

## Using Statistical Analysis For Employee Misclassification

*Law360, New York (August 01, 2013, 1:13 PM ET)* -- The U.S. Department of Labor's Wage and Hour Division (WHD) is expanding its enforcement of cases alleging that workers have been misclassified, while private plaintiffs also continue to pursue such cases. For companies facing these claims, the existence of abundant electronic data can provide information about employees' days and duties, and statistical analysis of this data can be a valuable tool for companies to respond to allegations of misclassification.

### Recent Developments in FLSA Exemption Cases

The growth in government enforcement has been spurred by the Obama administration's substantial increase in the size and budget of the Department of Labor's Wage and Hour Division over the past four years. The fiscal year 2014 WHD budget request (released in April 2013) reflects a nearly 40-percent increase in budget and staff over 2008 levels. With the WHD's continued focus on worker misclassification claims, the budget request includes funds specifically earmarked for increased investigations in this area.

Private civil litigation under the Fair Labor Standards Act also has increased significantly in recent years and includes cases alleging worker misclassification. According to the Public Access to Court Electronic Records, an electronic service providing case and docket information from U.S. district courts, FLSA filings reached a new high with 7,700 cases reported in 2012, almost four times as many cases as in 2001.

Claims specifically alleging misclassification of employees as exempt from overtime have posed a significant risk for employers. From 2007 through 2012, NERA's wage and hour settlement database of state and FLSA cases indicates that about 18 percent of settled wage and hour claims involved misclassification. A small fraction of these misclassification claims alleged misclassification of independent contractors, temporary workers or interns, but the bulk of claims alleged that the workers were misclassified as exempt from hourly wages.

The WHD has added to the risks, facing companies with workers classified as exempt by attempting to narrow the number of employees who qualify for such hourly wage exemptions. To date, the WHD's efforts have had mixed success.

- In the pharmaceutical industry, the U.S. Department of Justice intervened on the WHD's behalf in several cases (first with an amicus brief In re: Novartis Wage and Hour Litigation, 09-0437, in U.S. Court of Appeals for the Second Circuit and second before the U.S. Supreme Court in *Christopher, et al. v. Smithkline Beecham Corp.*, 11-204), arguing that pharmaceutical sales representatives did not qualify for exemption under either the outside sales or administrative exemption. In June 2012, the Supreme Court granted exempt status under the outside sales exemption, and the federal docket was purged of a significant number of cases from that industry. But the earlier amicus brief may have aided in the rush to a \$99 million settlement in Novartis on the eve of the Christopher ruling.
- In the financial industry, the WHD has targeted mortgage loan officers. In March 2010, the WHD filed an administrator interpretation (see Administrator Interpretation FLSA 2010-1) stating that mortgage loan officers did not qualify under the administration exemption as being exempt from overtime pay requirements, reversing a prior opinion letter (see Wage and Hour Opinion Letter FLSA 2006-31). The Mortgage Bankers Association (MBA) challenged the interpretation as having been issued without "notice and comment." On July 2, 2013, the D.C. Circuit Court overturned the lower court's order denying the MBA summary judgment and "remanded the case with instructions to vacate DOL's 2010 administrative interpretation" (*MBA v. Harris*, No. 12-5246, D.C. Cir. 2012). But the court made clear it was not commenting on the merits of the administrative interpretation, which the DOL could reissue in the future with appropriate "notice and comment rulemaking."

To assess extent of misclassification filings as well as the industries being targeted, NERA compiled data on new wage and hour cases reported in Law360 over the past three years. We found that pharmaceutical cases represented only about 12 percent of misclassification case filings, and, as expected, these filings ended with the Christopher decision.

But filings continue in the financial industry as well as other industries, with misclassification cases representing 35 percent of filings reported. The affected industries included the following:

- Retail: Were the activities of the managers sufficiently different from those of the hourly workers to qualify for an exemption?
- Telecommunications: Did technicians exercise discretion?
- Health care: Should nurses and other health care workers have been paid hourly instead of per visit?
- Transportation: Do on-road managers have discretion in their oversight duties, or are they bound by company guidelines?

Over the past three years, in addition to the pharmaceutical cases, 28 percent of exempt/nonexempt filings reported in Law360 came from the financial services industry, 16 percent came from the retail industry, and 44 percent came from other industries.

## Using Statistical Analysis in Exemption Cases

In light of the continuing WHD efforts to narrow the number of employees subject to FLSA exemptions, as well as private litigation related to misclassification, the capability to carefully evaluate misclassification claims remains an essential facility. Frequently, data exist that can help address the questions and issues raised in misclassification cases. These data sets may include phone records or other call records, computer log-in information, expense records or personnel records.

By analyzing these types of information, economists can make critical contributions to the understanding of a claim. Below, we discuss examples of contributions that could be made in addressing the appropriateness of class certification, the merits of claims relating to the exercise of discretion and/or managerial activity, potential damages and the identification of highly compensated employees not subject to exemption.

