

2014 Employment and Labor Law Seminar

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The FLSA: Common Mistakes or The Ostrich Effect

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Presented by:
Dorraine A. Larison

These materials are provided for general informational purposes only and should not be construed as legal advice or legal opinion on any specific facts or circumstances. You are urged to consult a lawyer concerning any specific legal questions you may have.

Mistake or Ostrich Effect

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mis-take

- *verb* \mə- 'stāk\ : to understand (something or someone) incorrectly
- : to make a wrong judgment about (something)
- : to identify (someone or something) incorrectly

Mistake or Ostrich Effect

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Ostrich Effect

- unwilling to recognize or acknowledge a problem or situation



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The Environment - Ignore the FLSA at Your Own Risk 

- Recent study – more than 75% of class actions nationwide were related to wage and hour claims
- Political Environment – More Enforcement
- Settlements
 - Satellite Link Corp \$203,000
 - Minnesota Wal-Mart \$54 million

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Why FLSA Claims Are Popular 

- Often impacts entire groups of employees
- Favorable burden of proof
 - Employees presumptively non-exempt
 - Lack of records of hours detrimental to employer
- Favorable damages
 - Overtime rate 1.5x regular rate of pay
 - Liquidated damages (potentially doubling back pay award)
 - 2 – 3 year limitations period
 - Attorney fees
- Generates public revenue

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Mistake 1 - Misclassification of Employees – Exempt or Non-Exempt 

- The Number One Mistake Made By Employers
- Examples:
 - Treating All as “Salaried”
 - Assuming Employees Are Exempt
 - Failure to Constantly Evaluate the Position
- What are the Most Misused Exemptions?

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Administrative Exemption



- Bona fide administrative employees:
 - Weekly salary at least \$455
 - Primary duty office / non-manual work management of general business operations
 - Discretion / independent judgment in matters of significance

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Executive Exemption



- Bona fide executive employees:
 - Weekly salary at least \$455
 - Primary duty management of the business, department or subdivision
 - Directs work of 2+ fulltime employees
 - Hire, fire, promotion recommendations given particular weight

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Outside Salesperson



- Primary duty *making sales or obtaining orders or contracts* for services
- *Customarily and regularly* engaged away from employer's place of business
- Salary requirements do not apply
- Incidental work to employee's own sales

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Professional Exemption – Learned Professional



- Primary duty
 - Work requiring advanced knowledge in a field of science or learning;
 - Advanced knowledge must in be field of science or learning; and
 - Advanced knowledge must be customarily acquired by a prolonged course of specialized intellectual instruction

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Highly Compensated Employees



- Employees who earn at least \$100,000 a year
- Who perform one or more exempt duties or responsibilities of an executive, administrative, or professional employee
- Must perform office or non-manual work

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Misclassification Questions



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Tightwad Bank

Is Jeff exempt from the FLSA requirements as an Executive Employee?

(A) Yes, absolutely
(B) Maybe
(C) No

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Tightwad Bank

Is Jeff exempt from the FLSA requirements as an Administrative Employee?

(A) Yes, absolutely
(B) Maybe
(C) No

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Tightwad Bank

Is Jeff exempt from the FLSA requirements as a Salesperson?

(A) Yes, absolutely
(B) Maybe
(C) No

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Tightwad Bank 

Is Jeff exempt from the FLSA requirements as a Professional?

(A) Yes, absolutely
 (B) Maybe
 (C) No

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Tightwad Bank 

If you give Jeff a \$10,000 bonus at the end of the year is he exempt as a Highly Compensated Employee?

(A) Yes, absolutely
 (B) Maybe
 (C) No

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Losing Exempt Status: Salary Basis 

- No reductions for variations in quality / quantity work
- Exceptions:
 - Personal leaves for one or more full days
 - Full day absences for sickness/disability if part of bona fide plan
 - Penalties for infractions of major safety rules
 - Unpaid full day disciplinary suspensions for infractions of written workplace conduct rules
 - Employees commencing or leaving employment mid-week
 - Intermittent FMLA leave
- Risky Policies?
 - Requiring a 45 hour/week schedule?
 - Fining \$100?

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Importance of Safe Harbor Complaint Process

- Clearly communicated policy
- Prohibit improper pay deductions - good faith commitment to comply with law
- Include complaint mechanism
- Reimburse employees for improper deductions

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Mistake 2 – Not Compensating for All Time Worked

- What Time at Work is Compensable?
 - Break times
 - Other issues: on-call, training, travel time, unauthorized work, donning and doffing

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Time Worked Questions



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True or False

Employers must pay for all hours worked even when employees volunteer to work “off the clock.”

