

HR COMPLIANCE OVERVIEW



Best Practices for Reducing Wage and Hour Claims

Wage and hour claims are a common source of legal challenges for employers. With ever-evolving laws and regulations, employers must stay vigilant to ensure compliance with wage and hour laws. Even unintentional violations can lead to costly lawsuits, penalties, reputational damage and employee dissatisfaction. Implementing effective practices can help employers reduce the likelihood of wage and hour claims, safeguard their business, and foster a fair and transparent workplace.

The following are effective practices that can help employers manage wage and hour issues effectively and reduce potential claims and legal risks:

- Classifying employees correctly;
- Paying employees properly;
- Developing clear and consistent workplace policies;
- Conducting regular training;
- Ensuring accurate recordkeeping; and
- Addressing employee complaints promptly.

This HR Compliance Overview provides employers with best practices for reducing wage and hour claims.

ACTION STEPS

Employers should carefully consider their obligations and potential legal or business risks when implementing new workplace practices. This Compliance Overview provides best practices for employers to reduce wage and hour claims by ensuring compliance with legal requirements.

Highlights

Employers can consider the following practices to help reduce wage and hour claims:

- Classify employees correctly;
- Pay employees properly;
- Develop clear and consistent workplace policies;
- Conduct regular training;
- Ensure accurate recordkeeping; and
- Address employee complaints promptly.

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Overview of Wage and Hour Laws

Employers must comply with the varied and complex requirements of wage and hour laws. These laws change frequently, making compliance an ongoing challenge for employers. That's why it's important that employers familiarize themselves with these laws and review them regularly to ensure their businesses stay compliant.

The Fair Labor Standards Act (FLSA) regulates the wages and hours of most U.S. employees. The FLSA's key provisions include the following:

- **Minimum wage**—Employers must pay employees at least the federal minimum wage, which is \$7.25 per hour. However, the FLSA provides various exceptions to minimum wage requirements under specific circumstances (e.g., workers with disabilities, full-time students, student workers, tipped employees and workers under age 20). States and municipalities may have higher minimum wage requirements that employers must comply with;
- **Overtime pay**—Employers must pay covered, nonexempt employees overtime wages—at a rate of 1.5 times their regular rate of pay—for all hours worked in excess of 40 hours in a workweek unless they qualify for an exemption;
- **Minimum wage and overtime pay exemptions**—The FLSA provides several exemptions for minimum wage and overtime pay requirements. The most common exemptions are known as the “white-collar” exemptions, which apply to workers in certain executive, administrative, professional, outside sales and computer-related occupations, as well as certain highly compensated employees. In general, employees must be paid on a salary basis at a rate at least equal to the salary threshold to qualify for the exemption and perform duties that the FLSA assigns to the exemption;
- **Employee classification**—For a worker to be protected by the FLSA, the worker must be an employee, meaning the worker has an employment relationship with an employer. Independent contractors are not entitled to FLSA protections. An individual is typically an employee if they perform services for an organization that controls what work must be done and how it should be completed. On the other hand, an individual is typically an independent contractor if the employer has the right to control or direct only the result of the work and not what will be done or how it will be done;
- **Child labor**—The FLSA restricts the hours that 14- and 15-year-old minors can work and the types of work minors under the age of 18 can perform; and
- **Recordkeeping**—Employers must maintain accurate records of all hours worked and wages earned by employees. While the FLSA does not require these records to be kept in any particular format, employers must ensure they include specific information regarding employees, hours worked and wages earned.

The U.S. Department of Labor's (DOL) Wage and Hour Division (WHD) enforces federal minimum wage, overtime pay, recordkeeping and child labor requirements of the FLSA. Generally, the WHD will initiate an audit after a current or former employee files a complaint or during a routine investigation. A WHD auditor will visit an organization to conduct interviews, examine time clocks and ensure that all employment notifications are available to employees. The auditor will also review up to three years of wage and hour records to determine whether there are any violations in an employer's payroll practices.

