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Export Codes of Conduct, Not Employee Handbooks

By Donald C. Dowling Jr.

HR professionals understand why an employee handbook is a vital best practice for U.S. employers. Handbooks communicate big-picture rules, standards and expectations, as well as detailed practical information, such as how the employer handles leave, overtime, dress code, co-worker dating, and benefits, to name just a few topics typically addressed in handbooks.

What may be less familiar to U.S. employers is the fact that detailed handbooks are, if not unique to the United States, uncommon abroad. While handbooks are found in a few common-law countries (e.g., Australia, Canada and India), much more typical in the global workforce are other employee communication tools, including codes of conduct, which are substantially different from U.S.-style handbooks.

As U.S. multinationals align HR practices around the world, cohesive global communications with employees become a priority. But overseas, comprehensive employee communication tools can be more complex than many U.S. employers might at first assume.

Why U.S. Handbooks Rarely Work Abroad

U.S.-style employee handbooks, for example, rarely work abroad. Global codes of conduct, on the other hand, can promote effective global HR management—but only if they account for a number of unexpected legal and practical issues.

Domestic U.S. employee handbooks typically spell out rules, policies, practices and benefits, and they usually include a disclaimer announcing that the document does not create a binding contract of employment.

As domestic U.S. businesses grow overseas and as HR leaders struggle to manage emerging international workforces, thoughts often turn to globalizing the company's U.S. handbook by

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Risky Volunteer Work: Self-Audits of Compensation

By Joshua S. Roffman and Alissa A. Horvitz

Since 2004, multiple-regression analysis has become the Office of Federal Contract Compliance Programs' (OFCCP) preferred approach to investigate compensation discrimination. In November 2004, the OFCCP published proposed standards on how to evaluate systemic discrimination in compensation. On the same day, it issued proposed guidelines for contractors on how to conduct self-audits of their compensation systems to identify systemic discrimination. Final standards and guidelines were issued June 16, 2006.

Many in the federal contractor community have simply accepted that because the OFCCP is evaluating systemic discrimination in compensation using multiple-regression analysis and has presented guidelines for the contractor community to assess its own practices, following the OFCCP's approach is either required or advisable. This article debunks that myth.

Federal contractors that wish to be proactive in pay equity are not well-served in evaluating compensation from a systemic perspective. Why would a contractor want to look for systemic compensation discrimination within its workforce? It wouldn't. Shouldn't a prudent contractor be more concerned with ensuring pay equity on a more individualized basis? It should.

Analyzing compensation with the same techniques that many federal contractors used prior to the OFCCP's visible multiple-regression initiative can still work very well to ensure pay equity, avoid systemic compensation problems and, at the same time, limit the legal exposure inherent in any self-critical analysis of compensation.

Contractor's Obligation

The OFCCP's regulations are located in Chapter 41, Part 60 of the Code of Federal Regulations (CFR). The only mention of the contractor's obligation to evaluate compensation is in 41

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extending it to employees worldwide, either in the same U.S. version or in a modified "rest-of-the-world" version. A global handbook addressed to a company's entire international workforce can seem a logical way to accomplish a number of important HR goals: to communicate with non-U.S. employees; to harmonize HR offerings worldwide; to propagate headquarters' culture abroad; and, to align workforces internationally.

It is unfortunate, then, that a detailed global handbook rarely works. A U.S.-style handbook imposed across a number of other countries can create a range of problems.

Creation of contractual obligation

Because employment at will exists virtually nowhere outside the U.S. (with such exceptions as Singapore), an employment-at-will disclaimer in a handbook is usually void overseas. Abroad, handbooks (even those with disclaimers) can become binding contracts.

Collective labor

Trade unions, works councils and "labor/management conferences" (which are like in-house unions) are common abroad and often enjoy rights to consult on work conditions. Unilaterally launching a U.S.-style workplace policy book can breach an employer's "information, consultation, participation" duty, which is like a U.S. mandatory subject-of-bargaining duty. And handbook terms can conflict with existing overseas collective bargaining agreements (CBAs). U.S. employers contemplating global handbooks too often forget that in many countries, "sectoral" (industry) CBAs apply by operation of law and reach even employers that never signed on.

Culture

Certain U.S. handbook provisions that make good sense stateside often raise hackles abroad.

