



# Employers Furlough Without Weighing Legal Risks

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Employers are implementing furloughs without due consideration of all the legal risks, Robert Duston, an attorney with Saul Ewing in Washington, D.C., told *SHRM Online* on June 5, 2009. These legal risks run the gamut from wage and hour issues, possible unlawful discrimination, Worker Adjustment and Retraining Notification (WARN) Act requirements and possible labor relations challenges to benefits issues.

Mandatory furloughs rose sharply in the first quarter of 2009, according to an April 21 Watson Wyatt survey, which found that 17 percent of surveyed companies had instituted mandatory furloughs. Furloughs can help companies avoid layoffs, and “there is a recognition that employers will need to be poised for a turnaround,” stated Laura Sejen, global director of strategic rewards consulting at Watson Wyatt. “Some cost-cutting measures such as reductions in force can put them at a disadvantage once the economy improves.”

But the cost savings of furloughs could be undone by legal costs if compliance risks aren’t considered up front. Duston said that furloughs are “a ripe area for class-action” lawsuits under the Fair Labor Standards Act (FLSA) because many employers are not thinking about wage and hour issues before instituting furloughs. “In such suits, it does not matter that the recovery for any one employee is small—the money is in the class certification, double damages and attorneys’ fees,” he noted.

The greatest danger of a wage and hour class or collective action arising from a furlough “is probably the claim that the employer has negated the exempt status of its salaried workers by making improper deductions based on either partial-week furloughs or else suffering or permitting exempt workers to engage in productive activity such as sending and receiving work-related e-mails during a full-week furlough and not paying the salary,” according to Paul DeCamp, an attorney in the Washington, D.C., area office of Jackson Lewis and a former administrator of the U.S. Department of Labor’s (DOL) Wage and Hour Division, the chief office responsible for interpreting and enforcing the FLSA.

## Wage and Hour Concerns

DeCamp said that the main concern from a wage and hour standpoint is maintaining compliance with the salary basis requirements for salaried exempt personnel. When a furlough is for one or more full workweeks, federal law does not require payment of the predetermined weekly salary, DeCamp told *SHRM Online*. When a furlough is for less than a full workweek and a salaried exempt worker performs any work during that week, the employer must pay the exempt employee’s full weekly salary, he added.

Most employers furlough salaried exempt workers only in increments of full workweeks because of the salary basis concern, according to DeCamp. Although a partial-workweek furlough allows an employer in effect to reduce its contingent liability for vacation pay or other paid leave, the cost savings is usually not immediate or substantial enough to justify a furlough. Companies that need to implement furloughs generally need to conserve cash immediately, thus the need to eliminate the need to pay workers the full weekly salary, DeCamp explained.

“Furloughing exempt employees for entire workweeks is definitely one of the two best options,” said Brian Dixon, an attorney at Littler Mendelson’s San Francisco office.

“The other good option is just to reduce the salaries of employees who do not have contracts to be paid at a certain rate for a particular period of time. Employees with such contracts are comparatively rare,” he stated.

Duston said that for most at-will employees, when the employer is offering a unilateral change in compensation, the so-called legal “consideration” for the change is continued employment, and the employee is deemed to accept it by staying on the job. But the law gets murky in some states since “in some states even less dramatic changes in benefits under an employee handbook have been deemed to be contractual and require some form of consideration,” he cautioned.

It’s clear though that if an exempt employee is furloughed for a day, an employer cannot generally dock the employee for the day, Dixon emphasized. “If there is an extended period of time during which an employee’s regular schedule is changed such that the employee works fewer days per week, it may be possible to ‘revalue’ the employee’s job and pay a lesser salary,” he added.

“There is some risk in telling an exempt employee to take individual days off and then to reduce the employee’s salary,” Dixon noted. “If the reduction in schedule is for an extended period of time, there is a possibility of prospectively changing the employee’s salary. There is no consensus in the courts as to whether this can be done and the frequency with which salaries can be changed.”

Dixon said that “California may well reject the option of telling an exempt employee to work fewer days per week and pay the individual at a lesser rate of pay,” he said. “California’s labor commissioner does not believe that there can be part-time exempt employees, though there is latitude for disagreeing with that conclusion.”

DeCamp’s recommendation is that “any revised salary level should be in place for six months or more so that it does not look like the guaranteed weekly salary is illusory.” But he noted that there is some case law “suggesting that a proportionate reduction in the workweek and the guaranteed salary (e.g., going from five days to four and reducing salary by 20 percent)” constitutes a prohibited deduction from the predetermined salary based on quality or quantity of work performed.

“HR should definitely have in place a written salary pay policy, as required by the DOL’s white-collar exemption regulations, so that errors in salary pay can be corrected,” Dixon emphasized. “Carefully evaluate potential work sharing programs to determine the extent that they can be used with nonexempt and exempt employees.” And, he added, “carefully evaluate state law to determine if an extended furlough might trigger an obligation to pay final wages.”

