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WAGE AND HOUR LAW

Risk Factors Combine to Make Wage-and-Hour Audits a Priority for Employers in 2022

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Special to the Legal

As 2021 draws to a close, many employers are looking ahead to 2022 and hoping to reduce legal risk in the new year. Yet, pay practices put in place for nonexempt employees during the pandemic combined with the Pennsylvania Supreme Court's decision in July in *Heimbach v. Amazon.com* have created a perfect storm of wage-and-hour risk for Pennsylvania employers.

Prudent employers are examining both *Heimbach* and employee pay practices to assess their wage-and-hour risk via wage-and-hour audits. These audits look at employer pay practices, worker classifications, and remote work policies, among other areas, to identify potential noncompliance, make any required modifications and potentially avoid costly litigation.

• *Heimbach* expansively interprets the Pennsylvania Minimum Wage Act.

In *Heimbach*, the Pennsylvania Supreme Court held that time spent by nonexempt employees on an employer's premises waiting to undergo, and undergoing, mandatory security screening, was compensable under the Pennsylvania Minimum Wage Act (PMWA). The U.S. Supreme Court had found the exact same time not compensable under the federal Fair Labor Standards Act (FLSA) in 2014 in *Integrity Staffing v. Busk*. The *Heimbach* court also held that the FLSA's de minimis doctrine, which excludes from compensable time "insubstantial and insignificant periods," does not apply to bar claims for negligible or insignificant amounts of time worked under the PMWA.

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Beyond the two legal questions answered by the Pennsylvania Supreme Court in *Heimbach*, the decision underscored that the FLSA establishes a "national floor," and Pennsylvania has never adopted the Portal-to-Portal Act (PTPA) which amended the FLSA to create limits on the compensability of time that is preliminary or postliminary to the "principal activities" of employees.

Since the Pennsylvania Supreme Court issued its *Heimbach* decision this summer, we already have seen an increase in class action lawsuits brought under the PMWA, especially with respect to time spent by employees where they were required to be on the employers' premises.

• COVID still has an impact.

The Supreme Court's *Heimbach* decision comes at a time when employers continue to struggle with the challenges created by the COVID-19 pandemic. In March 2020 and throughout the last 21 months, employers quickly put in place various policies and practices in order to keep their businesses running.

Whether it was creating mechanisms to prevent employees from coming to work with symptoms of COVID-19, increases in the rates of pay for nonexempt employees to incentivize work during the pandemic or other wage-and-hour practices, now is the time for employers to take a step back and looks at these new practices as well as others with a critical eye.

• Wage-and-hour audits provide valuable snapshots.

There is no one-size-fits-all wage-and-hour audit. Some employers may want to focus on specific areas while others may want to do a more comprehensive analysis. The focus of wage-and-hour audits often is heavily impacted by an employer's industry. For example, over the last several years there has been a surge in class and collective action lawsuits in the hospitality industry challenging employers' implementation of the FLSA's tip credit and tip pooling regulations. Likewise, many employers in the energy industry have been sued for paying a "day rate" to employees.

While there is no "typical" wage-and-hour audit, the process includes an analysis of some foundational areas:

• Assessing potential exposure for off-the-clock work: Eliminating all off-the-clock work litigation risk is impossible. However, there are specific steps that can and should be taken to reduce that risk and ensure that such work is neither permitted nor encouraged. The stakes are high—alleged failure to pay nonexempt employees for all hours "worked" is by far the most common source of class and collective action wage-and-hour litigation.

• Determining whether nonexempt employees are permitted or encouraged to work off-the-clock typically requires the audit team to take the following steps:

—Define exactly what time qualifies as "hours worked" for a particular class of employees.

—Determine whether employees are permitted to perform preliminary work before their shift start time, postliminary work after their shift end time, or other compensable work during unpaid breaks or off-shift time (e.g., while not on the worksite).

—Identify any other factors that may result in the systemic underreporting of time (e.g., departmental protocols that discourage employees from incurring overtime, which could be interpreted mistakenly as discouraging employees from reporting all time worked).

"Hours worked" should include all compensable activities that occur during the "continuous workday" as defined by U.S. Department of Labor (DOL) regulations, which might include time spent "donning" and "doffing" work attire/equipment at the beginning or end of the workday; site-to-site travel time; or time spent working remotely. "Hours worked" also should include any off-shift work performed, assuming the knowledge or tacit approval of supervisors.

