Human Resource Hot Topics for Closely Held Businesses

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This article addresses some common small business questions and high-level hot topics surrounding human resource matters. (Ms. Goncharsky is an Arizona- and California-licensed attorney and encourages the reader to seek appropriate legal counsel. This article should not be construed as legal advice.)

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Often times, closely held businesses do not have a designated human resource (HR) professional on staff. Instead, the business relies on the owner and/or office manager to oversee its employee relation issues among other daily tasks, such as accounting, leaving the owner(s) pulled in many directions. The required multitasking can lead to issues being missed and mistakes encountered that could have been prevented or minimized with earlier recognition. Some of these issues are discussed below.

#1: Employee Classification

Companies must appropriately classify each position to stay in legal compliance and avoid hot water with government agencies such as the Internal Revenue Service (IRS) and the Department of Labor (DOL) and their state equivalents. First, the business must determine if the worker is an employee or an independent contractor. Then, if the worker will be in an employment relationship, the company must determine if the position is properly classified "exempt" or "non-exempt" under the Fair Labor Standards Act (FLSA) (and any applicable state or local laws).

As do many of the government agencies, the IRS provides helpful guidance to assist employers in determining whether a worker is an independent contractor or employee. As referenced by the IRS, "The keys are to look at the entire relationship, consider the degree or extent of the right to direct and control, and finally, to document each of the factors used in coming up with the determination." [*https://www.irs.gov/businesses/small-businesses-self-employed/independent-contractor-self-employed-or-employee*]

Often the behavioral expectations, financial arrangement, and type of relationship will determine if an individual is an independent contractor or an employee. An employer should consider:

- Does the individual control what work s/he does and how that work is done?
- Who provides the equipment (computer, office space, *etc.*) for the individual to complete his/her job?
- Is the work performed a key aspect of the business?

More often, the work to be performed will indicate an employment relationship rather than that of an

independent contractor. That means that the company will then be responsible for employer-side taxes, unemployment compensation contributions, and other employee benefits. Accordingly, some companies will seek to have certainty as to the costs of the employment relationship by taking such action as classifying the position as exempt and not paying the employee for overtime hours worked. Companies that consider this should first evaluate whether it is appropriate to classify the position as exempt versus nonexempt under the FLSA (and any applicable state or local laws).

The FLSA requires that employees be paid at least minimum wage for all hours worked and overtime at one and one-half the regular rate of pay for all hours worked in excess of 40 hours in a particular workweek. However, the FLSA provides an exemption from these requirements for individuals employed in bona-fide executive, administrative, professional, outside sales, and certain computer positions (as defined by the FLSA). The positions are considered "exempt" and are not subject to the FLSA's minimum wage and overtime pay requirements. Employers, therefore, would be wise to familiarize themselves with the guidance provided by the DOL at *https://www.dol.gov/whd/overtime/fs17a_overview.htm*.

The ultimate burden of and responsibility for determining each employee's classification falls on the employer. If done incorrectly, the employer can encounter heavy fines that may include back pay, interest, and penalties. So, as with everything else, it is always a good idea to consult an experienced employment attorney.

#2: Restrictive Covenant Agreements

A typical restrictive covenants agreement (contract) prohibits an individual (a current or former employee) from soliciting clients, employees, and/or going to work for a competitor. These documents are common, but are not always enforceable as written. The enforceability of these agreements are governed by state, not federal, law. As a result, they can vary greatly from state to state. For example, states such as California are less likely to enforce noncompete agreements than other states. If an employer expects to rely on this protection, the employer must be familiar with what restrictions will be enforceable in the applicable jurisdiction.

Most states require a degree of reasonability for the agreement to be enforceable. Factors that a court will consider in deciding whether the agreement was reasonable and should be enforced include: if consideration was given in exchange for the signed agreement, what harm the employer may suffer if the former employee engages in competitive behavior; the duration of the agreement (for example, is the agreement only for the time period required for the information acquired by the employee to expire); and finally, whether the restrictive covenants prevent the employee from making a living without having to relocate.

#3: Employee Handbooks

Some small business employers believe they are too small for an employee handbook. While these employers are correct that certain laws do not apply to small businesses, we believe a well-drafted employee handbook can provide the employer with some legal protections, aid in the employee on-boarding process, help to establish and maintain employee expectations, and minimize internal employee disputes. Additionally, some states require employers to have written policies and when a government agency investigates, one of their first requests likely will be to see all applicable written policies so as to establish the business's compliance efforts. A well-written employee handbook can help employers not only to comply with the law but to establish and foster the appropriate corporate culture.

Like all written documents, though, employee handbooks also can be harmful to the company if not written well. It is very important that an employer is confident the company handbook is in compliance with federal, state, and local employment laws. Most employee handbooks will contain, among other things, a legally compliant employment at-will clause. Additionally, employers should consider adopting policy language preventing discrimination, harassment (such as sexual harassment), and retaliation; addressing the Americans with Disabilities Act (ADA) (for companies with 15 or more employees); establishing a Code of Conduct; defining work hours; communicating expectations regarding use of technology, including telephones, email systems, and social media; describing employee benefits; and detailing paid time off (PTO) (including vacation, holiday, and sick).

An employee handbook is a "living document": it should evolve with the company, not be written once and then never followed, referenced, or updated. It should be a key part of the orientation and employee management process. To achieve this, most companies find it useful to update the handbook as often as needed, reviewing it at least once a year. Employers

should avoid making promises (such as permanent employment) in the handbook. Finally, when an employee handbook is updated, it is a best practice to require that each employee receive and read the handbook. We suggest you also obtain an acknowledgment form from each employee acknowledging receipt of the new handbook.

#4: Managing Employee Performance

All employers likely will encounter an employee who struggles with his or her performance. Managing employee performance is often one of the greatest employer challenges for small business employers. Poor employee performance may be a result of a lack of understanding, training, or motivation. The worst thing an employer can do when there are performance issues is nothing. Ignoring poor performance will not result in improved performance. Rather, it will lead to no improvement and potential disengagement and resentment from other employees.

When a performance issue arises, it is important to address the issue. It may be appropriate to develop a formal performance improvement plan (PIP) for the employee, which should be communicated to the employee and documented in writing. The documentation should include objective and factual information. Editorial comments should not be included in the documentation.

If a PIP is developed, it should include an action plan for improved performance. That action plan should include specific and measurable goals for improvement. In addition, the plan should include a set timeline for the objectives to be met (typically 30-90 days). The PIP should be communicated with the employee and it is best practice to have both the employee and the employee's supervisor sign this plan. The employee and his/her supervisor should meet regularly to monitor the progress of the PIP.

If the employee is able to improve performance, this should be documented and can be used as a motivation tool. If the employee is unable to improve performance, the employer needs to consider if a demotion or termination is appropriate. If so, again, we highly recommend this process is documented.

Conclusion

We know there are endless employment issues to consider as a small business. Having a strong understanding and plan surrounding the above topics can help put small businesses on the path toward increased employment law compliance and continued business success. ■