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In addition to complaints, the WHD selects certain businesses and industries for investigation. For example, the WHD often targets low-wage industries due to high rates of violations, the employment of vulnerable workers and rapid industry changes, such as growth or decline. Occasionally, several organizations in a specific geographic area will be examined.

Many states and municipalities have enacted wage and hour laws that provide additional protections beyond federal requirements. These laws may include higher minimum wage rates or more generous overtime requirements. Employers should familiarize themselves with federal, state and local laws to ensure full compliance.

Wage and hour violations can result in significant penalties, including unpaid overtime, civil fines and other damages. Examples of common minimum wage and overtime violations include:

- Misclassifying employees as exempt;
- Misclassifying employees as independent contractors;
- Paying workers less than the minimum wage;
- Refusing to pay unapproved overtime;
- Paying employees straight-time rates for overtime hours;
- Miscalculating employees' wage rates;
- Failing to compensate employees for pre- and post-shift activities, such as mandatory meetings or trainings;
- Withholding tips;
- Automatically deducting meal and rest breaks from employees' weekly work hours;
- Offering employees compensatory time off in lieu of overtime;
- Allowing employees to waive their right to overtime;
- Requiring workers to work off the clock without compensation; and
- Improper wage deductions for uniforms, tools, meals or other work-related expenses.

Avoiding wage and hour violations is not always easy. Due to the complex nature of employment laws, compliance is an ongoing challenge for employers. However, by establishing best practices to address and reduce potential wage and hour violations, employers can keep their businesses compliant and their workers satisfied.

Best Practices for Reducing Wage and Hour Claims

Classify Employees Correctly

One of the most widespread wage and hour issues stems from incorrect employee classification. Under the FLSA, employers typically encounter two main challenges when classifying employees. First, employers must avoid misclassifying employees as independent contractors. Second, certain employees may be exempt from the FLSA's wage and hour provisions, including executive, administrative, professional and outside sales employees. These exemptions have specific criteria that employers must carefully evaluate to determine whether an exemption applies. In both instances, failing to properly classify can lead to costly legal violations.

Employee Versus Independent Contractor

Whether a worker is covered by a particular wage and hour law often depends on whether the worker is an employee or independent contractor. However, classifying an individual as either an employee or an independent contractor is not a simple task. Employers must determine the true nature of their relationships with their workers in order to properly classify them.

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For a worker to be protected by the minimum wage and overtime pay requirements of the FLSA, the worker must be an employee, meaning that there is an employment relationship between the worker and employer. Independent contractors do not have these protections. Whether a worker is an employee or an independent contractor under the FLSA is determined by looking at the economic realities of the worker's relationship with the employer. If the economic realities show that the worker is economically dependent on the employer for work, then the worker is an employee. If the economic realities show that the worker is in business for themselves, then the worker is an independent contractor. The economic realities of the entire working relationship are looked at to decide whether a worker is an employee or an independent contractor.

The **economic reality test** outlines several factors an employer may consider to determine the level of financial dependency. Under this test, one factor standing alone is not sufficient to establish dependency, but as a whole, these factors enable the employer to evaluate the nature of an employment relationship. These factors evaluate:

1. The degree of the employer's right to control the manner in which work is performed;
2. The degree of skill required to perform the work;
3. The worker's investment in the business;
4. The permanence of the working relationship;
5. The worker's opportunity for profit or loss; and
6. The extent to which the work is an integral part of the business.

Accurate worker classification requires employers to evaluate the economic reality factors when determining a worker's status for FLSA purposes. Employers can learn more by reviewing the DOL's [FLSA reference guide for employers](#).

In addition to the economic reality test, employers must be aware of state and local variations of these tests that may apply in certain situations.