Although there is no 'magic bullet' in the wage-and-hour context, a wage-and-hour audit is a crucial step employers should take to reduce exposure to a large (and often uninsured) financial risk in the form of a DOL investigation and class and collective action litigation.

Pennsylvania employers should pay particular attention to the PMWA's regulations that define "hours worked" to include "time during which an employee is required by the employer to be on duty or to be at the prescribed work place" and "time spent traveling as part of the duties of the employee during normal working hours." As the *Heimbach* court made clear, these regulations are interpreted more expansively than the FLSA and do not incorporate PTPA principles.

Break time is compensable time, assuming the break is of insufficient duration for the employee to make effective use of that time for his or her own purposes (note that DOL regulations provide that breaks of less than 20 minutes duration must be paid and "bona fide" meal periods of 30 minutes or longer where an employee is completely relieved of duty need not be compensated). Likewise, any instance where an employee is engaged to wait is compensable time, as opposed to those who are merely waiting to be engaged (picture grocery store clerks looking at their phone while waiting for customers to arrive as opposed to employees carrying work-issued phones while at home or on break).

• Review of pay practices: Pay practices that undercompensate employees can lead to expensive fines and penalties as well as class and collective action litigation—even in the absence of any specific intent.

Frequent offenders include calculation of the regular rate of pay to determine employees' overtime rates and payment for travel time. An audit team's payroll practices review also ensures compliance with applicable document retention requirements. Strong documentation (including electronic records) can be an essential ally in defending wage-and-hour litigation should it arise.

Pennsylvania employers should be particularly focused on reviewing the practices at issue in *Heimbach*, i.e., time that employees are required to be

on the premises of the employer and any potential de minimis time worked by employees.

• Analysis of worker classifications: A classification audit typically aims to determine whether:

—Exempt employees' primary duties fall within one or more of the exemptions from overtime and minimum wage obligations recognized by the FLSA and relevant state law.

—Exempt employees are actually paid on a "salary basis," which is a condition precedent to exempt status in almost all circumstances.

—Exempt employees are paid the minimum salary required in order to be classified as exempt under the FLSA and state law.

—Independent contractors are treated like employees to such an extent that workers are misclassified and should be treated as employees for all purposes including tax and benefits.

—Unpaid interns or volunteers are properly classified and not entitled to wages or other compensation for their unpaid efforts. Although the job duties contained in a written job description should meet the pertinent requirements of state and federal law pertaining to exempt status, evaluation of written materials alone is generally insufficient to confirm that employees are properly classified as "exempt." It is essential also to determine whether the written job descriptions reflect the primary duties actually being performed by employees in that classification.

Similarly, assessing whether independent contractors, volunteers, and unpaid interns are classified properly can be a fact-intensive exercise. In the case of independent contractors, their status depends largely on an employer's degree of control over an individual worker, as well as the scope of work responsibilities and the degree of oversight and supervision. By comparison, in the case of volunteers their motivation and mindset are directly at issue. This is because unpaid volunteers must perform work for civic, charitable, or humanitarian reasons and must do so without expectation or receipt of more than nominal compensation for services rendered. Similarly, unpaid interns must have access to valuable experience comparable to that which would occur in an educational environment and employers should receive no immediate advantage from their work activities.

• Privilege considerations and methodology: Employers initiating an audit should ensure privilege protection to the maximum extent feasible, because to the extent an audit detects violations, any written audit report could be used against an employer in a subsequent lawsuit. Accordingly, most employers elect to engage counsel (either inside or outside counsel) to conduct the audit, invoke the attorney-client and attorney work product privileges, and thus shield many—although potentially not all—audit-related communications from discovery.

Ultimately organizations may wish to waive the privilege in the context of litigation. To avoid liquidated (double) damages under the FLSA, a defendant must prove that it had a "reasonable" or "good faith" belief that its actions were FLSA-compliant, and evidence of good faith reliance on an audit conducted by qualified legal counsel could help establish that defense.

Employers have weathered an unprecedented increase in wage-and-hour lawsuits over the past decade. In Pennsylvania, the state's Supreme Court and pandemic-related challenges have come together to create an especially attractive backdrop for wage-and-hour litigation. Although there is no "magic bullet" in the wage-and-hour context, a wage-and-hour audit is a crucial step employers should take to reduce exposure to a large (and often uninsured) financial risk in the form of a DOL investigation and class and collective action litigation. As Ben Franklin famously remarked, "an ounce of prevention is worth a pound of cure." •

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