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Legal Considerations in Conducting a Pay Equity Audit

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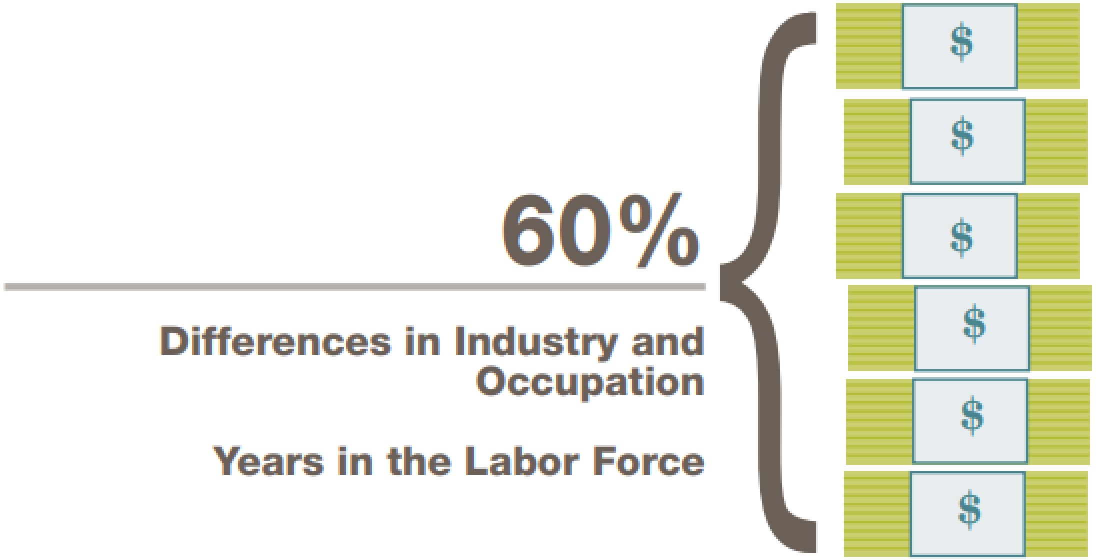
The Wage Gap Persists Whether We Admit it or Not

Change The Story VT, 2019 Status Report: Women, Work, and Wages in Vermont

Research Suggests…

- The wage gap has been narrowing, but very slowly. Research has found the wage gap is the product of intersecting variables:

60% of the gender wage gap is due to two factors: occupational segregation—or career clustering—and time in and out of the labor force.[5]



What About the Other 40%?

- There are many different psychological and sociological factors, both within and outside the workplace, that make eliminating the wage gap difficult. Research suggest these start affecting girls very early in life.
- A study of 10,000 families found that on average American parents pay boys twice as much for doing weekly chores ($13.80) as they pay girls ($6.71).
- We need to recognize that there are both conscious and unconscious stereotypes and expectations surrounding children and families from—or even before—birth.

$13.80

$6.71

Why Care About Pay Inequity?

- Research shows that diversity and equity improve profitability.
- Pay equity is a key indicator that many of your other employee-focused systems are working well.
  - Pay equity is determined at the nexus of your recruiting, performance review, compensation, and promotion systems. In each of these systems, you may have many people making many decisions, and they all affect someone's pay. If those decisions collectively support pay equity, it is a great indication of a cohesive organization with excellent values embedded in your workforce.
- If you can confidently and accurately state that you are paying your employees equitably, your recruiting, retention, employee engagement, reputation, and brand value will be strengthened.
- Pay equity reviews will help your organization avoid lawsuits, negative publicity, and a poor reputation. Those are the "defensive" reasons for doing such a review, and it should go without saying: there are laws against paying a protected class of employees inequitably that we'll talk about shortly.
- You should pay people fairly because it is the right thing to do.