(A) True
(B) False

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True or False

If an employee is working and eating during her lunch break it is not considered compensable time.

(A) True
(B) False

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Is the time that employees spend at the annual company picnic work time?

(A) Yes, absolutely
(B) Maybe
(C) No

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Mistake 3 – Miscalculating Overtime Pay



- What is the Regular Rate of Pay?
 - How to calculate hourly rate?
 - Include bonuses?
 - Fixed schedule (default) vs. fluctuating workweek methods

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Miscalculating Overtime Questions



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Are discretionary bonuses included in the regular rate of pay?

- (A) Yes, absolutely
- (B) Maybe
- (C) No

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Are commission payments included in the regular rate of pay?

- (A) Yes, absolutely
- (B) Maybe
- (C) No

Regular Rate of Pay

- Included
 - Commissions
 - Nondiscretionary bonuses
 - Shift differential
 - On-call pay
- Not Included
 - Discretionary bonuses
 - Gifts
 - Tuition/Loan Forgiveness
 - Vacation/Sick/Holiday
 - Profit Sharing, Etc.

Mistake 4 – Multiple Job Issues

- Can pay different rates for different jobs
- Track and aggregate hours of all jobs
- Determine regular rate of pay:
 - Alternative 1: Weighted average
 - Alternative 2: Time and one-half during overtime hours

John delivers furniture for two separate locations of Fabulous Furniture. Can John be paid by separate checks for the hours worked at each location?

- (A) Yes, absolutely
- (B) Maybe
- (C) No

Other Common Mistakes

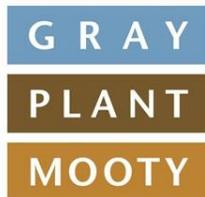
- Misclassifying workers as Independent Contractors
- Use of unpaid Interns
- Failing to Keep Records of Time Worked

Questions and Answers



Thank you for your time.

The FLSA – Common Mistakes or The Ostrich Effect



Dorraine A. Larison
Gray, Plant, Mooty, Mooty & Bennett, P.A.
Suite 500
1010 West St. Germain Street
St. Cloud, MN 56301
(320) 252-4414

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The following is a summary of some of the basic wage and hour and hour rules and regulations relating to the presentation.

I. Calculating the Regular Rate of Pay and Overtime

The federal Fair Labor Standards Acts (“FLSA”) and state law do not prescribe a method of payment or form of remuneration that employers must always utilize. Employers and employees may agree upon almost any method and period for the payment of wages, and the computation of wages may be made in a variety of manners.¹ The federal FLSA does prescribe, however, that regardless of the form of remuneration, employers must comply with the minimum wage and overtime requirements of the statute. This is why so many employers unwittingly end up paying more money than initially anticipated. Generally, an employee’s regular rate is the standard for computing overtime pay under the FLSA.

The regular rate, regardless of its form, must be converted to an hourly rate which will be the rate at which the employee is deemed to have been actually paid for each week’s work. Overtime pay is generally figured on a weekly basis under the FLSA; therefore, the regular rate must be computed each week.

$$\begin{array}{c} \textit{TOTAL REMUNERATION FOR EMPLOYMENT IN A WORKWEEK} \\ \textit{(except statutory exclusions)} \\ \div \\ \textit{TOTAL NUMBER OF HOURS ACTUALLY WORKED} \\ = \\ \textit{REGULAR HOURLY RATE OF PAY} \end{array}$$

What Is Included in Remuneration?

The regular rate of pay includes all remuneration for employment paid to, or on behalf of the employee except payments specifically excluded under the Act. The regular rate may be based on an hourly rate, a piece rate, a day rate or job rate. 29 C.F.R. §§ 778.108–778.113.

Other forms of payments included in the regular hourly rate:

- Commissions.
- Non-cash Payments: For compensation not in the form of cash, the employer must compute the fair market value of the goods into the regular rate of pay.
- Nondiscretionary Bonuses: Regularly paid bonuses must, as a general rule, be included in calculating the regular rate of pay including production, good

¹ Note that Minnesota requires that wages be paid at least every 30 days by negotiable instrument.

attendance, and other similar bonuses. These bonuses must be attributed to the period of time in which they were earned in order to recalculate the regular rate of pay.

- Other forms of payments not included in the regular hourly rate: Discretionary bonuses, e.g. any bonus not subject to prior contract or agreement; gifts or gratuities; tuition or loan forgiveness programs, vacation, sick leave and holidays; profit-sharing, pension and welfare payments; and certain overtime premium payments.

