

# Misclassification of workers and unpaid overtime

## The next litigation gusher

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Federal and state laws governing overtime are a minefield for employers. “Wage and hour lawsuits are rising, outpacing all other types of workplace class actions” with “the 10 largest private wage and hour settlements totaling \$364 million” in 2009, according to an article in *The Kiplinger Letter*. In 2008, Wal-Mart Stores, Inc. agreed to pay between \$352 million and \$640 million to settle 63 wage and hour lawsuits filed in 42 different states. These kinds of cases can be extremely lucrative for the lawyers filing them. And now, jumping on the bandwagon are plaintiff lawyers who are starting to pursue claims against energy companies.

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hour violations can be brought on behalf of individuals or on behalf of large groups of similarly situated employees. Because many oilfield workers are highly compensated and work significant hours, exposure for wage violations can be very large.

Companies that employ field service engineers, mud engineers, tool pushers, field service technicians and other field service workers typically pay them on a fixed salary, day rate, or per job basis (or some combination thereof) regardless of the number of hours worked per day or per week. Although many service companies don’t pay overtime when these

workers work more than 40 hours, many of these workers may actually be owed overtime under state and federal law. It is not a defense that your competitors pay their people the same way you do.

### **State or federal law?**

Overtime obligations are typically governed by state and federal law. The federal Fair Labor Standards Act (“FLSA”) sets minimum standards with respect to minimum wage and overtime. The FLSA presumes that employees are entitled to payment of overtime for hours worked in excess of 40 in a week at a rate not less than one and one-half times each employee’s

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"regular rate" unless the employer can prove otherwise. States can enforce their own wage payment laws as long as they provide for at least the same protections as the FLSA. For example, some states (like California) require payment of overtime after eight hours worked in a day and mandatory break time. When addressing your pay practices, you must consider and comply with state and federal law.

**Who is exempt and who is not?**

Not all employees are entitled to overtime wages. Certain categories of workers can be "exempt" from overtime. The categories of workers who are exempt tend to be either industry specific or defined by the duties and responsibilities of the employee. Some industry specific exemptions are seamen working on particular vessels, and drivers,

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mechanics and helpers subject to Department of Transportation oversight. Other employees may qualify as exempt based on their duties, including certain executive, administrative, and professional employees; outside salesmen; and certain computer systems analysts, computer programmers, and software engineers — the so-called "white-collar" exemptions.

The white-collar exemptions, which are most commonly implicated in the misclassification of oilfield workers are the "executive," "administrative," and "professional" exemptions. These exemptions generally do not apply to manual laborers (i.e. workers who perform repetitive operations with their hands that

involve physical skill and energy) or to non-management employees in production, maintenance, construction and similar occupations such as technicians, carpenters, electricians, mechanics,

welders, inspectors, craftsmen, operating engineers, longshoremen, construction workers and laborers.

To qualify for the three primary white-collar exemptions under the FLSA, an employee must be paid a minimum salary of at least \$455 per week (\$23,660 per year) and the employee's primary duty must consist of qualifying exempt work. A primary duty is one that occupies the major part of an employee's work time. Exempt status may be

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harder to establish under some state laws. For example, California law requires employees to devote more than half of their work time to exempt duties in order to qualify as exempt.

Being paid on a salary basis means the employee receives a fixed amount of compensation each pay period on a weekly or less frequent basis. This fixed salary cannot be reduced because of variations in the quality or quantity of the employee's work. Subject to certain exceptions, a salaried employee must be paid in full for any week in which the employee performs any work, regardless of the number of days or hours worked. Docking a properly exempt employee's salary for hours or days not worked or for deficiencies in the quality of work can destroy the exemption and expose the company to overtime liability.

#### **The executive exemption**

In addition to receiving a fixed salary, an employee classified as an exempt "executive" must: (1) manage an enterprise or a customarily recognized department or subdivision of an enterprise; (2) customarily and regularly

direct the work of at least two or more full-time employees or their equivalent (e.g. four half-time employees equal two full-time employees); and (3) have authority to hire or fire other employees or, alternatively, effectively recommend hiring, firing, promotion, or other changes in employee status.

Managing an enterprise includes, but is not limited to, interviewing, selecting, and training employees; setting and adjusting rates of pay and hours of work; directing the work of employees; handling

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employee complaints; disciplining employees; planning the work; determining the material, tools, and techniques to be used; apportioning work among employees; planning and controlling the budget; and providing for the safety and security of employees or property.