Drawbacks of Pay Equity Audits

- Disclosure of unfavorable audit results
  - The unintended disclosure of audit results is a primary risk and can occur when an audit's results or processes are not privileged or not handled in a confidential manner and are discoverable in litigation.
- Providing evidence of known violations
  - Worse than not conducting an audit is conducting an audit that reveals unjustifiable pay disparities and then doing nothing to remedy the problem.
- Employee suspicion of results
  - Even if an audit reveals no statistically significant pay disparities, the employer may choose to disclose the results to its workforce. Some employees may be suspicious of positive audit results. This may lead employees to file suit or threaten litigation to force the company to disclose the underlying information in discovery, including the data collected or the audit methodologies and processes used.
- Privilege considerations

Federal and State Laws

- Federal law guarantees equal pay for equal work under:
  - Title VII of the Civil Rights Act of 1964 (Title VII)
  - The Equal Pay Act (EPA)
  - The Lilly Ledbetter Fair Pay Act (see Lilly Ledbetter Fair Pay Act of 2009)
- State law considerations
- Defenses
  - Employers defending sex-based pay discrimination claims under Title VII may also take advantage of the affirmative defenses available under the EPA (42 U.S.C. § 2000e-2(h).
  - Employers can defend against an EPA claim when any unequal wages result from: a seniority system; a merit system; a system that measures earnings by quantity or quality of production; any factor other than sex if the employer does not reduce the wage of any employee to comply with the EPA.

Establishing Purpose and Parameters

- To best ensure a productive pay equity audit, employers should clearly identify:
  - The purpose and goals of the audit.
  - The desired breadth and scope of the audit, including:
    - the business unit or units covered;
    - the time period analyzed;
    - the physical locations covered;
    - the forms of compensation to be analyzed; and
    - the data points analyzed, such as an employee’s location, gender, age, race, ethnicity, education, experience, performance, production metrics, and other factors that may correlate with, or even explain, pay disparities.

The Three Audit Types

- Depending on its goals, a company can choose one or more approaches to a pay audit, such as (i) a foundational audit, (ii) a remedial audit, and (iii) a causal analysis (or root causes) audit.
- Foundational
  - The goal of a foundational audit is to identify any potential pay disparities and perhaps isolate the issue to specific departments or groups.
  - The focus is on data collection and analysis to determine if any statistically significant pay disparities exist.
  - This may be the most effective approach when a company has an objective, well-documented, and fair compensation approach, but still faces immediate or threatened litigation and must quickly investigate to determine whether it faces substantial liability exposure.
  - This audit approach is also typically used when a company lacks the financial resources to remediate any identified disparities, at least in the short term.

Audit Types, contd.

- Remedial
  - With a remedial audit, a company takes the additional step of creating a remediation plan to address any identified pay disparities.
  - A company should develop a detailed remediation plan to properly plan for unexpected results and maintain fiscal responsibility.
- Causal
  - Using a causal analysis approach, a company looks beyond the data and analyzes whether and to what extent its own internal systems and processes may be causing or contributing to pay disparities. This includes an analysis of:
    - Compensation and incentive philosophy, policies, practices, and procedures.
    - Methods of talent acquisition, talent retention, and promotion.
    - Whether the company is relying on fair and job-related performance review metrics and methodologies.
    - A causal analysis may ultimately require structural changes to a company's management and operations.

Privilege Considerations

- A company facing immediate or threatened litigation generally can rely on both the attorney work product doctrine and the attorney client privilege to protect the confidentiality of the audit.
- However, a company conducting a pay audit for general compliance purposes may not be entitled to the same protections, as it is likely driven by other factors, such as achieving a compensation structure that mirrors the company's cultural goals and avoiding costly litigation in the future.
    - Although this type of proactive, self-driven pay equity audit is encouraged, it requires careful consideration of processes and team selection to maintain confidentiality and privilege.

Privilege Considerations, contd.

- Companies must adhere to strict protocols to establish and preserve the attorney-client privilege. When preparing for a pay audit, they should:
  - Determine whether outside counsel is necessary. Courts may view in-house counsel as primarily or purely functioning in a business capacity, which can create ambiguity about whether communications have a legal purpose. Engaging outside counsel for their legal expertise clearly establishes the legal purpose of the audit, but this should be explicit in any engagement letter.
  - Set the scope, breadth, and approach of the pay equity audit depending on the purpose of the audit, in particular, whether the audit is:
    - in response to pending or threatened pay discrimination litigation; or
    - part of a proactive legal compliance exercise.