Common Overtime/Regular Rate Mistakes

- Failure to combine hours worked in more than one department or at more than one facility when determining the total hours worked for the calculation of overtime.
- Improper calculation of the regular rate of pay to include such items as shift differential, bonuses or on-call pay in calculating an employee's regular rate of pay.
- Allowing "comp time" in lieu of overtime payment. Compensatory time off cannot substitute for overtime payment unless the time off is provided within the same period used to determine whether an employee has worked overtime (e.g., time off within the same week).

II. Employers Must Pay Employees for All Their Working Time

A. Time Clock Issues

Although employers must maintain accurate records of time worked, they are not required to use time clocks, time cards, or any particular type of time-recording system. If an employer does use time clocks, it can disregard early or late punching by employees who voluntarily arrive early or remain after hours, so long as the employees do not perform work during these periods. When employees work more hours than their time cards show, the employer must pay for the extra hours, but may instruct the employee not to do so in the future.

Whatever time-recording system an employer uses, problems may arise over the treatment of small amounts of scheduled or unscheduled time missed or worked by employees. Employees generally must be paid for all time worked; an employer cannot use rough estimates or arbitrary formulas to compute hours worked. However, regulations establish the following two rules:

- **"Rounding off"**: Employers may record employees' starting or stopping times to the nearest five minutes or to the nearest one-tenth or quarter of an hour, provided that the amounts rounded off average out over time and the practice does not result in the failure to compensate employees for all time worked.

- **“De minimis” rule:** An employer may disregard insubstantial or insignificant amounts of time beyond a worker’s scheduled hours if it cannot “as a practical administrative matter” precisely record the small portion of time involved. This rule only applies “where there are uncertain and indefinite periods of time involved of a few seconds or minutes duration, and where the failure to count such time is due to considerations justified by industrial realities.” An employer, however, may not arbitrarily fail to count as hours worked any part of fixed or regular working time or “practically ascertainable” periods of time that workers are required to spend on assigned duties.

In addition, some employers are tempted to simplify recordkeeping and pay employees for a set number of hours, regardless of the employees’ time worked. While this might be possible under certain limited circumstances, it is not advisable. This system could create problems, particularly if an employee claims that his or her hours were greater than the standard time that was compensated.

B. Lunch and Work Time: “Suffer or Permit to Work”

A common mistake employers make is time-clock issues surrounding lunch, where employees choose to work during a designated lunch period. The FLSA simply defines employee as “suffer or permit to work.” The general test developed from case law and Wage and Hour regulations is that work not requested but “suffered or permitted” must be included in hours worked. If an employer knows or has reason to believe that the employee is working, the hours are compensable.

Employers often try to control overtime hours by only paying for authorized overtime. However, if an employer knows or has reason to know that the employee is working unauthorized hours, the employer must compensate the employee for those hours unless it takes action to stop such unauthorized hours. The hours are compensable unless the employee works hours without the knowledge of the employer or under circumstances in which a reasonable employer would not have knowledge.

C. Ignoring Employees Who Work Without Recording Time/Not Paying For Unauthorized Work

Employees who choose to work after their shift is over or when not authorized for other reasons almost always must be paid. It does not matter why the employee works so long as the employer “suffers or permits” employees to work on its behalf, proper compensation must be paid. This generally means that once an employer allows the employee to work, or knows that the employee is working, the employee must be compensated. This is true whether the work is being performed at the place of business or at home. A violation of the FLSA occurs when, as a result of unreported hours worked, an employee’s hourly wage for a pay period falls below the minimum wage. Similarly, a violation also occurs if, as a result of “off-the-clock” work, an employee is not paid for hours worked in excess of 40 hours in a workweek. An employer may not change an employee’s time, even with the employee’s agreement, so as to reduce hours based on unauthorized work.

Management must make sure that any work it does not want done—whether “regular” work or overtime work—is not performed in the first place. Mere issuance of a rule to that effect is not sufficient to avoid compensation for additional hours actually worked. Moreover, an employee’s violation of the employer’s rules is not a bar to recovery. Even if the employer only has reason to believe that an employee is submitting inaccurate time cards, the employer may be liable to pay for additional overtime hours.

Some management practices may heighten an employer’s risk of exposure to claims for additional compensation. For example, employees successfully argued in one case that their employer knew that its productivity goals could not be met without working “off-the-clock.” In that case, there was clear evidence that the employees had been working “off-the-clock,” including a manager’s telling them, “Don’t get caught — if you get caught, they will bust you.” The employees also had keys to the store so that they could work beyond their scheduled hours.

