

Beware the Pitfalls of the FLSA

As we enter 2007, employers continue to face ever-increasing legal liability for alleged violations of the Fair Labor Standards Act ("FLSA"). Every week we read about large settlements and new lawsuits alleging wage and hour violations. Just this week, IBM and Tyson Foods were hit with class actions alleging that they had failed to pay overtime. In the past two months, UPS agreed to pay \$87 million to settle an FLSA class action, IBM agreed to pay \$65 million to settle a suit alleging that it had failed to pay overtime to its technical workers (and has now been sued again by a different group of employees), and Wal-Mart agreed to pay \$33.5 million to settle claims that it had underpaid overtime. These companies are far from alone, in 2006 virtually every industry – from pharmaceutical companies, to securities firms, to banks, to restaurants, to retailers – has been hit with FLSA litigation.

This trend has not abated and is now taking a disturbing turn. Possibly since most of the "mega-companies" have already been hit, the plaintiff's bar is now turning its attention to smaller and mid-size companies, and even targeting the non-profit sector. **The message is – if you have employees – you are a potential target.**

You should not sit back and wait to be sued. There are a number of areas where we see clients typically run afoul of the FLSA, and there are steps that you can

and should take now, to ensure that your salary practices are in compliance with the law.

Pitfall # 1 – Worker Misclassification

► Do you know how to determine who is an "exempt" employee?

Misclassification of employees continues to confuse employers. Many companies still have misconceptions as to which employees are properly classified as "exempt" under the FLSA, and thus do not have to be paid overtime. Employers tend to think that all "salaried" employees, or everyone earning over a certain salary, is automatically exempt from overtime. **That is not the law.**

There are only 3 primary categories of employees that are "exempt" and thus do not have to be paid overtime – **executive**, **administrative** and **professional** employees – all terms that are defined by statute and case law. Outside of these groups, certain computer professionals, outside sales employees, and commissioned retail sales employees may also be "exempt." As a general matter, these employees are "exempt" only if their responsibilities satisfy certain legal requirements, and they have discretion in how they carry out their duties.

Also, as of 2004, employees who are paid an annual salary of over \$100,000 per year may also be exempt – again assuming they meet certain FLSA criteria.

► **Are your managers really “managing”?**

The FLSA regulations were amended in 2004 to make it clear that, in order to be exempt, “executives” must exercise discretion and have some authority to make, or “effectively recommend,” termination and hiring decisions. Are all of your exempt executives meeting this criteria?

► **Which computer or IT employees are “exempt”?**

The FLSA has just issued new guidance on the parameters of the exemption for computer professionals. If you employ technical workers, you should familiarize yourself with those requirements before deciding which of your computer professionals are exempt.

► **When are sales employees exempt?**

Many employers suffer from the misconception that all “sales employees,” or those who work on commission, are exempt. **This is not the law.** As a general matter, only outside sales employees and retail sales employees, who work on commission, are exempt, provided they meet certain specific criteria. There are also exemptions for certain types of sales or retail employees in the financial services industry, again if their duties satisfy specific criteria. “Inside” sales employees, even if they are eligible to earn commissions, are generally not exempt. If you have “exempt” sales employees, do they truly satisfy the FLSA standards for exemptions?

► **Are your exempt employees paid on a salary basis?**

The FLSA also requires that all exempt employees be paid on a “salary-basis.” Put simply, you should be paying your exempt staff a set salary each week (of at least \$455) – which should not fluctuate based on the number of

hours they work. As a general matter, exempt employees should not be ‘docked’ or have their salary reduced when they are out or absent for part of a workday. There are also limitations on an employer’s right to discipline or suspend an exempt employee without pay. Are you satisfying those criteria?

► **Have you checked your state laws?**

All states have wage/hour laws and many have exemptions and other requirements that are different from the federal FLSA. If your state’s law is stricter than the federal law, you must comply with the state law. Make sure you check the laws in every state where you employ people to confirm that you are properly classifying employees.

Pitfall # 2 – Proper Pay Practices for Non-Exempt Employees

Many employers also run into difficulty when paying their non-exempt staff. Computing overtime and keeping track of regular and overtime hours worked are two common problem areas. Mistakes here can prove costly, particularly at the hands of a practiced class action plaintiffs attorney.

Here are some basic reminders:

► **Capture and Compensate for All “Hours Worked”**

The FLSA requires that employers pay the minimum wage for all “hours worked” in a workweek and pay an overtime premium for all “hours worked” in excess of 40 hours per week. The key question, then, is what are “hours worked.”

Under the FLSA, “hours worked” includes all time spent on work that is either “suffered, required or permitted.” Thus, employers must compensate non-exempt employees for time spent correcting errors (“rework”),

waiting for work, and working at a remote location, including the employee's home.

Generally, we see clients run into trouble where employees don't punch a clock. Are you capturing all work they do, even if done before or after the "normal" "workday"? If employees work through meal breaks, do they get paid for that time? If employees work from home, are they being paid for all of that time and how do you keep records of that time?

► **Pay for All Overtime Hours**

Many of our clients have rules that require employees to secure a supervisor's authorization before working overtime. Such rules are lawful. However, if an employee works overtime that is "unauthorized" – you **must pay them** for it (you can, of course, otherwise discipline the employee). Is that your policy? Also, do all of your managers understand that this is the law?

Our Advice: Be Proactive

As proven by recently reported lawsuits and settlements, an employer's failure to comply with the FLSA can have disastrous financial consequences. These actions are a warning to all employers to get their FLSA house in order. Don't wait to be sued. Preemptively review (and correct, if necessary) your pay practices now.

Start with two simple tasks. One, review all exempt/non-exempt classifications to ensure compliance with FLSA and state law criteria. Two, review your pay practices for non-exempt employees to ensure you are calculating "hours worked" and overtime hours correctly.

If you do just that, you'll do quite a lot to avert the FLSA class action net in which so many employers have recently been caught.

For more information or advice on the area of FLSA compliance, please contact:

Barbara E. Hoey, Esq.

(212) 808-7836

bhoey@kelleydrye.com

John E. Kiley, Esq.

(212) 808-5000

jkiley@kelleydrye.com

Jean Y. Park

(212) 808-5019

jpark@kelleydrye.com