Outside the United States, dress codes, open-door policies, smoke-free/alcohol-free workplaces, nepotism, and co-worker dating restrictions may not play well.

Also, U.S. harassment provisions often come across abroad as heavy-handed. Multinationals that respect cultural differences may decide that imposing some of these provisions globally is not worth the effort.

Conflict with local law

Many U.S. handbooks detail practices on topics regulated abroad—for example, recordkeeping, holidays/vacation, leave, breaks, overtime, pay period, direct deposit, grievance procedures, hotlines, grounds for discipline, health benefits, bonuses, co-worker dating, and benefits for part-time workers. On these topics, a one-size-fits-all approach will often conflict with overseas laws.

This very specificity of overseas employment rules diminishes the need for a U.S.-style handbook abroad. In Europe, laws already mandate a written statement of employment terms (although these statements are often in the form of contracts, much different from U.S.-style handbooks). Written works council and trade union agreements spell out other terms. Many non-U.S. employees already know their rights. A handbook may add little.

Alternatives to Handbooks

If a global U.S.-style handbook presents so many problems, what can a multinational employer use as an alternate employee communication tool? Depending on the company's specific needs, several options exist.

These options include:

- Global "welcome" booklet, describing company and culture.
- Aligned handbooks.
- Audit/inventory of overseas HR policies/practices followed by global alignment initiative. (When U.S. HR considers a global handbook, the underlying need sometimes is helping headquarters learn about, and align, HR practices across the overseas offices. A global HR audit/inventory/alignment project may meet this need without the drawbacks of a handbook.)
- Global code of conduct (setting big-picture policies on discrimination, harassment, improper payments, the Sarbanes-Oxley Act (SOX), the Foreign Corrupt Practices Act (FCPA), antitrust, confidentiality, hotline(s), and compliance/sweatshop issues—but sidestepping handbook topics like vacation/holidays, hours, pay, dress code, overtime, discipline, breaks, leave, part-time, dating, nepotism, smoking/alcohol and benefits).

Launching a Global Code of Conduct

This last alternative—a global code of conduct—is emerging as a crucial tool for aligning HR globally. In many contexts, it amounts to a "best practices" substitute for a global handbook.

Global codes of conduct can, and do, work well, but lurking within every global code of conduct is a range of often-neglected legal issues that employers need to address if they want codes that are globally enforceable. First, we should define our term. Within corporations today, a range of very different documents bear the title "code of conduct." The two most common are ethics codes of conduct and sweatshop codes of conduct.

Corrections and Clarifications

An October/November 2006 *Legal Report* article, "Reconciling the FMLA with State Leave Laws," said that a leave law in Massachusetts covers employees who have worked at least six months, not three, as the state's maternity leave law actually requires. In addition, Kansas does not have a state family and medical leave law or rule for private employers. Minnesota's parental leave law applies to employers with 21 or more workers at one site; its school conference leave law applies to all employers. State leave laws that cover smaller employers than does the FMLA include pregnancy (not more general family and medical) leave laws in Iowa, Louisiana and Montana.

Many multinationals' codes of conduct are rulebooks setting out ethical standards for complying with mostly U.S. laws that have cross-border effects, such as anti-bribery, anti-fraud, anti-discrimination and antitrust rules. Today's heightened attention to SOX and FCPA compliance, as well as general ethics and good corporate governance, push multinationals to launch these codes of conduct.

Among multinationals such as apparel manufacturers and retailers that source products from developing countries, a code of conduct is usually a very different policy—one that sets a baseline of minimum labor standards chiefly for employees of overseas supplier/contractor companies—to guard against accusations of sweatshops. These multinationals contractually require their foreign suppliers and contractors to adhere to sweatshop codes of conduct, so that suppliers' employees enjoy better-than-substandard conditions.

In rolling out global codes of conduct, be they ethics or sweatshop codes, challenges arise that mulitnationals too often overlook. Whenever headquarters imposes new rules (such as via a code of conduct) on employees of an overseas subsidiary or contractor, headquarters issues commands to those it does not directly employ. This spawns potential problems. Here is a list of these problems, as well as "best practices" tips for addressing them.

Dual employer

When U.S. headquarters imposes a global code of conduct, the employees of an overseas subsidiary or contractor could claim the U.S. parent has now started setting some of the terms and conditions of their employment and, under local law, has become a joint employer, jointly liable for employment claims along with the local entity. This "dual employer" theory, which presents a particular risk in Latin America, might even theoretically implicate tax issues, to the extent imposing the code means the U.S. parent now transacts business directly in-country as a "permanent establishment."