Under federal law, an employer can require a worker to use accrued paid time off or vacation for time not worked during that partial workweek, or even put the worker into a negative paid leave balance, as long as the worker receives the same dollars for the workweek that he or she would have received in salary, DeCamp noted. But, Gerald Hathaway, an attorney at Littler Mendelson’s New York office, cautioned that whether vacation time can be forced or denied during a furlough varies under state law.

DeCamp agreed that employers should pay attention to state law requirements, saying, “I have not yet come across any specific state-law restrictions on furloughs, but that is certainly something that must be examined on a case-by-case basis, particularly in the area of paid time off serving as an acceptable substitute for salary as long as the total dollars provided for a partial-week furlough equal the predetermined salary. The concern is not only the state wage and hour laws but also, for example, any express or implied contractual limitation on the ability to require a worker to use accrued vacation pay.”

Employers need to understand that a day off because of a furlough does not qualify as a full-day absence for personal reasons other than sickness or disability, which is one of the enumerated permissible deductions under the federal salary basis regulations, DeCamp also noted.

Moreover, when an exempt worker is off for the entire week, “it is very important to make it clear to the individual not to perform any work at all, including checking voice-mail, reading or writing e-mails, or performing other tasks away from the workplace,” he emphasized.

“Getting an exempt person to put down the BlackBerry is a lot more difficult than one might think. And the individuals who manage furloughed exempt staff should be instructed not to contact those workers during a furlough of one or more full workweeks unless making contact is so important that it is worth entitling the worker

to the full week's salary."

As for nonexempt workers, off-the-clock work as a practical matter tends not to be a significant issue, DeCamp added. But he said "it is certainly worth reminding at least those nonexempts who have the ability to perform work away from the workplace that they are not to do so during a furlough."

Salaried exempt employees furloughed for one or more full workweeks should be instructed—in writing, and with their signature to confirm that they were so instructed—not to perform any work at all, DeCamp recommended. They should be told that the only time they are to perform any work during the furlough is if someone to whom they report calls them at home or on their cell phone and asks them to perform work-related duties. And they should be advised that if that situation arises, they must notify someone in HR or payroll promptly to ensure that they receive payment for that workweek.

As soon as the employer becomes aware that employees have worked on their furlough days in violation of company policy, the worker should be counseled for violating company policy, he noted. "If the employer has duly instructed the worker in advance not to perform any work during the furlough, and if no supervisor has instructed the worker to perform these tasks anyway, then there is a strong argument that the employer has not suffered or permitted this work and that the employer therefore need not pay for that time," he said.

But Dixon said that "the better practice is, generally, to record and pay for the time and discipline the employee for not following directions."

If there are hourly nonexempt workers whose work is of such a nature that the employer doesn't mind paying for the time necessary to maintain contact with the office via telephone or e-mail, it is fine to let the nonexempt worker continue to perform those tasks as long as the employer instructs the worker to report all time spent on such activities during the furlough, DeCamp added. He noted that unlike with salaried exempt workers, allowing an hourly nonexempt worker to spend a few minutes a day during a furlough keeping up with workplace events entitles the worker to compensation for only the actual time spent on those tasks rather than compensation for the entire workweek.

However, the risk of off-the-clock work is so great that Kevin Vance and Mark Beutler, attorneys in Epstein Becker & Green's Miami office, told *SHRM Online* in an e-mail that employers should "take away company-owned BlackBerries and cell phones during furloughs, and consider taking away remote Internet access privileges as well."

### **Discrimination Concerns**

A uniform policy of "last hired, first furloughed" does not appear to raise age discrimination concerns, nor would a policy assigning more of the burden of a furlough to more recent hires than to longer-tenured workers, DeCamp said. But he cautioned that "the devil is in the details, however, so it will be important to examine the effect of a proposed furlough for unintended demographic impact."

Vance and Beutler cautioned that "there are discrimination concerns any time you pick and choose one employee over another. Employers implementing a furlough plan should test their proposed selections before implementing them to make sure that their selections do not have a disparate impact on any protected groups, including those over 40."

When asked whether it is permissible to prorate furloughs based on the date an employee is hired and whether an employee is full- or part-time, Dixon said that "it is unlikely that full- or part-time status would involve a protected status except, possibly employees whose disabilities are being accommodated." But he added that "there may be a correlation between seniority and age, and an employer would be well advised to statistically test that correlation before giving more senior employees longer furloughs."

### **WARN Act**

Wage and hour and discrimination issues are not the only compliance challenges employers face when instituting furloughs. Advance notice of furloughs may be required in limited circumstances.