#### **The administrative exemption**

In addition to receiving a fixed salary, an employee classified under the "administrative" exemption must perform office or non-manual work directly related to the management or general business operations of the employer or the employer's customers, and exercise discretion and independent judgment with respect to matters of significance. Work directly related to management or general business operations includes work in such areas as tax, finance, accounting, budgeting, auditing, insurance, quality control, purchasing, procurement, advertising, marketing, research, safety and health, personnel management, human resources, employee benefits, labor relations, public relations, government relations, computer network and database administration, and legal and regulatory compliance. In general, the exercise of discretion and independent judgment involves comparing and evaluating possible courses of conduct and acting or making decisions after the various possibilities have been considered. The term implies that the employee has authority to make an independent choice, free from immediate direction and supervision. Factors to consider include whether the employee has authority to formulate, affect, interpret, or implement management policies or operating procedures; carries out major assignments in conducting the operations of the business; performs work that affects business operations to a substantial degree; has authority to commit the employer in matters that have a significant financial impact on the business; and has authority to waive or deviate from established policies and procedures without prior approval.

#### **The professional exemption**

In addition to receiving a fixed salary, an employee classified as an exempt "professional" must be a "learned professional," an "artistic professional," or a teacher. Only the learned professional classification ordinarily applies to oilfield workers. To qualify, an individual must perform work

requiring “advanced knowledge,” i.e., work that is predominantly intellectual in character and requires the consistent exercise of discretion and judgment, as distinguished from work involving routine mental, manual, mechanical, or physical work. The advanced knowledge must be in a field of science or learning and must be customarily acquired through a prolonged course of specialized intellectual instruction. Advanced knowledge cannot be gained at the high school level or just from routine work experience or training.

The phrase “field of science or learning” includes the traditional professions of law, medicine, accounting, actuarial computation, engineering, architecture, various types of physical, chemical, and biological sciences, and similar occupations that have a recognized professional status. Positions that involve the mechanical arts or skilled trades in which the knowledge may be of a fairly advanced type, but is not in a field of science or learning,

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don’t ordinarily qualify as exempt. Unless your company’s technicians and tool operators are all degreed engineers, it is likely they are not properly exempt from overtime.

**Calculating overtime wages**

Properly classifying employees as exempt or non-exempt is only half the battle. Once employees are properly classified, they have to be paid proper wages. This poses several potential traps. For example, the method for calculating overtime rates and the time when they kick in can vary between state and federal law.

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“regular rate” of pay. Under the FLSA, an employee’s regular rate is the hourly rate actually paid the employee for the normal, non-overtime workweek for which he is employed. If an employee is paid a day rate or a job rate without regard to the actual number of hours worked, then the regular rate is determined by totaling all compensation paid in the workweek and dividing by the total hours actually worked. If paid solely on a salary basis, an employee’s regular rate is typically computed by dividing his weekly salary by the number of hours (normally 40) that the salary is intended to compensate (not necessarily the

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hours actually worked). Payment of salary and a day/job rate may require using the total amount paid for both to calculate the regular rate.

Calculation of the regular rate of pay can vary by state. In California, the regular rate of pay is computed by dividing an employee's weekly compensation by 40 hours, even if the employee worked more than 40 hours that workweek. The result is that the regular rate of pay under California law may be greater than that under the FLSA when an employee works more than 40 hours in a workweek.

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Many companies unknowingly violate the law by not including all required amounts in their regular rate calculation. For example, non-discretionary bonuses (such as some job bonuses and production bonuses) must be included in the regular rate. Certain kinds of premiums must also be included in the calculation. When certain payments associated with work done in one week are paid in a later pay period, the company may be required to recalculate and apportion overtime retroactively. It can all be very confusing, and it is easy to make a mistake.

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example, California and Alaska require payment of overtime after eight hours worked in one day. California requires payment of double-time after 12 hours worked in a day; payment of overtime for the first eight hours worked on the seventh consecutive day in a workweek; and double-time for work beyond eight hours on the seventh consecutive day in a workweek. Colorado requires payment of overtime for hours worked in excess of 12 hours in one day. Kentucky requires payment of overtime for hours worked on the seventh consecutive day of work.

There are lots of other problems that can arise with respect to employee compensation, including issues relating to: (1) use of "independent contractors"; (2)

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waiting time, on-call time, travel time, and time spent preparing for and concluding work; (3) mandatory rest and/or meal periods; and (4) recordkeeping requirements.


**Carefully get your shop in order**

State and federal rules governing overtime are complex, inconsistent and hazardous to the unwary or uninformed. Proper classification of employees can be factually and legally complicated. If you are not confident that your company's compensation scheme could survive close scrutiny by an eager plaintiff's lawyer, you should seek assistance from an experienced lawyer you trust to audit your practices and ensure that they comply with applicable state and federal laws and regulations. Please note that use of a non-lawyer to audit pay practices ordinarily will not invoke the attorney-client privilege, which means communications about the audit could be discoverable and used against you in court. You could make a bigger mess for your company if you don't do it right. Proceed with caution. 🏠

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