An Overlooked Giant: Top 10 Things California Employers Need to Know While Responding to Federal Labor Department Wage Audits

Insights
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Although California businesses may be preoccupied dealing with attorneys invoking the Private Attorneys General Act, a federal government investigator may come knocking at your door when you least expect it asking to conduct an audit of your wage and hour practices. While you might be familiar with state-specific best practices, would you know what to do if the U.S. Department of Labor showed up tomorrow? These audits may involve a lot more than you think and have some particular nuances unique to the federal government. Here is a general overview of the process along with the top ten things you need to know about this often-overlooked giant.

The DOL Audit Process

An audit conducted by the U.S. Department of Labor (DOL), Wage-and-hour Division (WHD) typically involves the following stages:

1. onsite inspection;
2. opening conference;
3. employee interviews;
4. document production;
5. back-wage findings;
6. closing conference; and
7. follow-up issues.

The audit may be initiated by an onsite visit, but generally involves a formal letter seeking documents and information. The DOL-WHD investigator will seek to know if employees have been notified of their rights, and may generally begin by looking to determine whether the employer has made the necessary postings. The DOL-WHD requires employers to post in areas frequented by employees their rights under the FLSA, including minimum wage, overtime, and COVID-19-related paid leave rights (in addition to other federal entitlements).

1. **Employee Complaints Often Trigger Audits**

Not all audits are triggered by employee complaints, but many are the result of a complaint. Commonly, the DOL investigator may ask specific questions regarding the employer's specific wage-and-hour practices on issues that puzzle employers regarding the possible existence of employee complaints or "informants."

Clearly, although DOL audits may be random, employers understandably want to know the substance of such allegations that triggered the audit in order to defend any possible underlying allegations of wage-and-hour violations. On the other hand, the DOL may have an interest in protecting such witnesses and informants from retaliation and other potential harm. Where such information is not forthcoming, the reality is that employers may be shackled unfairly from investigating and defending such claims.

In short, employers often understandably maintain they cannot investigate or defend claims effectively when the DOL does not want to disclose the identity of the witnesses for a variety of reasons. Indeed, such individuals may be witnesses in a later government lawsuit, and they may have created the impetus for a DOL audit as well. An audit provides opportunities for the DOL to obtain information and documents prior to initiating litigation, should that be found necessary.

In a wage and hour audit, claims regarding potential violations are still at the investigation stage. Like California's DLSE (as to California's state laws), the federal DOL has an obligation to investigate complaints regarding violations of federal laws. If the DOL's actions are limited to conducting a wage-and-hour audit, the employer may not know the identity of such individuals because the DOL may be concerned that its investigation could be hampered if witnesses stop cooperating for fear of retaliation. Nonetheless, the DOL investigator for practical reasons may disclose the nature of the allegations giving rise to the audit, in whole or in part, which may provide sufficient information for the employer to begin an internal investigation. Otherwise, the specific items on the audit request may be the employer's only clue regarding the basis for possible claims triggering the audit. If the topic of interest relates to a particular position, shift, or period of time, this helps create the landscape for limiting the scope of the audit, if that's possible.

2. **Recent Case Potentially Provides Some Relief from Government Use of "Informant Privilege"**

In situations where the DOL actually brings a lawsuit against an employer, the agency may be forced to disclose the identity of such individuals. A 2021 federal appeals court decision from the Ninth Circuit upheld a lower court's order requiring the DOL to disclose the identities of informants before dispositive motions were due in light of the employer's right to defend claims raised against it.

For sure, it is important for California employers to investigate actual or suspected claims and issues brought by a DOL investigator without regard to whether the identities of witnesses and "informants" are disclosed. Such complaints may lead to investigations and audits by the DLSE or attorneys representing employees in PAGA Actions to address California's unique regulations

that go beyond what federal law requires. Things could spin out of control quickly if allegations are not addressed and resolved as soon as possible.

3. **Preparation for Employee Interviews is Critical**

   Employers should take reasonable steps, with assistance of counsel, to prepare employees for a DOL audit interview. That may include a reasonable list of rights and obligations, including not making false statements during an interview, which may help employers defend against potential claims by investigators that employers are "coaching" employees to paint a false picture regarding employer compliance. Employees may request a supervisor to be present, but employees generally need to know that the DOL likely will insist on holding private interviews of non-managerial employees.

   Although employers should tread carefully to avoid government accusations of obstruction, employees may be advised that they need not cooperate or sign affidavits that DOL investigators may seek to obtain. Each situation presents different risks and issues, so each situation should be addressed on a case-by-case basis with legal counsel. If the employer is viewed as interfering with the investigation and audit, this could hamper prompt resolution and lead to the filing of a federal civil enforcement action, which option the DOL has taken frequently where it deems it necessary.

