not only, from changes in these two components.

Perhaps the most frequently quoted example of an attempt to control the maximum number of standard work hours and the minimum number of overtime work hours is the U.S. Fair Labor Standards Act (FLSA), which sets a standard weekly hours limit of 40 and a minimum premium of time and a half times the standard hourly rate. The daily and weekly lengths of standard hours are often fixed by collective bargaining. In fact, in many instances they are set exogenously to the firm, at national or industrial levels.

"Why do firms pay an overtime premium?" asks Hart. He gives us three reasons. First, governments may attempt to reduce the health and social costs of excessive work demands by imposing high labor costs on firms' marginal daily or weekly hours beyond acceptable norms. Second, labor unions may require high marginal rates as compensation for potential adverse effects on their members' welfare. Third, overtime premiums satisfy unanticipated increases in product demand while minimizing hiring and firing costs.

The United Kingdom, says Hart, is an economy with no imposed rules governing the timing and payment of overtime hours. Overtime agreements tend to be undertaken at the company level, with different companies offering different premium rates.

Workers express a broad range of reasons for their decision to work overtime. Hart cites a 1998 British Workplace Employee Relations Survey in which one-fifth of 26,000 employees surveyed reported that they worked overtime because they needed the money. An even larger percentage (24 percent) worked overtime because their job required them to do so. Ten percent claimed that they did not want to let their colleagues down, and 5 percent worked overtime because they like the job they do.

We know that overtime working is an important labor market phenomenon in economies with either weak or nonexistent overtime regulations. Even under the relatively strong regulations in the United States, which imposes high marginal rates of overtime pay, up to 20 percent of workers receive a premium before maximum standard workweek hours are reached. That is, they receive an overtime-like premium, based on established custom and practice, before they even begin working overtime.

Is working overtime here to stay? Undoubtedly, many firms view overtime as a useful means of dealing with unanticipated economic events, including fluctuations in product demand and in rates of absenteeism, as well as breakdowns in production or the organizational workflow. Overtime work designed to accommodate unforeseen, usually short-term events is likely to remain a permanent feature of the labor market scene.

On August 23, 2004, the Employment Standards Administration issued new overtime regulations that affect the exempt status of some workers covered by the FLSA. The change in regulations caused the exemption status of some jobs to be reclassified, thereby affecting the eligibility of those jobs for overtime pay. In response to the new regulations, the National Compensation Survey is reviewing all jobs currently being sampled to ensure that all changes in company overtime practices are properly recorded for the survey. (For details, see Secretary of Labor Thomas E. Perez, “Wages: overtime pay” (U.S. Bureau of Labor Statistics), http://www.dol.gov/dol/topic/wages/overtimepay.htm.)

So, the question remains: Who really benefits from working overtime? The employee? The employer? Both? No one? The answer, per Hart, is “It depends.” Both parties benefit when a good product is made and employees are well compensated. No one benefits if there is no demand for the product and the pay doesn’t cover travel expenses. Employees seldom benefit when working overtime takes away from family time. Everyone will benefit when well-compensated and happy employees produce a cost-effective product that is in high demand.

This book is a must-read for anyone fascinated with the policies, formulas, and demands that center around overtime. It is also a must-read for those seeking a crash course in the many facets of workers’ commitments to overtime work. I recommend this book highly.