### ***Class Certification***

The first stage of the FLSA wage and hour case is provisional certification of an opt-in class under at least one of the FLSA's specific exemptions. The purported class may cover different positions, seniority levels, offices or business practices. Statistical analysis of the alleged class can reveal differences among purported class members, if they exist, and may also be pertinent to the merits of the claims.

For example, statistical analysis can help address the specific prongs necessary for the administrative exemption, i.e., whether employees' primary duties related to the management of the firm or client's business and whether employees "exercised discretion and independent judgment" in their work.

Likewise, statistical analysis may shed light on the merits of a managerial exemption, which depends upon employees' actual job duties, not just their title, and the actual duties may vary from one employee to another.

By reducing often complex data to simple statistics, an analyst can evaluate the class members in each category, assessing the statistical significance of differences among each group. More complex analysis may rely on regressions or other tests to quantify any relationship between certain activities and the employee's success, both within and across groups.

With vast amounts of data available, the compilation of simple statistics can be powerful for evaluating whether there is variability among purported class members in daily, weekly or monthly behaviors or differences in the mix of activities. The case of mortgage brokers provides one such compelling example.

Mortgage brokers may rely on a variety of activities to generate customers. Some may rely solely on internal leads, while others may be more involved in marketing activities, e.g., direct mailings or seminars. These differences may appear across offices or even within a given office. This assortment of behaviors may demonstrate conflicts among the class members and may be at odds with the plaintiffs' allegations that the employees' jobs were carefully scripted, with the employees merely following activities outlined by company training sessions.

More sophisticated statistical tests, which can be used in class certification analyses, include the regression analysis. Continuing with the mortgage broker example, regression analysis can be designed to control for the different factors that may affect loan officers' production, e.g., experience, training, office and external factors such as interest rates (if the proposed class covers different time periods), to see whether variation in production still exists for the individual employees after accounting for observable factors.

This residual variation, if found, would again demonstrate differences at the employee level, quantifying the impact of employee-specific behaviors in performing the job. If employee-specific issues are determined to be relevant, classwide defenses would not be applicable.

### ***Analysis of Merits: Discretion and Managerial Activity***

Statistical analysis can also help refute allegations that a job is simplistic and does not require employee discretion. If production can be achieved with different types of employee activities (e.g., making calls or visiting prospective clients), then the act of just showing up and making calls may not explain why an employee is successful.

Again using mortgage brokers as an example, some brokers who make hundreds of calls may be unsuccessful, while others making far fewer calls may have more success. This finding would suggest that the content of the calls may be more important than the volume of calls (or the number of clients visited).

Statistical analysis can also be used in conjunction with survey data to determine what fraction of an employee's activities are spent on calling prospective clients versus, e.g. analyzing financial data.

Another analysis that would be informative of discretion exercised in conducting a given activity is an assessment of whether success increases linearly with the frequency of the activity. If so, then the activity itself will generate the outcome rather than any discretion on the part of the employee.

For example, in work on a pharmaceutical representatives case, we found that some activities demonstrated diminishing returns (e.g., sales calls made to physicians). As more calls were made, the pharmaceutical representative's performance ranking increased, but after a certain point, additional calls were actually correlated with a lower ranking. This type of pattern suggests that it is the quality of the calls, which differs by employee, rather than the quantity that is important.

### ***Estimating Damages***

Statistical analysis can also be used to assess specific employee activities and estimate damages, if any. Many employers maintain large numbers of databases with time stamps. The data from these various sources may be gathered and merged to reconstruct the time use of employees. It is likely to be excessively laborious to engage in such a detailed reconstruction for every day of every employee across an entire class period. A focus on the named plaintiffs or a random sample of the purported class may be more tractable and valuable.

In one case involving pharmaceutical representatives, we used a database of sales calls (with information on time and location of call) and expense reports to reconstruct the activities undertaken for each day worked by the named plaintiffs. Based on these databases, we determined that contrary to the plaintiffs' allegations that they frequently worked overtime, the available record in fact indicated that the plaintiffs' work hours did not exceed FLSA regulations regarding regular hours.

### ***Identifying Highly Compensated Employees***

Another category of exemption from overtime pay under the FLSA is high compensation: Workers making over \$100,000 are classified as exempt if they "perform at least one of the exempt duties or responsibilities of an exempt executive, administrative or professional employee."

Statistical analysis may be helpful in identifying such highly compensated employees. While seemingly straightforward, the calculation as to whether an employee exceeded the compensation threshold can become extremely complicated. The annual period for evaluation of total compensation can be the calendar year, the employer's fiscal year or the year computed from the hire date of the employee.

Pro-rating for partial years and allocating bonuses to the appropriate time periods can yield very different lists of highly compensated employees. A scenario analysis testing the results of the computations to various assumptions may be useful for identifying groups of highly paid employees.

Companies' businesses are becoming increasingly automated, resulting in abundant data becoming available to provide information about employees' days and duties. As misclassification cases continue to be filed and pursued by the WHD, as well as by private plaintiffs under the FLSA, statistical analysis of this data can be a valuable tool for companies in addressing allegations that their employees were misclassified.

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