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# The Wage and Hour Mistakes That Cost Companies Millions: Best Practices for Avoiding a Class or Collective Action Lawsuit

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# The Proliferation of FLSA Collective Actions

- The FLSA permits an individual or group to file suit “on behalf of himself or themselves and other employees similarly situated.”
  - Current or former employees
- Individual can also assert state law claims as part of a “hybrid” FLSA collective and Rule 23 class action



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# The Proliferation of FLSA Collective Actions

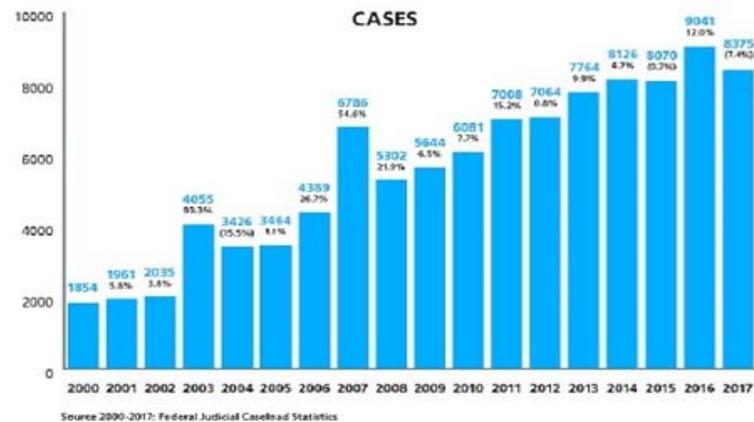
- One of the biggest employment-related liability risks for companies
- Every company, regardless of size, is a potential target
- Only way to “win” such a lawsuit is to avoid it
- Best way to avoid is to apply proactive litigation avoidance techniques



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# The Proliferation of FLSA Collective Actions

- The number of FLSA actions filed decreased slightly in 2017



- FLSA collective actions continue to significantly outpace every other type of employment class claim



# The Proliferation of FLSA Collective Actions

- The FLSA's complex and nuanced framework
- The low bar for conditional certification
- High-dollar, highly-publicized settlements



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# The FLSA's Complex and Nuanced Framework

- Difficulties inherent in applying the FLSA's Depression-era concepts to the realities of the modern day on-demand economy
- Advances in technology
- Changes in how, when, and where work is performed



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# The FLSA's Complex and Nuanced Framework

- Patchwork maze of more restrictive state laws
  - Daily overtime for hours in excess of 8 in a workday
  - Mandatory meal and rest breaks
  - Different and heightened exemption standards
  - Laws governing payment of “wages”
    - Prohibit employers from taking deductions from earned wages except in limited circumstances
    - Regulate when commissions, bonuses, and PTO are earned wages



# The FLSA's Complex and Nuanced Framework

- Pennsylvania wage and hour laws
  - Pennsylvania Minimum Wage Act – minimum wage and maximum hours
  - Pennsylvania Wage Payment and Collection Law – payment of earned wages
  - Construction Worker Misclassification Act (Act 72) – classification of workers as independent contractors in the construction industry
  - Prohibition of Excessive Overtime in Healthcare Act (Act 102) – prohibiting healthcare facilities from requiring employees to work beyond their agreed-upon, predetermined, regularly-scheduled shifts



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# The FLSA's Complex and Nuanced Framework

- Pennsylvania wage and hour laws
  - Child Labor Law – amount and type of work performed by minors
  - Equal Pay Law – requiring pay equity
  - Prevailing Wage Act – regulating the prevailing minimum wage and fringe benefits for certain construction projects



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# The Low Standard for Conditional Certification

- A plaintiff need only make a modest factual showing that she is “similarly situated” to the members of the proposed collective
- Often met by filing a complaint asserting a handful of factual allegations supported by plaintiff’s own affidavit
- Once conditionally certified, the potential exposure and cost of defense increase dramatically



# The Low Standard for Conditional Certification

- Motion to decertify must generally wait until the parties complete class-wide discovery
  - Costly and disruptive
- Because of the fact intensive nature of these cases, conditional certification can cause a risk-averse employer to seek settlement
  - Including settlement of claims on which the employer was more than likely to prevail



# High-Dollar, Highly-Publicized Settlements

- These cases can result in high-dollar (seven- or eight-figure) settlements
- Because these settlements must be approved by the court, they become highly publicized
- Results in copycat lawsuits against company or others in the industry



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# Common Collective and Class Action Claims