There are some legal ways to help prevent unauthorized work, however, including:

- Adopt a clear time and attendance policy outlining when employees are allowed to work and sending a clear message to their employees not to work “off the clock,” even if a manager tells them to.
- Training managers regarding the requirements of the FLSA, the employer’s policies and holding them accountable for violations of those policies.
- Requiring managers to review weekly time entries, particularly with automated systems.
- Training all staff about timekeeping policies, including training the payroll department to identify questionable timesheets.
- Uniformly addressing any policy violations by employees or supervisors.

D. Electronic Work Outside the Office

As mobile technology and computer systems become ubiquitous, employers often find non-exempt employees checking email or voicemail or doing other potentially work-related tasks outside of the workplace, outside of normal work hours. Many employers forget that even relatively small amounts of time spent by employees outside of work may require payment and count toward overtime according to the FLSA. A recent case provides some guidance on this complicated issue.

The courts and DOL have recognized that insubstantial or insignificant periods of time outside scheduled working hours may be disregarded in recording working time. This rule applies, however, only where a few seconds or minutes of work are involved and where the failure to count such time is due to considerations justified by industry realities. Such time is considered *de minimis*, that is, minor or trivial.

In *Rutti v. Lojack*, that court (the federal Ninth Circuit Court of Appeals) considered wage and hour claims brought by a technician employed to install and repair alarms in customers’ cars. In addition to interesting travel time issues presented, the

employee argued that certain pre- and post-work activities required compensation. He was paid on an hourly basis starting with his arrival at the first job of the day and ending with his completion of the last job of the day. He was not paid for certain pre-commute activities or for uploading his report of the day's activities after he returned to his home in the evening. Before leaving home, the employee spent time receiving assignments for the day, mapping his routes to the assignment, and prioritizing the jobs, and sometimes filling out forms for the jobs. After returning home, he had to upload data about the work he performed on a portable computing device and check that the transmission was successful. If there was a problem he would have to transmit again. In his lawsuit, the employee claimed that he (and others like him) should have been paid for the pre- and post-shift work.

The court considered whether the employee's pre- and post-shift activities were part of his principal activities and therefore compensable or whether such activities were so de minimis as to be noncompensable. The court held that plaintiff's pre-commute activities were not integral to his principal activities because "most of his activities – 'receiving, mapping and prioritizing jobs and routes for assignment' – are related to his commute." The court also concluded that the plaintiff's completion of pre-commute paperwork took only a minute or so, and was, therefore, de minimis. The plaintiff's post-commute computer transmissions, however, could be compensable because they were closely related to the plaintiff's principal activities. The panel was divided as to whether the record showed that these transmissions took just a few minutes or 10 minutes or more. Ultimately, the court remanded the issue to the district court to resolve the issue in accordance with the court's previously adopted test for determining whether certain work-related activities were so de minimis as to be noncompensable. That test requires a consideration of: (1) "the practical administrative difficulty of recording the additional time," (2) "the aggregate amount of compensable time," and (3) "the regularity of the additional work." In the end, while the case does not provide clear answers, it is instructive regarding the type of analysis that could be applied in situations such as employee's checking mobile email devices or answering an after-hours work phone call.

E. Examples of Compensable Working Time

The following are examples of working time for which an employee is entitled to receive compensation:

- time spent by budget or fiscal employees required to remain until an official audit is finished;
- changing clothes, if required by the nature of work;
- charitable work requested or controlled by the employer;
- cleaning and oiling machinery;
- driving van pools when the driver is chosen by the employer and under the control of the employer;
- driving employer-owned vehicles between secure parking locations and work sites and back at the end of the work shift, which benefitted the employer;
- emergency work or travel time;

- fire drills or other disaster drills, whether voluntary or involuntary, either during or after regular working hours;
- grievance assistance (under a union agreement to handle worker complaints) during the time an employee is required to be on the premises, unless a contract provides otherwise;
- labor-management committee meetings on daily operations or contract interpretations, unless a union contract provides otherwise;
- make-ready work;
- meal periods, if: (1) employees are not free to leave their posts, or (2) the time is too short to be useful to employees;
- medical appointment during working hours at the request of the employer's insurer;
- medical attention during working hours at the employer's direction;
- on-call time where liberty is restricted;
- preparatory work which is part of the principal activity;
- principal activities;
- rest periods of 20 minutes or less;
- show-up time of 10 or 15 minutes, if the employees are required to remain on the premises that long before being sent home;
- stand-by time during short plant shutdowns;
- training in regular duties to increase efficiency;
- training programs required by the employer;
- traveling (but not performing work) from one work site to another or traveling out of town during work hours;
- uniform laundering or cleaning of other distinctive clothing required by the employer, at least to the extent it cuts into the minimum wage;
- waiting for work after reporting or while on duty;
- walking back and forth from the locker rooms to the production floor after donning and before doffing required protective gear at a meat-processing plant;
- waiting to doff required protective gear at the end of a work shift at a meat-processing plant; and
- washing up or showering, if it is required due to the nature of the work.