"When an employer orders a temporary furlough, it generally need not issue WARN notice unless it anticipates the layoff will exceed six months," said René Roupinian and Jack Raisner, attorneys at the New York firm of Outten &

Golden, which represents employees, in an e-mail response they prepared together. However, if temporary furloughs are extended and exceed six months or become permanent, “employees may allege that advance written notice should have been issued 60 days before the furlough began.”

Roupinian and Raisner said that “an unscrupulous employer may wish to manipulate its WARN numbers by recalling employees before they cross the six-month tripwire that turns temporary layoffs (or furloughs) into actionable ones. If the employer has a proper business purpose for returning the employees to work, the first period of layoff will not count towards the six months.” However, they cautioned, “if the purpose of returning the employees to work is merely to interrupt the layoff or furlough period to evade WARN liability, the employer can be held liable for violating the law.” They also observed that “it is possible that some employers are using ambiguous terms such as ‘furloughs’ to conceal WARN triggering events.”

Hathaway explained that “the word ‘furlough’ is used by different people to mean different things.” He noted that “to some a furlough means taking a day off once a week. To others it means a rotating one-week layoff. To still others, it means an unscheduled (until now) plantwide shutdown of a fixed period. There is no general, universally recognized definition.”

“Depending on the circumstances, a furlough of a sufficient number of employees might fall into one of the ‘employment loss’ categories that trigger WARN liability,” Roupinian and Raisner cautioned. For example, they said a furlough that reduces hours “to less than 20 per week will also be considered an employment loss triggering the possibility of WARN liability if a sufficient number of employees are affected at a particular site.”

Suppose a furlough is not at first expected to be permanent, but extends beyond six months. Would WARN requirements take effect as of the first day of the furlough? Under the WARN Act “a ‘temporary’ layoff—one that is not expected to extend beyond six months—is considered an employment loss on the day the layoff commenced if it becomes permanent or extends beyond six months, unless an intervening unforeseeable event occurred during the layoff period. In the latter situation, an employer is still required to provide WARN Act notice at the time the need for the extension became reasonably foreseeable or face liability for the full 60 days,” Roupinian and Raisner said.

State WARN acts might apply to some furloughs too, Hathaway added. For example, “whether a ‘furlough’ would be a plant closing (where there is a cessation of operations) under California and Maine state WARN laws is not crystal clear,” he noted. “We think and will advocate that it is not, but clients have to understand that the issue has not been tested in the courts.”

As for the federal WARN Act, the complexity of its preconditions “help explain why the law is often overlooked by employees—but, in 2009, should not be by HR,” they added.

### **Labor Relations**

Furloughs can be even trickier to implement in unionized workplaces. “A union’s ability to challenge a furlough depends on what the collective bargaining agreement says,” Hathaway explained. “If the employer wants to use a method not in the agreement, the employer will have to assess its management rights clause, and if it has not reserved the right to implement a furlough, the employer will have to bargain with the union about it.”

If a furlough is contradicted by language in the agreement, the employer must get the union’s consent before implementing a furlough. “Unions often take the position that they would rather have permanent layoffs of junior employees than rotating furloughs among all employees,” he said.

“Usually a collective bargaining agreement would have a seniority clause, and that will dictate how the workforce is reduced in light of economic conditions.”

If a worksite is not unionized, employees still might bring a legal challenge of furloughs under the National Labor Relations Act (NLRA) if a group of employees object to the furlough and are fired for raising the issue.

### **Benefits Issues**

Employers also should take into account the many different benefits questions that may arise because of furloughs.

“Furloughs may make 401(k) nondiscrimination testing a bigger problem for employers to the extent that nonhighly

compensated employees lower their 401(k) contributions when their salaries are cut,” Steven Friedman, an attorney with Littler Mendelson in New York, said on June 9. “This could cause larger amounts to be required to be refunded to high-paid employees.”

Furloughs also might affect employees’ eligibility for pension plans, matching contributions and health care coverage. “To the extent that plans base eligibility on hours worked, a furlough could reduce hours to such an extent so that formerly eligible employees become ineligible,” Friedman noted. “This could impact those who receive matching and profit-sharing contributions, as well as those who accrue benefits in certain types of defined benefit plans.”

Friedman said that some employers are considering treating employees on furlough as remaining active for plan eligibility purposes because “employers often want the cost savings associated with the salary savings of furloughs, but do not want to go so far as to take away plan benefits.” He noted that employers may count furloughed hours as working hours for medical plan purposes, but that this may require an amendment to the medical plan.

If employees become ineligible for coverage because of a reduction in hours, the employers are not subject to the government’s COBRA subsidy, as long as the hours are not reduced to zero, he said. “However, if hours are reduced to zero, this may permit employees to be considered involuntarily terminated and thus eligible for the subsidy.”

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