- Status as Employee versus Independent Contractor
- Classification as Exempt versus Non-Exempt
- Compensable Time and Off-the-Clock Work
- Calculation of the Regular Rate for Overtime Pay
- Payment of Commissions and Incentives



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# Employee *versus* Independent Contractor

- The FLSA's minimum wage and overtime provisions do not apply in the absence of an employer-employee relationship
- Question is whether the worker is economically dependent on the alleged employer
- Courts apply an economic realities
  - Six-factor test in the Third Circuit. *Martin v. Selker Bros., Inc.*, 949 F.2d 1286, 1293 (3d Cir. 1991)



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# Third Circuit's Economic Realities Test

1. the degree of the alleged employer's right to control the manner in which the work is to be performed;
2. the alleged employee's opportunity for profit or loss depending upon his managerial skill;
3. the alleged employee's investment in equipment or materials required for his task, or his employment of helpers;



# Third Circuit's Economic Realities Test

4. whether the service rendered requires a special skill;
5. the degree of permanence of the working relationship;
6. whether the service rendered is an integral part of the alleged employer's business



# Employee *versus* Independent Contractor

- In 2015, the Administrator of the Wage and Hour Division issued an Administrator's Interpretation applying the FLSA's definition of "employ" to workers classified as independent contractors
- On June 7, 2017, the DOL withdrew Administrator's Interpretation No. 2015-1
  - Still an accurate statement of the Wage and Hour Division's position



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# Liabilities of Misclassifying Employees as Independent Contractors

- Minimum wages and/or overtime pay
  - Plus liquidated damages and interest
- Employee benefits
- Unpaid employment taxes, social security, Medicare,
  - Plus penalties and interest
- State unemployment and workers' compensation taxes
  - Plus penalties



# Compliance Strategies

- Audit Independent Contractor Agreements
  - Avoid language suggesting control over when or how work is performed
  - Avoid setting specific hours when work must be performed
  - Avoid setting a specific location where the work must be performed
  - State that the independent contractor determines the manner and means of the work and that the company is interested only in the result
  - Place responsibility for taxes, insurance, business licenses, and expenses on the independent contractor
  - Do not require progress reports or status updates



# Compliance Strategies

- Audit Independent Contractor Agreements
  - Avoid setting an indefinite term or at-will termination
  - Avoid payment by the hour, day, or week
  - Require that the independent contractor provides all tools, equipment, and materials needed to perform the work
  - Allow independent contractor to subcontract or hire helpers or employees
  - Allow the independent contractor to perform services for others without requesting permission



# Compliance Strategies

- Train HR and operations managers that they must **not**:
  - Tell an independent contractor how to perform the work
  - Tell an independent contractor when to perform the work or require the independent contractor to notify them when they are not working
  - Question an independent contractor about whether they are performing work for other companies or individuals
  - Include an independent contractor in employee meetings/events
  - Invite the independent contractor to company functions
  - Retain an independent contractor work that is integral to the company business
  - Provide the independent contractor with training



# Compliance Strategies

- Train HR and operations managers that they must:
  - Handle independent contractor performance issues as breach of contract issues, not as disciplinary issues
  - Provide payment for services to the worker's business entity, not the individual worker
  - Be willing to negotiate terms and conditions with the independent contractor
  - Reiterate to the independent contractor that he or she must hire helpers or assistants to perform the work
  - Enforce provisions stating that the independent contractor will not be paid if certain requirements are not met



## Exempt *versus* Non-Exempt

- Employees who satisfy specific salary and duty requirements are exempt from FLSA's minimum wage and overtime provisions
  - 29 U.S.C. § 213(a)(1); 29 C.F.R. § 541.200(a)
- For decades, exemptions have been “narrowly construed”
- Now, exemptions must be given a “fair interpretation”
  - Plainly construed as written applying traditional principles of statutory construction



# Exempt *versus* Non-Exempt

- Salary Level Test

- For most exemptions, the minimum salary level is \$455/week
- Must be paid “free and clear” (e.g. cannot require that it be “kicked-back” or recouped from future earnings)

- Salary Basis Test

- Paid a predetermined amount for entire workweek in which employee performs any work
- The compensation cannot be reduced because of variations in the quality or quantity of the work performed



# Exempt *versus* Non-Exempt

- Employees who satisfy specific salary and duty requirements are exempt from FLSA's minimum wage and overtime provisions
  - 29 U.S.C. § 213(a)(1); 29 C.F.R. § 541.200(a).
- With a few exceptions, must meet three tests
  - Salary Level
  - Salary Basis
  - Job Duties