To avoid this problem, a best practice is for the parent to direct the code of conduct only to the overseas subsidiaries and contractors, not to their respective employees. Each overseas entity ratifies the code and imposes it directly. Currently, U.S. multinationals tend to do this as to sweatshop codes of conduct (imposed on suppliers). But multinationals seem far less vigilant as to having subsidiaries ratify ethics codes.

Inapplicable headquarters' policy

The flip side of the "dual-employer" coin is that an overseas subsidiary's employees might contest discipline imposed for violating a headquarters' code of conduct, arguing the rule came from a foreign nonemployer with no direct authority to set work conditions or to discipline local (subsidiary) employees. The argument gets even stronger if local corporate law or the subsidiary's bylaws require local directors to approve certain policies, such as rules relating to financial matters.

This is yet another reason for local subsidiaries formally to adopt or ratify a headquarters' code.

Clash with local practice

Overseas HR staff need to account for the local ramifications of a headquarters' code of conduct that clashes with local practice and customs. Inconsistent, unaligned rules can wreak havoc.

A prime example is age discrimination. U.S. multinationals routinely issue global codes of conduct that prohibit discrimination on, among other grounds, age. But age-discrimination concepts remain undeveloped abroad.

Another example involves local overseas laws that go farther than analogous topics covered in U.S.-drafted handbooks. Consider again groups protected by discrimination law: global U.S.-issued handbooks tend to prohibit discrimination on grounds prohibited in the U.S. (gender, ethnicity, race, religion, age, disability and veteran status). But, overseas laws add yet other categories, including, in Europe for example, political opinion, political belief, temporary status and part-time status. (The widespread U.S. practice of withholding benefits from part-timers is, in Europe, illegal discrimination.)

A one-size-fits-all list of protected categories based on U.S. concepts, therefore, falls short of local laws. Even adding a catch-all clause like *"and any other category protected by applicable law"* is not effective HR, because an employee cannot understand the work rule without doing legal research.

As a similar and related example, many countries prohibit workplace "bullying" and "mobbing." U.S.-drafted definitions of "harassment" tend to fall short of these laws: under U.S. definitions, illegal harassment is a form of discrimination, whereas bullying and mobbing laws prohibit rude workplace behavior unconnected to status in a protected category.

Business Ethics in the Global Arena

For more information on codes of conduct, see the online version of this article at **http://www.shrm.org/hrresources/lrpt_published/toc.asp#co**. There you will find links to:

- A Briefly Stated article on business ethics in the global arena.
- A Briefly Stated article on codes of conduct.
- A Legal Report article on the Sarbanes-Oxley Act.
- A SHRM Global HR Library article on the Foreign Corrupt Practices Act.

For an archive of past Legal Report articles, as well as other resources on workplace law, visit **www.shrm.org/law**.

Misinterpretation

The global codes of conduct issued by headquarters can be misunderstood, misinterpreted or ignored by local overseas HR.

U.S. multinationals have had trouble getting traction with typical U.S. code-of-conduct provisions on harassment and diversity, and it has taken years for overseas subsidiaries to take FCPA provisions seriously. These problems persist with today's SOX provisions, which strike many non-U.S. employees as heavy-handed.

Global codes of conduct enforcing U.S. values need to be rolled out proactively, with sophisticated communications fostering local engagement.

The reasons that underlie provisions in a typical ethics code of conduct are obvious to U.S. employees; the challenge is to see the code through the eyes of non-U.S. employees.

Mandatory subjects of bargaining

As mentioned regarding employee handbooks, works councils and labor/management conferences in Europe, Korea, Taiwan and elsewhere have a right to "information and consultation" before an employer launches new work rules.

Where trade unions are powerful, provisions in a new code of conduct might be mandatory subjects of bargaining. A best practice is to involve local HR—early and often—in implementation. Local involvement will slow down a code-of-conduct rollout, but building in needed time for local HR to meet with labor representatives will enhance enforceability and local compliance.

Individual employment contracts

Just as collective labor agreements can obstruct global codes of conduct, so can individual employment agreements. Employees overseas commonly are parties to written individual employment contracts. Laws from the European Union to China to Colombia to Mexico actually require written contracts or statements.