Privilege Considerations, contd.

- Identify and limit the pay audit team members to those who are relevant and necessary. Even for team members, such as legal counsel, companies must ensure that their role involves legal compliance by providing legal analyses, conclusions, and recommendations.
- Allow counsel to engage any necessary third parties, such as experts or consultants. Counsel should also ensure that any third parties sign nondisclosure agreements.
- Establish protocols, such as the preferred methods and manner of communications and the distribution and preservation of privileged and other confidential materials.
- Communicate to the audit team that the attorney-client privilege only applies to communications that are:
  - meant to be confidential; and
  - made for the purpose of obtaining or rendering legal advice.

Data Security, Collection and Analysis Considerations

- A pay equity analysis usually includes the following steps:
  - Consideration of data privacy and security laws.
  - Collecting extensive data, including at least:
    - compensation information;
    - employee personal information; and
    - workforce data, including data on factors that a company uses to set or determine pay.
  - Determining comparator job groups comprised of positions where employees perform equal or substantially similar work.

Data Protection

- The collection and use of employee information to conduct a pay equity audit raises potential privacy concerns.
  - To prevent unauthorized disclosure and inspire confidence that the pay equity audit process and results remain confidential, a company should engage data privacy experts as part of the audit team to ensure data privacy and security of underlying data.
  - For pay equity audits involving employees located in any member state of the European Union (EU), companies must comply with the General Data Protection Regulation (GDPR).

Data Collection

- Breadth and Scope Considerations
  - Geographical and organizational considerations are usually the primary factors in determining the breadth of an audit.
  - If a large and complex company is conducting a pay equity audit for the first time, collecting and analyzing the raw data for the entire company may pose a significant undertaking from a logistical and financial perspective.
    - These companies may consider first conducting a pay equity audit for a smaller subset of employees.
  - For multi-state and multinational companies, an audit's scope may be driven primarily by geographic considerations, especially because different jurisdictions may have different compliance requirements.
    - For example, Massachusetts has an equal pay statute that only applies to gender-based pay discrimination (M.G.L. ch. 149, §§ 105A to 105C). New York has passed legislation expanding coverage of its equal pay statute to additional protected characteristics (N.Y. Lab. Law § 194) (effective October 8, 2019)).

Data Collection, contd.

- The scope of a pay equity audit, including the protected characteristics (such as gender, race, or ethnicity) that are the focus of the audit, influences what employee personal information must be collected.
- Any audit, however, requires the collection of certain baseline information, such as employee name or identification number, and age.
- One of the most important data sets used in a pay equity audit is workforce data, including job titles and classifications and other employment-related information.
    - Companies should work closely with local management, human resources, and payroll personnel to ensure that the job information collected is accurate and reflects their employees' actual skill, effort, and job responsibilities.
- Companies must consider all forms of compensation and benefits when conducting a pay equity audit.

Data Collection, contd.

- Categories of data to potentially collect and consider, include things like:
  - Full-time or part-time status.
  - Geography.
  - Seniority and hire date (for all positions with a company).
  - Leave of absence history.
  - Flexible work arrangement history.
  - Performance reviews and ratings.
  - Educational qualifications and any relevant training, licenses, or credentials.
  - Prior job experience.
  - Exempt versus nonexempt status.

Data Analysis

- When determining which employees to compare, the employer must ensure that the employees who perform equal or substantially similar work are grouped together for review. This generally requires that the employees:
  - Use equal or substantially similar skill, effort, and responsibility in the performance of their duties.
  - Perform those duties under similar working conditions.
- If a company lacks current or incorrect job descriptions, it should update them as part of the audit process.
- Identifying proper comparator job groups is crucial to a pay equity audit.

Data Analysis, contd.