# Duties Test - Administrative Employee Exemption

- Primary duty is the performance of office or non-manual work directly related to the management or general business operations of the employer or the employer's customers
- Primary duty includes the exercise of discretion and independent judgment in matters of significance



# Duties Test - Administrative Employee Exemption

- Primary duty is management of the enterprise or a customarily recognized department or subdivision
- Customarily and regularly directs the work of two or more other employees
- Authority to hire or fire other employees or recommendations as to the hiring, firing, advancement, promotion or other change or status of other employees given particular weight



# Duties Test - Professional Employee Exemption

- Primary duty is the performance of work requiring knowledge of an advanced type in a field of science or learning customarily acquired by a prolonged course of specialized intellectual instruction; or
- Primary duty is the performance of work requiring invention, imagination, originality, or talent in a recognized field of artistic or creative endeavor



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# Duties Test – Outside Sales Employee Exemption

- No salary test
- Customarily and regularly engaged away from the employer's place(s) of business in performing such primary duty
- Primary duty involves:
  - Making sales; or
  - Obtaining orders or contracts for services or facilities for consideration paid by customer



# Exempt *versus* Non-Exempt

- State law often more protective
  - Fluctuating workweek method of calculation
  - Highly compensated employee exemption
  - Computer employee exemption
  - Outside sales exemption



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# Compliance Strategies

- Audit Exempt Classifications
  - Review actual job duties and ensure they qualify for the applicable exemption status
  - Ensure that job descriptions are current and accurately describe the actual job duties
- Train HR and operations managers re errors to avoid
  - Assuming employees paid a salary are exempt
  - Assuming that job descriptions accurately reflect the duties employees actually perform
  - Assuming that the FLSA and state laws are the same



# Compensable Time and Off-the-Clock Work

- Neither the FLSA nor the Department of Labor's regulations define "work" or "hours worked"
- The Supreme Court has yet to provide a precise definition
- Courts rely on the definition of "employ" which includes all work the employer "suffers or permits"
  - 29 U.S.C. § 203(e)(1)



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# Compensable Time and Off-the-Clock Work

- Meal Break Periods
  - Counted as hours worked
    - Employee performs any work
    - Less than 30 minutes
  - Not counted as hours worked
    - Employee is completely relieved of all duties
    - No phone calls, emails, emergencies
    - Auto-deduct policies
  - Confined to workstations / work premises permissible but dangerous
  - Many states require meal breaks



# Compensable Time and Off-the-Clock Work

- Preliminary/Postliminary Activities
  - Compensable if “integral and indispensable” to work duties
  - Examples
    - Employees booting up a computer and logging in
    - Drivers inspecting vehicles before start of shift
    - Technicians loading trucks before leaving to perform work
    - Filling out time sheets and picking up plans for the day’s work



# Compliance Strategies

- Audit Timekeeping Policies
  - Accurate time-keeping and record-keeping must be a priority
  - Review current employee handbooks and policies regarding accurate time-keeping and overtime
- Train HR and Operations Managers
  - Train human resources personnel and operations managers about the overtime regulations, the company policies, the company's expectations, and the consequences of non-compliance



# Calculation of the Regular Rate

- Employers must pay overtime hours at one and one-half times an employee's regular rate
  - 29 U.S.C. § 207(a)(1)
- The Department of Labor has issued regulations that include detailed examples explaining how to calculate the regular rate
  - 29 C.F.R. §§ 778.0 - 778.603



# Calculation of the Regular Rate

- Must Include in Regular Rate
  - Non-discretionary bonuses
  - Shift differential
  - Production, safety, and attendance bonuses
  - Longevity pay
  - Retention bonuses
  - Earned commissions and incentives
    - Must include in workweeks they were earned
    - Whether and when earned depends on the terms of the commission or incentive plan



# Compliance Strategies

- Ensure that all remuneration is being taken into account when calculating overtime rates for non-exempt employees
- Audit record-keeping policies to ensure retention of appropriate documents to substantiate payroll practices
- Train HR and operations managers



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# Compensation Plans and Policies

- State wage and hour laws prohibit deductions from earned wages
- Wages include commissions, bonuses, and incentive plans
- Whether and when earned depends on language of the plan
  - Ambiguous or poorly worded plans present significant risk