F. Examples of Non-Compensable Time

The following are examples of work-related matters for which an employee need not be compensated:

- absences (including sick leave, annual leave, holidays, funerals and weather-related absences);
- athletic contest involvement as a participant, official, or scorer, even if sponsored by the employer, so long as voluntary and not a condition of employment;
- charitable work done voluntarily outside of working hours;
- clothes changing at home;

- grievance procedures classified as non-paid by a union contract;
- holidays on which an employee does not work;
- jury duty;
- labor-management committee meetings on internal union affairs, unless a union contract provides otherwise, and labor-management committee meetings classified as unpaid time by a union contract;
- meal periods involving no duties and lasting one-half hour or longer;
- medical attention outside of working hours, or not at the direction of the employer;
- on-call time where the employee merely leaves a telephone number and is not restricted;
- operation of an employer's motor vehicle for employee's own commuting convenience;
- personal time for employees who live on an employer's premises;
- sleeping time up to eight hours under a contract if the tour of duty is 24 hours or longer;
- shutdowns for regular, customary equipment maintenance where the employee is free to leave the premises;
- time spent before, after or between regular working hours;
- trade school attendance, which is unrelated to present working conditions;
- training programs voluntarily attended that are unrelated to regular duties and involve no productive work;
- traveling: (1) from home to a work site, and vice versa; and (2) on overnight trips, during non-working hours, except while performing duties or other work;
- traveling from home to field inspection sites and back while carrying 15 pounds of work files;
- traveling through airport security checkpoint and then riding an employer-provided vehicle to and from the work site, where the procedure was required by the FAA and not the employer;
- traveling through security checkpoints at a nuclear power plant, parking and then walking to the job site and obtaining boots, safety glasses and helmets;
- voting time, as long as state laws do not require compensation;
- waiting time: (1) in a paycheck line; (2) to check in or out; and (3) to start work at a designated period;
- waiting to don required protective gear at the beginning of a work shift at a meat-processing plant; and
- washing up or showering under normal conditions.

III. Maintaining Accurate and Required Records

Employers subject to the FLSA must keep records for both nonexempt and exempt employees. FLSA regulations do not prescribe a particular order or form of records to be retained. Rather, recordkeeping requirements vary depending upon the

nature of the work performed by an employee. Records may be maintained on paper or in electronic form, provided that the record is accessible and reproduction possible.

DOL also has stated that employers can use “any timekeeping method they choose” for keeping track of employees' hours worked — for example, a time clock or an individual acting as a timekeeper — as long as the method is “complete and accurate.” Employers should note that records required for exempt employees differ from those required for nonexempt workers. Also, special information is required for employees paid under unusual pay arrangements or to whom board, lodging or other facilities are furnished. In addition to following recordkeeping requirements, employers are required to display the Wage and Hour Division’s minimum wage poster, which briefly outlines the requirements of the FLSA.

A. Nonexempt Employee Information to Maintain for Three Years

1. Full Name
2. Home Address
3. Zip Code
4. Birth Date (if under 19)
5. Gender
6. Occupation in Which Employee is Employed
7. Time and Date on Which the Work Week Begins
8. Regular Hourly Rate of Pay
9. Basis on Which Wages are Paid
10. Hours Worked Each Day
11. Total Hours Worked Each Work Week
12. Total Daily or Weekly Straight Time Earnings or Wages
13. Total Weekly Overtime Compensation
14. Total Deductions from Wages for Each Pay Period
15. Total Wages Paid Each Pay Period
16. Date of Payment and the Pay Period Covered by the Payment

B. Exempt Employee Records

The FLSA’s recordkeeping requirements for exempt employees are almost identical records for exempt employees, as for non-exempt employees, with the exception of some of the requirements relating to payment and hours worked (1-6 above but not 7-16). In addition, the employer must keep records reflecting the basis on which wages are paid. These records must contain sufficient detail to permit calculation, for each pay period, of the employee’s total compensation for employment, including fringe benefits and prerequisites. The regulations note that the basis of payment may be shown as a dollar amount of earnings per month, per week, etc., with appropriate addenda such as “plus hospitalization and insurance plan” or “two-weeks paid vacation.”