The texts of employees' individual contracts, therefore, should reference applicable HR policies—especially codes of conduct that enforce U.S. laws like SOX and the FCPA. Overseas, labor court judges can be reluctant to enforce rules based on U.S. laws, which they may see as encroaching on local sovereignty. One strategy is to get non-U.S. employees themselves to commit to follow key policies—in writing, in their contracts.

Version in local language required

U.S. multinationals are too prone to release codes of conduct only in English.

Some jurisdictions (Belgium, Chile, France, Poland, Portugal, Quebec and others) mandate that employee communications be in the local language—even where a company claims its "official language" is English. In other countries (Costa Rica and Spain are examples), work rules in a nonnative language like English can be all but impossible to enforce under law.

Translations of Handbooks Within the United States

As U.S. immigration and diversity crescendo, companies in the United States increasingly find themselves employing nonnative workers who speak little or no English.

This raises an ever-more urgent need to translate employee communications for local U.S. workforces—such as monolingual U.S. workers speaking only Spanish, Chinese, Polish, Portuguese or other languages. A U.S. company that employs enough U.S. workers who speak no English may ultimately decide it needs a version of its U.S. company handbook in another language; otherwise, the non-English-speaking workers in effect have no access to the document. What are best practices for employers translating U.S. handbooks for non-English-speaking U.S. workers?

Bad Translations

We have all seen comically bad translations into English. Too many companies have used a bilingual secretary, HR expert or other on-hand but nonprofessional translator to draft a translation—and gotten what they paid for. Get a good translation done professionally, preferably by a native speaker. Consider encouraging the translator to pepper it with contextual explanations of concepts that would be unclear, in a literal translation, to workers from abroad. For example, U.S. handbook provisions on employment at will, exempt vs. nonexempt, vacation accrual, and 401(k) plans may need background for readers born outside the country and with little U.S. work experience.

After a professional translator prepares a draft, a best practice is to get that draft reviewed by a bilingual U.S. employment lawyer and a bilingual U.S. HR generalist.

'English Controls'

In the translated version, add a prominent disclaimer saying (in the foreign language): "This is a translation of an English-language document, for your convenience only. The text of the English original shall in all respects control your rights and obligations. The English original is available on request from Human Resources."

ERISA Mandate

Beyond handbooks, suppose a U.S. employer offers plans regulated by the Employee Retirement Income Security Act (ERISA) and with formal summary plan descriptions. If that employer has enough employees "literate only in the same non-English language," then ERISA regulations affirmatively require "a notice, *in the non-English language common to these [plan] participants*, offering them assistance" with the plan (presumably) in their local language. See 29 CFR §2520.102-2(c) (emphasis added). Any U.S. employer needing to translate a U.S. handbook for non-English-speaking U.S. employees should also check its ERISA plans to ensure they contain at least this required foreign-language notice.

In all countries, codes of conduct need to be understandable to the local workforces and to local labor judges. No one would expect a judge in Tennessee or Kentucky to enforce a Japanese- or German-language work rule against a local auto worker. Labor judges overseas will be just as hostile to rules written in languages other than their own.

And translation is a special issue as to sweatshop codes of conduct imposed on the employees of contractors and suppliers in developing countries. U.S. multinationals have drawn public criticism for announcing they launched tough sweatshop codes of conduct that, in fact, were never communicated in local languages to the developing-country workers whom the codes were purported to protect.

Internationalization of Business

The internationalization of business drives the globalization—and the cross-border alignment—of U.S. multinationals' worldwide workforces.

The most likely substitute for a U.S.-style handbook to be rolled out worldwide is a global code of conduct. A global code of conduct can be an excellent HR practice, but it will likely raise a host of challenges for any multinational concerned about compliance with best practices and overseas laws.

Global HR communications and policies—even translated U.S. handbooks aimed merely at non-English-speaking U.S. workers—spawn projects substantially more complex than they first appear.

But managing global HR communications effectively can yield enforceable HR tools that sidestep the inevitable pitfalls of hastily conceived global HR initiatives. ◆

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C.F.R. §60-2.17(b)(3). In relevant part, the regulation states:

> The contractor must perform in-depth analyses of its total employment process to determine whether and where impediments to equal employment opportunity exist. At a minimum, the contractor must evaluate ... [c]ompensation system(s) to determine whether there are gender-, race-, or ethnicity-based disparities.