4. **Train Management Regarding Employers' Rights**

   The WHD has the authority to engage in "discovery" used to establish liability in its litigation activities, through record audits and related inspections. These can catch employers off guard if not prepared. Employers therefore should establish internal practices that enable them to be in a perpetual state of preparedness for responding to, and defending if necessary, demands for payment and/or litigation brought by the DOL-WHD.

   During DOL interviews, employees may claim that they are not aware of the most basic FLSA standards. Although legal postings may help dispel these claims, don't count on it – it's wise to provide employees with formal training and proof of such training regarding these laws. And, managers may be found during interviews to lack a basic understanding regarding federal laws such as timekeeping and calculating the regular rate when paying overtime.

   Of course, managers who do not understand federal and state wage-and-hour laws will not be in a position to function effectively during an audit, although knowledge of DOL audit procedures may assist in the employer's need to have adequate time to prepare and defend claims. While not a substitute for basic substantive knowledge of wage-and-hour laws, knowing such procedures in dealing with the DOL may compensate for a lack of some technical knowledge of the applicable laws.

   For example, managers should know that an employer has the right to request that interviews and onsite inspections by the DOL take place at reasonable times and in a reasonable manner. In

addition, an employer has the right to request and participate in an opening conference, which can provide the employer with valuable information regarding the audit.

5. **Audits May Include Inquiry Regarding Previous Audits**

   If the DOL has conducted prior government audits, it's important that any previous concerns raised have been addressed and resolved, generally with assistance of legal counsel. The investigator may specifically ask about a prior audit.

   Employers should be prepared to provide answers, if necessary, with assistance of legal counsel. If any new problems come to light during an employer's internal audit, employers ideally should have addressed and resolved them. In short, the employer should have taken actions to avoid, to the extent possible, any surprises in the event of a DOL-WHD audit. That means internal audits should have been performed regularly. The internal audit should be conducted under the direction of legal counsel (internal counsel or outside counsel) to protect the audit findings and recommendations, if necessary, under the attorney-client confidentiality privilege.

6. **Establish Audit Response Teams Ahead of Time**

   California employers should have in place a team to respond to federal (as well as state) audits. Although the DOL-WHD investigators may have heavy workloads, they can marshal together significant staffing to support an audit and enforcement action if necessary. To provide an adequate defense, you should gather your own forces ahead of time to match the resources that could come to bear on your business.

   Your employer response team should include a team leader. The team leader ideally should be legal counsel, or a high-level manager who works closely with legal counsel. It's important to make sure that any onsite visits or letters by the DOL are immediately brought to the attention of the team leader, a key responsible employee, or team of employees, and legal counsel.

   Individuals on a response team should be appointed and trained to handle an onsite walk-through with a DOL investigator, how to handle document requests (including marking "proprietary" and "business confidential" and documents turned over to the DOL), and overseeing the creation of an employee list which the DOL typically requests so it can contact employees.

   On the top of the action list will be the need to investigate basis for investigation if known; identify witnesses for audit issues; seek to narrow the scope of audit; and obtaining an extension without delay (silence may be interpreted as lack of cooperation). If a request is made for information or documents, the information provided should be limited to the specific request. The scope of the audit therefore should be nailed down as quickly as possible. If an investigator appears for an onsite audit, the employer should verify the credentials of the investigator (e.g., to prevent entry by an imposter planted by a competitor or adversary).

7. **Know the Process of Requesting an Extension**

If an investigator appears for an onsite audit and a team leader is not available, the agency should usually permit an extension of time and reasonable delay, as an employer has a right to have representative on site). The DOL-WHD frequently will grant extensions especially if it anticipates reasonable cooperation, although this may depend on the seriousness of the suspected or reported violations. At the very least, the DOL generally will consider granting a 72-hour extension for an employer to respond to investigation demands.

Although an employer may consider not turning over information or documents without a subpoena, legal counsel should be consulted on these issues. Refusal to cooperate without a subpoena could be viewed by the DOL-WHD investigator as obstruction by employer. In other words, they may believe the employer is hiding something, and this actually could create expedited enforcement activity. Thus, legal counsel may advise that consenting to an investigation – as opposed to demanding a subpoena – could facilitate DOL accommodations and cooperation, including reciprocal concessions and beneficial quid pro quos (limiting scope of audit, etc.). These can be extremely important strategic steps because most audits involve complicated facts that may require different approaches in responding and cooperating with the DOL-WHD investigator.