There is no limitation on employers requiring exempt employees from tracking hours worked and maintaining those records. In the event of challenge by an employee

of his or her exempt status, such records could be used to help demonstrate that an employee did not work overtime at all or to minimize potential damages.

IV. Classification of Employees as Exempt

Some employees are exempt from the overtime pay provisions or both the minimum wage and overtime pay provisions for the FLSA. Generally, exemptions are narrowly defined under the FLSA, so employers must carefully consider the actual circumstances for each position to determine if an exemption applies. It is a common misconception that an employer’s decision to classify employees as “salaried” or “hourly” or “office” or “production” controls an employee’s FLSA classification. It is an employee’s specific position and duties, however, that controls as well as whether an employee is exempt.

Reminder: Major Exemptions (from both minimum wage and overtime pay) and Their Requirements:

<i>Executive Employees:</i>	
Salary	\$455 per week or “Business Owner” with 20% or more bona fide equity interest
Duties	Primary duty is management of the enterprise or a recognized department or subdivision. Customarily and regularly directs the work of two or more other employees. Has authority to hire or fire other employees or whose suggestions and recommendations as to hiring, firing, promotion or other change of status of other employees are given particular weight.
<i>Administrative Employees:</i>	
Salary	\$455 per week
Duties	Primary duty is performing 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 with respect to matters of significance.
<i>Learned Professional Employees:</i>	
Salary	\$455 per week
Duties	Primary duty is performing: a) work requiring knowledge of an advanced type in a field of science or learning customarily acquired by a prolonged course of specialized intellectual instruction, but which also may be acquired by alternative means such as an equivalent combination of intellectual instruction and work experience; or

	b) work requiring invention, imagination, originality or talent in a recognized field of artistic or creative endeavor.
Computer Employees:	
Salary	<i>Either</i> \$455 per week on a salary or fee basis <i>or</i> if compensated on an hourly basis, at a rate not less than \$27.63 an hour
Duties	Employed as a computer systems analyst, computer programmer, software engineer or other similarly skilled worker in the computer field whose Primary duty is performing: 1) The application of systems analysis techniques and procedures, including consulting with users, to determine hardware, software or system functional specifications; 2) The design, development, documentation, analysis, creation, testing or modification of computer systems or programs, including prototypes, based on and related to user or system design specifications; 3) The design, documentation, testing, creation or modification of computer programs related to machine operating systems; or 4) A combination of the aforementioned duties, the performance of which requires the same level of skills.
Outside Sales Employees:	
Salary	N/A
Duties	Primary duty is: a) Making sales (as defined in the FLSA); <i>or</i> b) obtaining orders or contracts for services or for the use of facilities for which a consideration will be paid by the client or customer; <i>and</i> The employee must be customarily and regularly engaged away from the employer's place or places of business.

V. Misclassification of Independent Contractors

A common issue arising under the FLSA is whether an individual is an employee—and so subjecting his or her employer to the FLSA's requirements—or an independent contractor not subjecting the company to responsibilities under the FLSA. This classification is also important for tax purposes. The Obama Administration

recently sought \$25 million for 90 new employees to investigate employees misclassified as independent contractors making this issue even more important.

As a general rule, independent contractors bid to perform work and are evaluated based on results rather than their day-to-day performance. Contractors control their own employees and responsible for their employees' compensation and benefits. If there is a real independent contractor relationship, an employer contracting with the independent contractor is not responsible for FLSA compliance with respect to that contractor, unless "hot goods" are involved.

Employers, however, obviously are not free to set up sham independent contractor relationships that violate the FLSA. They cannot, for example, designate a particular employee as an independent contractor and then violate the FLSA with impunity with respect to the employee. The traditional FLSA legal test that establishes a true independent contractor is called the "economic reality test." In applying this test, the courts generally focus on five factors:

1. the degree of control exerted by the alleged employer over the worker;
2. the worker's opportunity for profit or loss;
3. the worker's investment in the business;
4. the permanence of the working relationship; and
5. the degree of skill required to perform the work.

DOL has endorsed an economic reality test of its own, adopting similar factors. DOL considers a number of factors, including:

1. the extent to which services rendered are an integral part of the employer's business;
2. the permanency of the relationship;
3. the amount of the worker's individual investment in facilities and equipment;
4. the opportunities for the worker to experience profit and loss; and
5. the degree of initiative, judgment or foresight exercised by the individual who performs the services.

If an independent contractor does not meet these tests, the individual must be considered an employee for FLSA purposes. DOL and the courts do not put great weight on whether an individual is called an "independent contractor." Instead, they take a close look at the realities of the relationship. Therefore, employers that seek to avoid the costs and responsibilities of entering into employment arrangements by calling employees "independent contractors" should beware. The courts and DOL use the tests discussed above to ferret out such sham arrangements.