Nothing in the OFCCP's standards for evaluating discrimination in compensation or the voluntary self-evaluation guidelines has changed whether other types of compensation analyses satisfy the federal contractor's obligations under this provision. What was lawful and compliant before is lawful and compliant still.

Prior to the OFCCP's emphasis on multiple-regression analysis, many contractors elected to evaluate their compensation systems without specifically emphasizing systemic patterns but rather by ensuring equity within job title, job grade, job family, as well as between job titles, job grades, job families and the like. If a federal contractor was ensuring pay equity in these smaller categories, it should follow that the contractor would avoid systemic problems in compensation discrimination.

This raises the question—why is it in the interest of a contractor to try to identify systemic patterns which, if found, will require significant attention by the contractor and, if found by the OFCCP or a plaintiff's attorney, will lead to significant financial remedies and exposure?

OFCCP's Investigation Standards

Recognizing the law as set forth in court cases dealing with systemic compensation discrimination, the OFCCP issued standards explaining how it intends to assess contractor compensation practices.

The OFCCP's standards focus on identifying systemic patterns of compensation discrimination by grouping contractors' workforces into similarly situated employee groups (SSEGs) and performing multiple-regression analyses on these groups using the variables that influence compensation, including race and gender. Employees are similarly situated "if they are similar with respect to the work they perform, their responsibility level, and the skills and qualifications involved in their positions."

The OFCCP will find systemic compensation discrimination when "there are statistically significant compensation disparities between similarly situated employees, after taking into account legitimate factors which influence compensation." In its standards, the OFCCP lists education, experience, performance, productivity and location as examples of legitimate factors that influence compensation.

Federal contractors should be asking themselves why the OFCCP is looking at compensation this way and, specifically, why the OFCCP is looking at it on a systemic basis.

Like any government agency, the OFCCP has limited resources and must compete for budget dollars with the rest of the federal government. As such, it is in the OFCCP's interest to use its resources efficiently and to have tangible results from its investigative efforts to lobby for its fair share of dollars in each successive federal budget.

It is simply not pragmatic for the OFCCP to use its investigative resources to evaluate individual pay inequities. However, if the OFCCP can pinpoint systemic pay inequities and recover millions of dollars in remedies, it has used its resources efficiently while fulfilling its mandate of remedying discrimination in compensation, among other areas.

It is logical that the OFCCP would choose to analyze compensation this way. That does not mean that it makes sense for employers to do the agency's work for it. They shouldn't.

Voluntary Guidelines

The voluntary self-audit guidelines were presented as an opportunity for con-

tractors to examine their own compensation systems. Under the guidelines, the contractor develops its own SSEGs, conducts its own multiple-regression analyses, implements back-pay remedies where it has found statistically significant disparities that cannot be explained, saves all of its documentation created during this process, shows that documentation to the OFCCP in an audit, and, if it does all that, it has the chance to receive "coordination" from the OFCCP in a compensation audit.

It is hard to view the self-audit guidelines as anything more than the OFCCP's attempt to have the contractor community do its work for it. For the same reasons that the OFCCP chooses to focus on systemic pay inequities rather than on individualized pay inequities (budgetary and resource constraints), the OFCCP hopes to have the contractor community conduct OFCCP's audits for it. It is another way for the OFCCP to achieve results using limited resources.

But what benefit can the voluntary self-audit guidelines offer the contractor? The only thing that the OFCCP offers in return is its Contractor Coordination Incentive (CCI). The OFCCP is willing to give the federal contractor a measure of "deference" in a compliance review but only if the contractor:

- Develops SSEGs, which groups would have to be acceptable to the OFCCP, must cover at least 70 percent of the employer's workforce, and must consist of no fewer than 30 employees with at least five from each protected category (five males, five females, five minorities, five nonminorities).
- Annually performs a multiple-regression analysis on the SSEGs.
- Investigates any statistically significant compensation disparities identified by the self-evaluation and provides appropriate remedies for those disparities that cannot be explained.
- Contemporaneously creates and maintains (for two years) several documents (see the sidebar).

Honestly, this is not much of an incentive. The OFCCP is in essence saying, "Do our work for us the exact way we want you to do it, and we'll let you do our audit work for us!"