8. **Responding to Back-Wage Findings**

The DOL-WHD investigator may make certain back-wage findings and assessments for liquidated (double) damages. n a DOL audit, this is a critical stage where the employer's response could be important in reducing liability and resulting in a resolution. Notably, if records are lacking, the investigator may base back-wage findings on verbal statements by employees. Alternatively, the investigator may base the back-wage assessments for the entire alleged liability period based only on working periods for which records are available, i.e., it will project similar liability across pay periods for which the records are not available. Sometimes these assessments are reasonable. But not always. Unfortunately, these "projections" sometimes may be based on inaccurate information, leading to exorbitant back-wage assessments that are unfair to employers.

The employer generally will be permitted to respond to the back-wage assessment. At this stage, there will be some back and forth negotiation in many cases – although the DOL generally would not reduce its assessment for clearly supported violations. One of the most seminal Supreme Court decisions in this field found that, when the employer's records are inaccurate or inadequate and the employee cannot offer convincing substitutes, the burden shifts to the employer to demonstrate the precise amount of work performed or to refute the inference to be drawn from the employee's evidence. You don't want to be in this boat.

If the DOL believes it has adequate evidence to determine by "just and reasonable inference" the unpaid working time, it is common for compromises to be made by the DOL where the employer

rebuts such evidence by making a good faith showing that the back-wage assessment are not accurate or supported by the evidence, in whole or in part, during the alleged periods where record keeping was deficient. Similarly, the DOL generally assesses liquidated damages for unpaid wages, including overtime and minimum wages. Certain defenses exist for these assessments, so the employer should assert such defenses in response to any back-wage assessment adding liquidated damages. If the employer does not make any effort to counter the findings, the DOL will rely on its back-wage assessments, even if they are excessive.

If there is a successful resolution, the DOL-WHD typically will facilitate payment of any unpaid wages and liquidated damages (sometimes an amount reached by compromise). However, legal counsel should guide the employer through these steps, including addressing the legal aspects (including scope) of any release of claims provided by the DOL as to payments made by an employer to its current and/or former employees. Legal counsel should also explain the advantages of resolving claims with the DOL, including the fact that courts have found that DOL or court approval is required to resolve FLSA claims.

9. **Keep State Audits in Mind**

Although not addressed at length in this article, the prospect of California DLSE audits needs to be kept in the back of mind when considering DOL audits. After an initial meeting with a state investigator, which may be similar to a DOL opening conference, employers may be permitted to perform self-audits subject to DLSE review and oversight. This could then be followed by potential back-wage assessments, penalties, and interest, which may include some negotiation and informal fact finding by the DLSE. Employees receiving payments following an audit generally are not required to sign releases. And, if DLSE demands are not resolved, employers may be subjected to administrative hearings, with awards enforceable by civil judgments. Or they may be sued in public civil actions filed by the DLSE where state judges following trial can order repayment of back wages, attorneys fees, interest, and penalties.

10. **More Than Compliance with the FLSA May Be at Stake**

Finally, although these issues extend beyond the scope of this article, it's important to note that, more than compliance with the FLSA may be at stake when audited by the DOL. A federal audit may extend to a variety of federal workplace laws, including the Families First Coronavirus Response Act (FFCRA), the Family and Medical Leave Act (FMLA), the Migrant and Seasonal Agricultural Worker Protection Act, the field sanitation standards of the Occupational Safety and Health Act, the Employee Polygraph Protection Act, certain employment standards and worker protections under the Immigration and Nationality Act, government contracts prevailing wage statutes such as the Davis-Bacon and related Acts and the McNamara-O'Hara Service Contract Act, and garnishment provisions of the Consumer Credit Protection Act. No wonder it's important to seek legal counsel to be fully prepared for such an audit.

What Should Employers Do?

The federal DOL-WHD has a formidable army of investigators and a seemingly unlimited federal budget. Employers should not overlook the fact that the DOL has jurisdiction in California over employment-related claims that arise under federal law, including but not limited to the FLSA.

As explained above, you should take steps in advance of any DOL-WHD audit, including conducting your own internal audits, to make sure to minimize any surprises that may result from a DOL-WHD audit. You must be ready at every stage to make an informed response, including by forming an audit response team, verifying the credentials of the DOL-WHD investigator, seeking any necessary extensions of time, limiting the scope of the audit and related access and exposure, overseeing the evidence gathering and witness interviewing processes to the extent possible, responding appropriately to back-wage assessments, and achieving if possible a successful resolution of any concerns arising from the audit.

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