

The Legal Intelligencer

THE OLDEST LAW JOURNAL IN THE UNITED STATES 1843-2013

PHILADELPHIA, MONDAY, FEBRUARY 3, 2014

VOL 249 • NO. 22

An **ALM** Publication

W A G E A N D H O U R

Employee Misclassification Litigation Is on the Rise

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Special to the Legal

On Jan. 10, conditional certification was granted to a nationwide collective action of some 1,750 human resources employees employed by Lowe's. The workers' allegation? That they were misclassified by the home improvement chain as "exempt" under the Fair Labor Standards Act (FLSA), and thus not paid overtime for hours worked more than 40 in a workweek. The workers claimed that although they were titled as "managers," such nomenclature was inaccurate as their daily work consisted mostly of administrative and clerical duties, as opposed to managerial functions such as employee supervision, hiring and firing.

The collective action in the Lowe's case is indicative of a growing trend confronting employers across the United States: employee misclassification litigation.

EXEMPT VERSUS NONEXEMPT AND THE FLSA

The classification of employees as exempt or nonexempt is one of the defining features of the FLSA. In most instances, in order to be classified as exempt, employees must be paid at least \$455 a week on a salaried basis, and with limited exceptions, such salary cannot be subject to deduction. Employees who are correctly classified as exempt are not entitled to overtime pay.

The FLSA provides categories of exempt workers and the U.S. Department of Labor regulations provide general parameters for analyzing exempt status, noting that "job titles do not determine exempt status," and



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that "in order for an exemption to apply, an employee's specific job duties and salary must meet all the requirements of the department's regulations."

Some of the categories of exempt jobs are as follows (note that each has specific parameters applied to it, including hours, salary, duties and other tests):

- Executive, administrative, professional, computer and outside sales employees.
- Seasonal amusement or recreational workers.
- Agricultural employees.
- Casual babysitters and persons employed as companions to the elderly or infirmed.

Unfortunately, many of the general standards and definitions of the various exemptions have proven difficult to apply in practice, and increasingly so as the American workforce has continued to evolve. When the FLSA was enacted in 1938, workers were more easily defined and classified. In an economy that was heavily manufacturing-based, most employers could look to the duties workers performed on a day-to-day basis and more easily determine what classification they fit into—for example, a

worker assembling products on a line was nonexempt; in contrast, the workers whose primary duties were overseeing those on the assembly line were exempt. But for years the U.S. economy has been transitioning from manufacturing-based to one that is heavily service-based. Instead of assembly line workers and machinists, U.S. jobs are now weighted toward customer service, accountants and administrative professionals who perform a variety of duties. However, the tests created to determine who is exempt in a 1938 U.S. economy are difficult to apply to our modern workforce.

Changes to the FLSA's overtime regulations regarding exempt and nonexempt status were made in 2004, ostensibly to help modernize the regulations. However, the regulations continue for the most part to contain generalized guidelines, which can be challenging to apply on a case-by-case basis.

A LOT AT STAKE FOR EMPLOYERS, EMPLOYEES AND GOVERNMENT

The issue of employee misclassification is not simply an annoying administrative issue that causes headaches and paperwork. At the core of employee misclassification, for all involved—employers, employees and the government—is money, and lots of it. The amount at issue in private employee misclassification litigation is startling; consider that in 2012, Walmart paid some \$5.3 million in a dispute over overtime related to vision center managers and asset protection coordinators, and, in the same year, a pharmaceutical manufacturer settled a class action lawsuit related to alleged employee misclassification for \$99 million (an

admitted outlier in settlement size).

These cases continue to play a growing and dominant role in FLSA wage-and-hour litigation. According to NERA Economic Consulting, from January 2007 to September 2013, overtime and misclassification cases comprised some 57 percent of all wage-and-hour settlements. And even the first month of 2014 has proven to be more of the same. The Jan. 10 conditional certification in the Lowe's case is in keeping with other recent settlements and decisions highlighting the upward litigation trend in this area:

- On Jan. 23, RBS Citizens N.A. agreed to a \$3 million class action settlement with a class composed of mortgage loan officers who alleged they were misclassified as exempt.

- On Jan. 9, several retail sales representatives of Kellogg Co. in various states across the country who alleged that they were misclassified as exempt were granted conditional certification under the FLSA. The class also includes territory managers and sales representatives (direct store delivery).

- On Jan. 2, an Ohio federal judge gave preliminary approval to a \$7 million class action settlement between PNC Bank N.A. and a class composed of mortgage loan officers, who had alleged they were misclassified as exempt.

CONCERN MAY DEPEND ON INDUSTRY, BUT NOT ON SIZE

NERA Economic Consulting notes that the top industries in terms of total settlement dollars related to FLSA wage-and-hour claims include retail, financial services/insurance, health care/health care services, food/food services, and technology, among others. This is not surprising given each of these industries are predominantly service-based.

Notwithstanding the large employers of the world, employee misclassification is by no means just a big-company issue. While organizations with thousands of employees have proven to be the easiest and most profitable to pursue thus far, both the government and plaintiffs bar have their sights set squarely on those they view as offenders among small and medium-sized businesses as well. While

smaller companies face less exposure when measured by gross numbers than larger businesses, the implications likely are far more dire for small and medium-sized organizations. And given that the FLSA allows for individual as well as corporate liability, for closely held businesses, this means that the owners, not just the company, could be at significant financial risk.

Proactive employers have begun to take steps to mitigate the financial and organizational risks posed by employee misclassification.

This scenario came true for an Ohio-based cable installer, Cascom Inc., which was found to have misclassified its cable installers as independent contractors, and ordered to pay approximately \$1.5 million in back wages and liquidated damages in 2011. As the company was no longer operating at the time of the judgment, its owner was pursued by the DOL (which had filed the lawsuit on behalf of the employees) for the damages. For small and medium-sized businesses, these settlements are not just a hit to the bottom line, they can mean losing a business, a house and personal assets.

STEPS TO TAKE TODAY

Not surprisingly, proactive employers have begun to take steps to mitigate the financial and organizational risks posed by employee misclassification. This includes the largest health care systems and hotel chains in the country, down to the owners of local lawn care services and corner restaurants.

While an inclusive audit of wage-and-hour practices and policies is the best way to ensure that classifications are accurate and up to date, here are some things that all companies

should consider doing today:

- **Review and update job descriptions.** Many times, employee job descriptions either are outdated or do not fully reflect the true nature of employee duties. Employee job descriptions should be reviewed and revised to the extent appropriate. Once any necessary revisions are made to job descriptions, employees should then be presented with job descriptions at regular intervals (typically during annual reviews) and asked to sign off on them. Such contemporaneous documentation can be extremely helpful down the road to the extent that employees challenge the nature of their job duties in misclassification litigation.

- **Analyze current exemption statuses.** Review current exempt and nonexempt employee classifications with a critical eye, and with special focus on those positions that may be close to the line. Carefully consider whether reclassification or other job restructuring may be warranted.

- **Make changes, under attorney-client privilege.** Make any necessary changes with care (and with consideration as to how to mitigate against the risk of litigation attendant with any reclassification), doing so under the ambit of attorney-client privilege to prevent disclosure of the process in any potential wage-and-hour litigation in the future.

Misclassification litigation has challenged and continues to challenge employers. However, armed with the right tools to proactively address this area of increasing exposure, employers can work to try to prevent this type of litigation from happening to them. •