# Compensation Plans and Policies

- *Braun v. Wal-Mart Stores, Inc.*
  - Wal-Mart's employee handbook provided that all employees who worked more than six hours would receive a 15-minute rest break
  - Employees required to take full, uninterrupted breaks
  - Policy prohibited employee from performing work during the rest period without being paid
  - Class made up of sales associates filed suit alleging that Wal-Mart forced them to miss breaks or work through breaks in violation of Wal-Mart's own handbook policy
  - Jury verdict of \$187 million



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# Compliance Strategies

- Audit payroll practices to ensure that improper deductions are not being made
- Audit compensation and commission plans to ensure that they clearly define when wages are earned
- Review policies and handbook provisions to ensure they do not create a contractual right regarding break periods and time off
- Train HR and operations managers



# Compliance and Litigation Avoidance Strategies

- Consider a Mandatory Arbitration Program
- Conduct a Wage and Hour Audit
- Establish Formal Policies and Procedures
- Conduct Wage and Hour Training



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# Consider a Mandatory Arbitration Program

- Employers may adopt mandatory arbitration programs that include class action waivers
  - *Epic Systems Corp. v. Lewis*, 138 S. Ct. 1612 (2018)
- Employers may adopt mandatory arbitration programs that include collective action waivers
  - *Gaffers v. Kelly Services, Inc.*, 900 F.3d 293 (6th Cir. 2018)
- Employers may include class and collective action waivers in independent contractor agreements
  - *O'Connor v. Uber Tech., Inc.*, 904 F.3d 1087 (9th Cir. 2018)



# Consider a Mandatory Arbitration Program

- Pros

- Efficiency (quicker resolution and reduced litigation costs)
- Confidentiality
- Greater predictability versus a jury
- Class and collective action waivers

- Cons

- Inefficiencies caused by numerous individual arbitrations
- Added costs for arbitrator's fees (some states require employer to pay all)
- Arbitrators less likely to grant dispositive relief



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# Consider a Mandatory Arbitration Program

- Create arbitration program and agreements with a focus on the current case law concerning enforceability
- Identify forum and procedural rules of selection of arbitrator and discovery
- Ensure arbitration agreement provides mutuality
- Exclude non-arbitral claims from the arbitration program
- Include class and collective action waivers



# Conduct a Wage and Hour Audit

- Reduces the likelihood that an employer will face an FLSA collective action lawsuit
  - Costs pale in comparison to the costs of a lawsuit
- Engage counsel (in-house or outside)
- Take steps to preserve the attorney-client privilege
- Determine the scope of the audit
- Comprehensive audit is advisable for:
  - Compliance and litigation avoidance
  - Due diligence for a corporate transaction



# Conduct a Wage and Hour Audit

- Treatment of workers as independent contractors using the factors considered by the Wage and Hour Division and the courts;
- Classification of employees as exempt from minimum wage and/or overtime requirements, including whether the applicable salary basis, compensation level, and duties tests are met;
- Calculation of the regular rate and overtime pay, including whether all appropriate remuneration is included;
- Recording and payment of hours worked, including whether all compensable time is recorded and paid;



# Conduct a Wage and Hour Audit

- Meal period and rest break policies and practices, including whether employees receive and are completely relieved of all duties;
- Compliance with all applicable tip, tip pooling, and tip credit rules;
- Compliance with all applicable child labor provisions;
- Payroll and compensation policies and procedures, including any policies relating to overtime, recording of hours worked, and recordkeeping



# Conduct a Wage and Hour Audit

- Once the audit is complete:
  - Meet with counsel to discuss any potential problem areas
  - Develop solutions for addressing or correcting any concerns
  - Determine a plan for communicating and implementing any changes
- Consider whether to use the DOL's Payroll Audit Independent Determination (PAID) program



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# Establish Formal Policies and Procedures

- Adopt a written wage and hour policy that communicates the employer's intention to avoid improper deductions and provides a specified procedure for reporting alleged improper deductions
- Adopt a policy that provides an anonymous complaint procedure, prompt investigation, and no retaliation
- Require employees and managers to review and certify timekeeping records



# Conduct Wage and Hour Training

- Training is one of the most effective ways to reduce risk and ensure compliance
- Consider conducting practical training focused on helping managers identify the situations most likely to lead to wage and hour mistakes
- Managers and supervisors must understand that seemingly compassionate decisions can result in FLSA violations



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# Conduct Wage and Hour Training

- Train Human Resources regarding how to promptly investigate complaints and correct any improper practice
- Train managers regarding proper timekeeping practices, proper deductions for disciplinary violations, and enforcement of overtime policies
- Train employees regarding proper timekeeping practices



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# Questions



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