Before entering into an independent contractor agreement, an employer should review the agreement carefully to ensure that the individual is truly an "independent contractor" and not an employee for purposes of the FLSA. Because different courts and DOL look at slightly different factors, employers should review both the economic

realities and the hybrid tests to determine if an individual is a true independent contractor. A contractual understanding is also advisable.

Other steps that may help protect an independent contractor from being deemed an employee include:

- have a written agreement;
- pay on a per-project basis, wherever possible, and ask the contractor to cover his or her out-of-pocket expenses;
- specify that the contractor is responsible for his or her employment and income taxes;
- explicitly state in the agreement that the worker is an independent contractor, and ensure that the worker does not represent himself or herself to be an employee;
- state that the contractor has a right to control the project;
- do not provide employee benefits;
- arrange for the contractor to provide his or her own equipment and tools; and
- specify the terms for renewal and termination of the project, including the contractor's right to terminate the relationship.

VI. Furlough of Exempt Employees and Related Cost-Saving Measures

A. Exempt Furloughs: No Work During the Entire Week

FLSA regulations provide that an exempt employee must be paid on a salary basis. According to the regulations, “[a]n employee will be considered to be paid ‘on a salary basis’ within the meaning of the regulations if under his employment agreement he regularly receives each pay period on a weekly, or less frequent basis, a predetermined amount constituting all or part of his compensation, which amount is not subject to reduction because of variations in the quality or quantity of the work performed.” In order to be considered paid on a salary basis, “the employee must receive his *full salary for any week in which he performs any work without regard to the number of days or hours worked,*” but “an employee need not be paid for any workweek in which he *performs no work.*” The regulations further state that “[a]n employee will not be considered to be paid ‘on a salary basis’ if deductions from his predetermined compensation are made for absences occasioned by the employer or by the operating requirements of the business.” Therefore, if an exempt “employee is ready, willing, and able to work, deductions may not be made for time when work is not available.”

If an employer asks or allows employees to take unpaid leave in increments of less than a week, it could lose exemptions for its employees during the entire period in which the policy is in effect. The regulations state, “where deductions are generally made when there is no work available, it indicates that there was no intention to pay the employee on a salary basis.” The regulations do, however, provide a window of correction for employers to correct improper deductions from exempt employees’ compensation. If the employer has inadvertently made these deductions already, the

exemption from overtime requirements will not be considered to have been lost if the company reimburses the employees for such deductions and promises to comply in the future.

B. Issues Related to Other Cost-Saving Measures

Certain cost saving actions aimed at reducing employee wages should be reviewed carefully to ensure that they comply with state and federal wage and hour laws.

- **State Notification Statutes.** Neither the federal Fair Labor Standards Act (“FLSA”) nor Minnesota’s wage and hour laws require that employers provide advance notice prior to implementing reductions in wages or work schedules. Several other states, however, do have such notification requirements. In South Carolina, for example, employers are required to provide at least seven days’ advance notice prior to implementing any changes to an employee’s normal hours or wages. As part of the planning process, employers with personnel in other states should determine whether similar notification statutes exist.
- **Non-Exempt Employees.** Employees who are not exempt from the minimum wage and overtime requirements of the FLSA should be notified of any changes to their regular rate of pay prior to such changes taking effect. To avoid any potential disputes, such notifications should be provided in writing. Employers need to track the hours worked by these employees, and make certain that they receive at least the minimum wage for all hours worked, and that they receive overtime compensation for all hours worked in excess of 40 in any workweek. While public sector employers are able to avoid paying overtime by providing compensatory time off in lieu of overtime pay, private employers are not permitted to adopt such practices.
- **Exempt Employees: Reducing Salary In Response to Reduced Hours.** Employees are considered to be paid on a “salary basis” if they receive their regular salary regardless of variations in the quality or quantity of work performed. Reductions in an employee’s salary because of changes in the amount of hours they are required to work could indicate that the employee is not truly being paid on a salary basis. To reduce this risk, companies should avoid justifying salary reductions by indicating that there will be a corresponding reduction in the employees’ work schedule.

VII. Unpaid Interns

The Fair Labor Standards Act (“FLSA”) requires employers to pay minimum wage and overtime to nonexempt employees covered under the act. Because the FLSA makes exceptions for volunteered services to non-profit charitable organizations or government agencies, unpaid internships in the non-profit or public sector are generally permissible.