Exempt Versus Nonexempt Employee

The FLSA provides minimum wage and overtime pay protections to most employees. Employees generally must be classified as nonexempt and, therefore, be eligible for such minimum wage and overtime protections unless they meet the criteria to be classified as exempt from minimum wage and overtime requirements. Typically, only employees in certain positions who meet certain salary and job duties criteria set forth under the FLSA may qualify for an exemption. Misclassifying employees as exempt when they are nonexempt is a frequent pitfall and can often be a costly mistake for employers, leading to expensive legal actions and penalties.

The FLSA provides several exemptions from the minimum wage and overtime pay requirements, the most common of which are the **white-collar exemptions**, which generally apply to employees in executive, administrative, professional, outside sales and computer-related occupations and certain highly compensated employees. To qualify for most white-collar exemptions, an employee must satisfy the following tests:

- The **salary basis** test requires that the employee is paid a predetermined and fixed salary that does not fluctuate based on the quality or quantity of work;
- The **salary-level test** requires that the employee meets a minimum specified amount to qualify for the exemption. However, outside sales personnel and certain other professions, including doctors, lawyers and teachers, are not subject to the salary level test; and

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- The **duties test** requires that an employee's actual work responsibilities match the description the FLSA assigns to the exemption. Highly compensated employees are subject to a less restrictive duties test.

Simply paying an employee salary does not relieve an employer of minimum wage and overtime obligations to that employee. Unless the employee meets all the criteria for a specific exemption, an employee covered by FLSA protections who is paid a salary is still due overtime pay if they work more than 40 hours in a week.

Employers can avoid common employee misclassification mistakes by taking the following steps:

- **Identify whether the employee meets the salary basis.** To qualify for an FLSA white-collar exemption, an employee must be paid on a salary basis. This means that an employee regularly receives a predetermined amount of compensation each pay period on a weekly or less frequent basis. The predetermined amount cannot be reduced because of variations in the quality or quantity of the employee's work. If an employer makes deductions from an employee's predetermined salary, the employee is not paid on a salary basis and may be entitled to overtime compensation. However, administrative, professional and computer employees may be paid on a fee basis rather than a salary basis;
- **Determine whether the employee meets the salary level test.** To satisfy the salary level test, an employer must pay an employee at least **\$684 per week** (or **\$35,568 per year**) for an executive, administrative or professional employee or **\$107,432** per year if the employee is a highly compensated employee;
- **Evaluate the employee's job duties and responsibilities.** The employee's job duties must primarily involve those associated with executive, administrative, professional, outside sales or computer employees. To satisfy the duties test, an employee's actual work responsibilities must match the description the FLSA assigns to each exemption. This analysis requires a more thorough evaluation of whether an employee can be classified as an executive, administrative, professional, outside sales or computer employee, or a highly compensated employee; and
- **Consider additional exemptions.** The FLSA's minimum wage and overtime exemptions are narrowly defined. Employers should be sure to carefully check the exact terms and conditions for each exemption.

Pay Employees Properly

The FLSA requires employers to pay their employees for all hours required or permitted to work. Failing to pay nonexempt employees at least the federal or state-mandated minimum wage, whichever is higher, for all hours worked and overtime pay—at a rate of 1.5 times the employee's regular rate of pay—for every hour they work over 40 during a workweek is one of the most common sources of wage and hour violations.

Minimum Wage Exemptions

Some employees are not subject to the FLSA's minimum wage requirements. Employers must carefully consider the exact terms and conditions for each exception to determine whether an employee meets one of the FLSA's narrowly defined exemptions. The following examples are an illustrative, but not all-inclusive, list of employees exempt from the federal minimum wage:

- Agricultural employees that are immediately related to their employers, are hand harvest laborers, work for employers that use more than 500 man-days of labor in any quarter of the previous calendar year, or work in the range production of livestock;
- Bona fide executive, administrative and professional employees (including teachers and academic administrative personnel in elementary and secondary schools);