- Once a company has completed the data collection and privacy protection stages, it must decide which statistical analysis tools best serve its audit needs.
- The most common analysis tools are regression, descriptive, discretionary review, and cohort analyses.
- Their purposes are to:
  - Identify pay disparities.
  - Identify legitimate explanations for any pay disparities.
  - Provide information to correct unexplained and problematic pay disparities.

Data Analysis, contd.

- Strongly consider:
  - Conducting a regression analysis for each comparator job group, where possible, to assess if pay disparities exist between employees of the opposite sex, another race, or another ethnicity, depending on the scope of the audit.
  - Reviewing discrepancies at an aggregate level, adding legitimate job-related factors to explain wage disparities for reasons other than a protected class characteristic.
  - Reviewing discrepancies at an individual level to ensure the relevant employment data was completely and accurately captured.

Data Analysis, contd.

- In addition to identifying proper comparator job groups and implementing appropriate pay grades, companies should also have a clear understanding of what factors primarily drive compensation within a comparator job group.
  - Objective factors like seniority, quantitative production, education, experience, and location are easy to track and are also recognized as valid job-related factors that can explain a pay disparity.
  - Factors like qualitative performance, however, are also job-related but they are more prone to subjectivity and bias, which can result in tainted compensation outcomes.
  - Companies should carefully scrutinize and document their compensation philosophy and the valid, job-related factors that can be considered when setting compensation. This will help address and mitigate the use of discretionary-based philosophies that may taint employee compensation and help to explain legitimate reasons for pay disparities.

Developing a Thorough Remediation Plan

- It is helpful to establish a general remediation approach **before** seeing the results of a pay equity audit.
- Even a company that sets aside funds to remediate may realize that pay disparities exceed available remediation funds.
- To help guide this difficult decision-making process, companies should establish guidelines stating, for example, that compensation decision-makers should:
  - Not reduce or freeze employee compensation to eliminate disparities.
  - Rely on consistent percentage increases for remediating the selected group, rather than allocating remediation amounts based on discretion.
  - Prioritize remediating comparator job groups (based on equal or substantially similar work), job positions or titles, or geographical areas where the disparities are largest.

Achieving Pay Equity – An Ongoing Commitment

- So, what is needed to achieve pay equity in every organization? In my experience, there are at least five elements:
  - Executive commitment, understanding, and attention
  - A compensation philosophy
  - Annual pay equity assessments
  - A diverse group of people in the room where pay decisions are made
  - Eternal vigilance and assigned responsibility

Achieving Pay Equity, contd.

- Pay equity is all about consistency. First, your company needs to be clear in its compensation philosophy: how you want to pay each position relative to the competitive market; and what criteria you will use to determine pay increases for each position. Second, you need to be clear about how you will ensure that you are actually operating consistently with your philosophy.

Is your organization paying *all* of your employees in ways that are consistent with its values and compensation philosophy?

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Are the decisions determining starting pay and pay increases consistent within each position or within groups of positions for which you have similar approaches to compensation?

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How can you be sure that you are acting consistently? How would you know when you have a problem?

Commit to Education and Training

- In addition to offering company management some guiding principles in setting employee compensation, the company should train management on the broader issues that relate to and impact pay disparities. These include training on:
  - Pay equity laws
  - Salary history bans. Employers that hire in certain jurisdictions, including California, Connecticut, Delaware, Hawaii, Illinois, Massachusetts, Oregon, and Vermont, should train management, recruiting, and other hiring personnel about any applicable salary history bans that restrict a company's ability to request an employee's salary history at various stages of the hiring process.

Education and Training, contd.

- Unconscious bias
    - Employers should train management on the dynamics and potential risks of unconscious bias and how their unintentional actions may have serious consequences for their employees' livelihoods.
- Pay transparency. The National Labor Relations Act (NLRA) has long been interpreted to prohibit policies that prevent employees from discussing their wages. Similarly, states like California, New York, New Jersey, Massachusetts, and others have enacted legislation protecting employees' rights to communicate about their compensation and limiting a company's ability to control the manner of the employee's disclosure.

Questions?

Thank you

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