

## **Amid Tough Times, Furloughs Can Save Employers Money and Employees Jobs**

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For many employers, these are desperate economic times. Every entity facing diminished revenue must consider cost cuts to survive. As news reports show, reductions in force (RIFs) are being used daily to achieve cost savings, and for some employers they may be the best solution. In some cases, however, the savings are not immediate as a result of statutorily required or voluntary notice periods, as well as costs of severance pay.

A different approach may be a furlough strategy, customized to fit each employer's needs, which may also achieve a significant cost-savings benefit. Implementing a furlough can help retain the employer's experienced workforce at a reduced cost, to help the enterprise weather the economic crisis. Most employees faced with, for example, the choice of a 20 percent annual pay reduction or the loss of their job would not hesitate to choose a reduction in pay. Further, both employers and employees taking advantage of a furlough program are well-positioned to take advantage of any increase in business activity in the inevitable economic recovery, whether it be this year or next. Furloughs are often viewed by the workforce more favorably than layoffs, thus preserving morale in the organization as well.

The Fair Labor Standards Act ("FLSA") requires hourly and non-exempt salaried employees to be paid time-and-one-half their regular rate for weekly hours worked over forty. Accordingly, the first place to look for cuts in employee payroll costs is in non-exempt employee overtime pay. The FLSA was designed to give employers an incentive to spread employment from employees who work over forty weekly hours to other workers who are working fewer hours. In an environment where costs are critical, it is generally an inefficient use of payroll dollars to pay the additional wage premium required for overtime work.

Eliminating non-exempt overtime work is only the first step in reducing payroll costs among hourly non-exempt employees, salaried non-exempt employees and salaried

exempt employees. Take an example in which it has been decided that in a department of 100 employees, where all three categories of employees work, that payroll expenses must be cut by 20 percent. One possibility is to reduce the department headcount by 20 percent, eliminating 20 jobs and the costs associated with them. Another possibility is to implement a mandatory furlough period with 20 percent pay cuts for all 100 employees. The furlough strategy takes more administrative time to manage properly, but it potentially saves 20 jobs while achieving the necessary cost-saving objective.

The FLSA allows employers to implement a variety of options to impose salary reductions and pay cuts, as do most state laws. A salary may be prospectively reduced without violating the “salary-basis” test of the FLSA for exempt employees, including a reduction in pay proportionate to a reduction in the number of days worked. Managers may implement furloughs and RIFs simultaneously or in a phased sequence. As with all such strategies, any applicable state and local requirements need to be determined, as federal law will defer to a state or local standard that provides a greater protection to the employee. California, as shown by the state’s decision to furlough state employees, allows furloughs to be implemented in accord with particular wage-hour requirements that must be considered.

The FLSA permits prospective adjustments to an exempt employee’s salary, including revisions to commission agreements or bonus compensation plans based on the quantity or quality of work, which do not reduce the “predetermined amount” of the employee’s salary (of course, the terms of the plans also need to be checked before changes are made). In concept, if the duties test for exemption is satisfied, the predetermined salary of, e.g., an exempt Sales Manager, could be as low as \$455 per week, while the compensation the employee actually receives could be substantially higher (based upon commissions for meeting sales goals or bonuses for meeting other performance criteria). To preserve the salary basis of the exempt employee, the predetermined amount of salary would have to be paid for workweeks in which there were no commissions, or for which no bonus payments were made.

Careful strategic planning is required before implementing a furlough. Considerations include:

- Exempt salaried employees may have their salaries prospectively reduced to a lower predetermined amount so long as they stay above \$455 per week. Salary adjustments may not be designed to circumvent the requirements of the FLSA.
- Hourly workers must be paid for every hour they are directed or permitted to work. Permitting “extra” work as, for example, spending more than *de minimus* time checking a Blackberry®, even when unauthorized, may well give rise to the obligation to pay for the time. Accordingly, managers must take the necessary steps to ensure the furlough plan realizes the necessary cost savings.
- It is a good practice to give employees clear notice specifying that no “volunteer work” is permissible and no work is to be performed unless specifically authorized by a predetermined schedule or authorization by an appropriate manager. Implementing a

strict policy of prohibiting unscheduled work and having an administrative procedure to uniformly enforce the policy is well advised.

- Managers may consider asking hourly and salaried non-exempt employees for the return of employer-owned remote access devices during a furlough. Employees who access their work email accounts while on their “time off” may be working, or may start working. If they are working, even though advised not to do so, the employer may well incur wage liability, defeating the purpose of the furlough. Unauthorized work by non-exempt employees in violation of the employer’s furlough policy may generate exposure to significant wage claims. Violations of the furlough policy should be considered a serious disciplinary issue, warranting sanctions, including suspension and discharge. Withholding pay for hours actually worked, however, is not a legal option, even when the hours worked were not authorized.
- Salaries for exempt and non-exempt employees may be prospectively reduced so long as those adjustments are not so frequent as to appear designed to circumvent the requirements of the FLSA. Quarterly adjustments have been found by the U.S. Court of Appeals for the Second Circuit to be in compliance with the FLSA. Adjustments to the predetermined amounts of salary should be implemented as infrequently as feasible so as not to raise an argument that the adjustments are a pretext to avoid compliance with the FLSA.

In sum, properly implemented salary reductions should comply with the salary requirements of the FLSA. Although it requires strategic planning and careful implementation, employers may find many benefits by implementing an effective cost-savings furlough plan that saves money and jobs, versus the RIFs dominating the news.

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