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- Babysitters and companions for the elderly whose employment is casual and who provide services for individuals who are unable (because of age or infirmity) to care for themselves;
- Computer system analysts, programmers, engineers and similarly skilled workers with wages of at least \$27.63 per hour and whose primary duty is to apply system analysis techniques and procedures, consult with users, or determine, design, develop, document, analyze, create, test or modify hardware, software or system functional specifications;
- Domestic service employees whose compensation is not classified as wages under the Social Security Act or who work for less than eight hours in a workweek;
- Newly hired employees under age 20 during the first 90 consecutive calendar days following their hiring date (as long as the employer does not fully or partially displace other employees' work hours or benefits to accommodate new hires);
- Newspaper delivery and publication employees when the newspaper has a circulation of less than 4,000 and its major circulation is within the county (or contiguous counties) where the paper is published;
- Crew members and seamen working on foreign vessels;
- Amusement park and recreational establishment employees working for a park that operates for up to seven months in a year or earns at least two-thirds of its total annual income in a six-month period (including individuals working for organized camps and religious and nonprofit educational conference centers);
- Criminal investigators receiving availability pay (compensation provided for unscheduled services beyond the investigator's 40-hour workweek in activities that require irregular or unscheduled work hours);
- Seafood processing employees (individuals employed in canning, catching, cultivating, farming, harvesting, packing, processing, propagating, or taking of any kind of fish, shellfish, crustaceans, sponges, seaweeds, and other aquatic forms of animal and vegetable life); and
- Switchboard operators working for an independently owned public telephone company having no more than 750 stations.

Additionally, the FLSA allows employers to hire students, student-learners, apprentices, messengers and disabled individuals at rates below the minimum wage rate. The FLSA also includes a special provision for tipped employees.

Compensable Time

Employers must pay employees for all time during which an employee performs productive work and all hours the employee remains available for their next assignment. However, employers do not need to pay employees for time when they are relieved of their duties and free to pursue their own interests. Employers must also track the number of compensable hours employees work during a workweek. To determine how much of an employee's time is compensable, employers must carefully consider whether their employees must receive wages for waiting time, on-call time, sleeping time, travel time, rest and meal periods, nursing breaks or attending lectures, meetings and training periods.

Calculating an Employee's Wage Rate

Understanding how to calculate an employee's rate of pay is essential for avoiding wage and hour violations. Under the FLSA, an employee's regular rate of pay is the average compensation an employee receives for every hour the employee worked during a workweek. To calculate an employee's regular rate of pay, the employer must divide the employee's total wages for a workweek by the number of hours the employee actually worked during that workweek. A workweek is a fixed and regularly recurring period of 168 hours or seven consecutive 24-hour periods. Employers may not average the hours an employee works during one workweek with the hours the employee works during other weeks. An employee's

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total wages may also be determined on a piece rate, salary, commission or some other basis. For salaried employees, employers should divide the salaried employee's weekly salary by the number of hours they are expected to work (usually 40) to determine their hourly rate.

Additionally, an employer must include all forms of compensation given to or paid on behalf of the employee when calculating an employee's wage rate, except for the following:

- Additional compensation for overtime hours, holiday hours or work that falls outside of a schedule set by an employment contract or collective bargaining agreement;
- Compensation for paid time off (such as vacation, illness, holidays and production downtimes);
- Gifts, discretionary bonuses and monetary awards that are not measured by hours worked, productivity or efficiency;
- Irrevocable employee benefit contributions (such as life insurance, health benefits and retirement accounts);
- Value or income derived from an employer-provided grant; and
- Value or income from stock option rights or stock appreciation and bona fide stock purchase programs.

The following strategies can help employers ensure they are properly paying employees:

- Determine whether employees are exempt from minimum wage and overtime requirements;
- Know the regular and overtime pay rates for each nonexempt employee;
- Track employee work hours accurately; and
- Pay wages promptly.

