Common Wage and Hour Problems

As Identified by the US Department of Labor

The United States Department of Labor (USDOL) is responsible for the enforcement of the federal Fair Labor Standards Act (FLSA). During an audit of an employer’s workplace, some of the more frequent problems identified by the USDOL include:

### Exempt/Non-Exempt Misclassification Issue:

 All employees under the FLSA are classified as either “exempt” or “non-exempt.”   The vast majority of employees are classified as “non-exempt” under the FLSA, which means they must be paid minimum wage for every hour worked, plus overtime for all time worked in excess of 40 hours in a given workweek.

A small minority of employees are classified as “exempt,” which means that they generally do not have to be paid minimum wage or overtime, but they do have to be paid a minimum weekly salary of $455.  To be classified as “exempt” an employee generally must fall into one of the white collar categories (e.g., professional, administrative, executive, outside sales, or computer person).  For example, lawyers are usually classified as “exempt” professional employees, and an Executive Director is usually classified as an “exempt” executive employee.[[1]](#footnote-1)

If an employer misclassifies an employee as “exempt,” when he/she is actually non-exempt, then the employer faces significant back wages, fines and other penalties.

### Independent Contractor Misclassification Issue:

To assess whether an individual is properly classified as an independent contractor (IC), the USDOL will review the totality of the circumstances. Among the factors which the USDOL considers relevant include:

1. The extent to which the services rendered are an integral part of the principal's business.
2. The permanency of the relationship.
3. The amount of the alleged contractor's investment in facilities and equipment.
4. The nature and degree of control by the principal.
5. The alleged contractor's opportunities for profit and loss.
6. The amount of initiative, judgment, or foresight in open market competition with others required for the success of the claimed independent contractor.
7. The degree of independent business organization and operation.

See [USDOL Fact Sheet 13](http://www.dol.gov/whd/regs/compliance/whdfs13.pdf). Many employers wrongly assume that by calling a worker a “consultant” and entering into a written independent contractor agreement with this consultant that they have automatically satisfied the IC test. However, this is not accurate. The law assumes that if an individual is performing work for an employer then the individual is working as an employer rather than as an IC. In order to properly classify an individual as an IC in terms of the USDOL, then all of the above factors should be satisfied.

If an individual has been misclassified as an IC, then the employer may be required to pay back wages for failing to comply with the minimum wage and overtime obligations of the FLSA, along with potential civil and criminal penalties and fines.

### Unpaid Interns:

The FLSA presumes that all employees will be paid for their work. Whether an intern is in fact an employee – and thus entitled to minimum wage and overtime – has not been an easy question to answer.  Courts have applied both a six-factor test promulgated by the USDOL, as well as a more general “primary beneficiary” test that asks whether the benefits of the internship accrue more to the intern than to the employer.  See [USDOL Fact Sheet #71](http://www.dol.gov/whd/regs/compliance/whdfs71.htm). Recently, a federal district court in New York ruled that workers were misclassified as unpaid interns on the movie set of the Black Swan. This decision has resulted in a wave of claims and litigation for back wages on this issue. The Black Swan decision has been appealed to the U.S. Court of Appeals for the Second Circuit, and a decision is expected in the near future, which may help clarify the parameters of unpaid internships for employers. In the meantime, employers should exercise extreme caution whenever classifying an individual in an “unpaid intern” status.

### Overtime Miscalculations:

Most employers understand their obligation to pay overtime at 1 ½ times an employee’s regular rate for all hours worked in excess of 40 in a given 7-day workweek. Employers struggle, however, when the math gets tricky, such as when employees work at different rates of pay during the 7-day period, or there is a tip credit involved. Employers should anticipate these issues in advance and work through the FLSA-approved methods for calculating overtime in these scenarios. See [USDOL Fact Sheet 23](http://www.dol.gov/whd/regs/compliance/whdfs23.pdf).

### Record-keeping requirements

The FLSA requires that employers keep certain time and payroll records for non-exempt employees. The USDOL has provided that an employer must maintain the following records:

1. Employee’s full name and social security number.
2. Address.
3. Birth date, if younger than 19.
4. Sex and occupation.
5. Time and day of week when employee’s workweek begins.
6. Hours worked each day.
7. Total hours worked each workweek.
8. Whether the employee is paid on an hourly, salary, or fee basis.
9. Regular hourly pay rate.
10. Total daily or weekly straight-time earnings.
11. Total overtime earnings for the workweek.
12. All additions to or deductions form the employee’s wages.
13. Total wages paid each pay period.
14. Date of payment and pay period covered by the payment.

The USDOL further provides that for a period of three (3) years, an employer must preserve payroll records. Similarly, records on which wage computations are based, time cards, wage rate tables, records of additions to or deductions from wages, and work and time schedules need to be retained for two (2) years. See [USDOL Fact Sheet 21](http://www.dol.gov/whd/regs/compliance/whdfs21.pdf).

1. A common misconception is that payment of a salary results in exemption from the overtime requirements of the FLSA. As discussed above, in order to be exempt from the overtime requirements, an employee must be paid on a salary basis and the employee’s job responsibilities must also fall within one of the exempt categories. [↑](#footnote-ref-1)