Unpaid internships in the “for-profit” private sector, however, are only allowed under narrow circumstances. The fact that the intern agreed to work for free is not the end of the analysis; administrative agencies and courts look past the parties’ agreement to the true nature of the relationship. Generally speaking, the more an intern resembles an employee, the more likely it is that the intern will be covered by the FLSA.

A. Requirements for Exemption From FLSA

Most often, internships in “for-profit” settings will be considered employment. In order for an internship to be exempt from FLSA requirements, it must satisfy the following criteria provided by the Department of Labor:

- The internship, even though it includes actual operation of the facilities of the employer, is similar to training which would be given in an educational environment.
- The internship experience is for the benefit of the intern.
- The intern does not displace regular employees, but works under close supervision of existing staff.
- The employer that provides the training derives no immediate advantage from the activities of the intern, and on occasion its operations may actually be impeded.
- The intern is not necessarily entitled to a job at the conclusion of the internship.
- The employer and the intern understand that the intern is not entitled to wages for the time spent in the internship.

If all six factors are met, there is no employment relationship under the FLSA, and an intern may serve on an unpaid basis.

B. For the Benefit of the Intern:

Perhaps the most important of these six factors is the question of who benefits most from the internship. Because many internships arise out of an educational curriculum, where a college or university maintains oversight and control of the program and the intern receives school credit, there is often an educational benefit to the intern. School credit alone, though, is not sufficient to satisfy the FLSA requirements, nor is it required, as long as the experience is educational in nature. However, if the skills developed are not generally useful or broadly applicable, and are instead related only to a specific workplace, the internship will be viewed as traditional job training that is part of an employment relationship.

Generally, the employer should not expect to enjoy immediate benefits of the intern’s work. For example, an employer cannot allow an unpaid intern to substitute the work that would normally be completed by a paid employee; in other words, the business

should not depend on the intern's labor for the completion of necessary work. Requiring unpaid interns to handle only menial and noneducational work is impermissible under the FLSA.

C. Supervision:

An unpaid intern is allowed to shadow other employees or work under close supervision, but problems can arise when the intern is responsible only for routine daily work; the more the unpaid intern handles routine operations, like filing, secretarial work, or customer service, the less likely it is that any additional benefit to the intern will excuse the work from FLSA requirements. Direct employer supervision lends itself to the educational nature of an intern's work, and it also ensures that the unpaid intern is not merely replacing the work of a normal employee.

Some employers view internships as a long-term job interview; a way to screen prospective employees. With regard to unpaid interns, this is not appropriate. It is not permissible to use unpaid internships as a trial period for potential employees, or as a means of displacing the inherent costs of on-the-job training.

VIII. Tips: Significant Differences Between Minnesota and Federal Law

Federal law allows employers to consider tips as part of wages under certain circumstances if the employer pays at least \$2.13 an hour in direct wages. Minnesota law, however, significantly differs. Under Minnesota law, no such "tip credit" is allowed and employers must pay the applicable (generally federal) minimum wage even to employees who receive tips. Further, employers may not require employees to contribute or share gratuities with the employer or other employees or to contribute any of their gratuities to a pool operated by the employer or other employees. Employees may voluntarily share tips so long as the employer is not involved in the arrangement. In situations where a tip is provided to more than one employee, such as a banquet, Minnesota regulations provide that only an "employee [that] provides direct service to a customer or customers" may share in the divided tip.

The FLSA – Common Mistakes or The Ostrich Effect:

Presented by:

Dorraine A. Larison

Tightwad Bank

Jeff Justice is a Commercial Account Manager at Tightwad Bank, which is a small locally owned bank. Jeff has a four year degree in accounting and has been in his position with Tightwad Bank for about two years. Jeff’s duties mainly involve building a commercial loan portfolio for the bank. Jeff is responsible for locating potential commercial loan customers and working with those customers and other bank employees to process and complete the loans. Jeff supervises two Loan Officers (Sue and Sharon). Sue and Sharon have the same duties as Jeff, without any supervisory responsibility. Jeff’s current salary is \$95,000.

The Environment – Ignore the FLSA at Your Own Risk

Why FLSA Claims are Popular

Mistake 1 – Misclassification of Employees – Exempt or Non-Exempt

Administrative Exemption

Executive Exemption

Outside Salesperson

Professional Employee

Highly Compensated Employee

Losing Exempt Status: Salary Basis

Importance of Safe Harbor Complaint Process

Mistake 2 – Not Compensating for All Time Worked

Mistake 3 – Miscalculating Overtime Pay

Regular Rate of Pay

Mistake 4 – Multiple Job Issues

Other Common Mistakes