Develop Clear and Consistent Workplace Policies

A clear set of wage and hour policies and procedures can establish the framework for how an employer operates, which is critical to prevent misunderstandings with workers that could eventually become costly wage and hour claims. By developing workplace policies that address common wage and hour violations, such as work hours, breaks and overtime, and consistently enforcing them, employers can help mitigate risks and potential violations. When these policies are communicated plainly, employees are more likely to follow guidelines and avoid confusion.

Communicating policies regularly to employees can also help reduce potential wage and hour claims by educating employees on how wages are calculated, overtime rates, deductions and timing of payments. Employers can do this by including wage and hour policies in their employee handbooks or another central place where employees can access and review information.

Examples of best practices for developing wage and hour policies include the following:

- **Set clear work hours.** Employers can prevent wage and hour claims by defining the regular hours employees are expected to work and communicating how they will handle requests for schedule changes or extra hours. Establishing a consistent workweek can also help employers calculate employee wage rates and overtime correctly. With the rise of remote work, employers may need to establish additional guidelines for work performed off-site or at irregular times by remote employees;
- **Define key wage and hour terms.** To avoid potential misunderstandings, employers can clearly define important terms and concepts, such as "workweek," "regular working hours" (e.g., 9 a.m. to 5 p.m., Monday to Friday), "overtime hours," "on-duty time," "on-call time," and "exempt and nonexempt employees";

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- **Outline time tracking expectations.** Employers can explain how employees are expected to track their hours, such as using time clocks, manual time logs or mobile apps. This can help ensure that all hours employees work are accurately tracked and accounted for; and
- **Clarify break times.** Employers should establish clear policies regarding paid and unpaid breaks, lunch hours and how employees should record this time on their timesheets. This can help prevent confusion among workers and reduce potential violations.

Since wage and hour laws can change frequently, workplace policies should be reviewed and updated regularly. Doing so can help ensure continued compliance with legal requirements.

Conduct Regular Training

Many wage and hour violations are preventable. However, employers cannot ensure compliance with wage and hour regulations unless managers and employees are aware of applicable laws and follow them. Effective training can improve an organization's compliance efforts by ensuring managers and employees recognize applicable laws and regulations, identify compliance concerns and issues, and report compliance issues properly. For example, training employees to follow proper time clock procedures can help employers to accurately track their workforce's working hours.

Managers are often on the front lines of implementing and enforcing an organization's wage and hour policies. If these individuals are not well trained, it can easily lead to costly violations. Manager training can cover topics such as overtime eligibility, employee classification (e.g., exempt versus nonexempt employees) and timekeeping practices. Additionally, employers can train supervisors to avoid practices that may lead to costly violations, such as pressuring employees to work through breaks or off the clock.

Ensuring employees are properly trained can drastically improve an organization's wage and hour compliance efforts. At a minimum, employers should train employees at the time of hire and every year thereafter. In addition to regular training, providing employees with guides and resources can help improve their knowledge regarding wage and hour regulations and workplace policies and enhance organizational compliance.

Ensure Accurate Recordkeeping

Proper recordkeeping is a critical component in reducing potential wage and hour claims. Under the FLSA, employers are legally required to maintain certain records for each nonexempt employee. While the FLSA does not require employers to keep these records in a particular form, it does require that the records include certain identifying information about the employee and data about the hours worked and the wages earned. The law requires this information to be accurate. Employers must maintain the following records for each nonexempt employee:

- Full name;
- Social Security number;
- Address, including zip code;
- Date of birth if the employee is younger than 19 years old;
- Sex, which can be identified by a gender-specific prefix (e.g., Mr., Mrs., Miss or Ms.);
- Occupation;
- Time of day and day of the week the employee's workweek begins;
- Total hours worked each workday;
- Total hours worked each workweek;
- Basis on which the employee's wages were paid (e.g., per hour, per week or piecework);

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- Regular hourly pay rate;
- Total daily or weekly straight-time earnings;
- Total overtime earnings for the workweek;
- All additions to or deductions from the employee's wages each pay period, including dates, amounts and nature of any additions or deductions;
- Total wages paid to the employee each pay period; and
- Date of payment and workweek or work period covered by the payment.

Employers must maintain payroll records, collective bargaining agreements, and sales and purchase records for at least three years and records on which wage computations are based (e.g., time cards, wage rate tables, work and time schedules, piece work tickets, and records of additions to or deductions from wages) for two years. These records must be open for inspection by the WHD's representatives and may be kept at the place of employment or in a central record office. Failing to maintain accurate records not only invites legal scrutiny but may also make it harder to defend against potential wage claims.

Employers can do the following to ensure accurate recordkeeping:

- **Track hours worked.** To comply with wage and hour laws, employers must accurately track employee hours. By adopting reliable time-tracking systems, organizations can better ensure they maintain accurate time records and reduce the chances of errors. These systems can help to accurately capture when employees clock in and out;
- **Maintain detailed records.** Accurate records can help employers avoid potential wage and hour violations. Employers should keep records of hourly rates, overtime payments, bonuses, deductions, employee breaks, total hours worked and any other required compensation details. Employers should also ensure that these records reflect the correct term when referring to each worker (e.g., "employee" as opposed to "independent contractor") and job titles;
- **Provide employees with access to time records.** Another way employers can ensure their time records are accurate is by providing employees with access to their time records. Providing employees with access to time records can aid employers in identifying and correcting errors;
- **Retain records for the required period.** Employers can remain compliant with wage and hour recordkeeping requirements by understanding how long records must be maintained. According to the FLSA, payroll records must be kept for at least three years, and records related to wage computations must be kept for two years; and
- **Review wage and hour records.** Regularly reviewing and auditing records can help employers identify potential wage and hour issues and address them before they turn into expensive legal matters. Auditing payroll processes, employee classification, and organizational compliance with wage and hour requirements can help employers stay on the right track and one step ahead.

Address Employee Complaints Promptly

Despite an organization's best efforts to comply with wage and hour laws, employers may still be subject to employee complaints. Taking employee wage and hour complaints seriously and resolving issues quickly can prevent internal complaints from becoming formal legal actions. Importantly, this can help employers reduce the risk of the same wage and hour issues reoccurring in the future.

Employers should encourage employees to report any wage and hour issues by establishing a clear reporting process. After receiving an employee complaint, it's important that employers investigate the issue thoroughly. This may include

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collecting relevant information and documents and interviewing employees. Once an investigation is completed, employers should implement corrective action to resolve any issues promptly. For example, if a wage payment mistake is discovered, employers should correct it immediately. After resolving any potential issues, employers can communicate the findings to the employee who raised the issue. After resolving the complaint, employers may need to update their policies and procedures and provide employees with additional training to prevent future instances of noncompliance. In some situations, it may be necessary or prudent to report the incident of noncompliance to the appropriate government agency.

By addressing wage and hour complaints promptly, employers not only reduce the risk of legal and financial issues but also build a stronger, more trusting relationship with their employees. An effective corrective action plan should facilitate the organization's overall wage and hour compliance goals. This includes identifying the cause of the issue, implementing steps to correct the issue in a timely manner, reducing the risk of the issue reoccurring in the future and establishing accountability.

Employer Takeaways

Complying with wage and hour regulations is a significant challenge for many organizations. Even inadvertent errors can be costly, both financially and reputationally. However, by implementing effective wage and hour practices, employers can significantly reduce their risk and help stay compliant with wage and hour laws. Employers can prevent many common issues that lead to wage and hour claims by classifying employees properly, paying wages correctly and maintaining accurate records. Regular training, clear policies and staying up to date on changes in the law are also successful strategies to ensure compliance and maintain a positive workplace. Establishing best practices to reduce wage and hour claims can enable employers to foster a culture of compliance that can not only help organizations avoid potential liabilities but also build trust and morale among their workforce, contributing to a more productive and harmonious work environment.