OFCCP's Guidelines and Enforcement

For more information on the OFCCP's voluntary self-audit guidelines, see the online version of this article at **http://www.shrm.org/hrresources/lrpt_published/toc.asp#co**. There you will find links to:

- An *HR News* article on the final self-audit guidelines.
- An *HR News* article on the OFCCP's emerging enforcement approach.

For an archive of past *Legal Report* articles, as well as other resources on workplace law, visit **www.shrm.org/law**.

Risks for Volunteers

Federal contractors that agree to apply the voluntary guidelines face many risks. For example, all documentation related to those analyses will not be privileged. The ramifications of this approach are potentially severe.

The contractor will have prepared an analysis that identifies statistically significant compensation disparities against females or minorities based on groupings that it has now endorsed. Having identified these disparities, the OFCCP is going to expect the contractor to make appropriate compensation adjustments, retroactively and prospectively.

Even for the federal contractor that makes these adjustments, if the adjustments fail to address compensation inequities adverse to men and nonminorities, the contractor has laid the foundation for a reverse discrimination suit against it. Moreover, having disclosed its analyses to the OFCCP, those analyses could potentially become available to third parties pursuant to a Freedom of Information Act (FOIA) request and, in any event, would be discoverable in litigation. Any argument that these analyses are privileged was lost the instant the contractor submitted them to the OFCCP.

Federal contractors that do not engage in coordination compliance face substantial risk in developing multiple-regression analyses of their compensation systems using SSEGs. Although contractors can put in place certain safeguards to ensure that such analyses remain privileged, there is no guarantee that the courts will recognize them as such.

Moreover, federal contractors will be looking to do their analyses on an establishment basis to conform to the structure of their affirmative action plans. Having developed SSEGs and regression formulas for one establishment, contractors run the risk of having adverse parties argue, sometimes

Lots of Documents, No Protection

Contractors that elect to follow the voluntary self-audit guidelines must contemporaneously create and maintain for two years several documents, including:

- Documents that explain and justify the formation of the SSEGs and the exclusion of certain employees from those SSEGs.
- The data used in the statistical analyses and the results of those statistical analyses.
- The data and documents related to nonstatistical methods used for employees who were not evaluated using multiple-regression analysis of SSEGs.
- Documentation related to the follow-up investigation into the statistically significant disparities, the conclusion of such investigation, and any pay adjustments.

In addition, to obtain the benefit of the OFCCP's coordination in a compliance review, the contractor must make available all the above data and documents.

successfully, that the same SSEGs and formulas should be used at other locations. Not knowing necessarily what the results of those analyses would show when applied to other establishments, the contractor may be stuck with unforeseen liabilities.

The best way to protect against that, within the multiple-regression analysis framework, is to develop different SSEGs for each establishment and different regression equations for each SSEG. Of course, doing so significantly increases the contractors' costs in assessing their compensation systems.

Most contractors put little thought into developing their SSEGs. Rather, they use pre-existing groupings that were not developed for the purpose of grouping employees who are similar with regard to compensation practices. Multiple-regression analyses evaluating compensation practices are mostly meaningless if they are not being used to examine employees who are similarly situated.

In addition, federal contractors frequently are not fully committed to developing robust multiple-regression equations that take into consideration many of the most important factors that influence compensation. Rather, contractors have a tendency to develop multiple-regression equations using only those variables that the contractors maintain in their human resource information system database.

For example, contractors will often admit that an individual's prior relevant experience and level of education and degree are among the most important factors that influence setting initial compensation upon hire. But many employers do not obtain this information from their new hires and do not maintain it in their systems.

Contractors often use age as a proxy for overall experience. Age, however, has been shown to be far from a perfect proxy, as it tends to overstate the prior experience of female employees, who are more likely to take breaks from the workforce for family reasons. Another potential influencing factor is the salary earned at the individual's prior place of employment. Although that information may be available on the application, it is rarely entered into the employer's database. Some employers also state that compensation increases are tied to performance, yet we often see that performance ratings have little correlation to employee compensation levels.

In any event, analyzing compensation to identify individualized pay inequities, rather than systemic discrimination in compensation, avoids the potential ballooning effect faced by a contractor who, in simply trying to do the right thing, uses multiple-regression analyses focused on systemic compensation problems to analyze its compensation practices.

Alternative Steps

As already noted, the OFCCP's multiple-regression initiative has done nothing to change the scope of the contractors' regulatory obligation to evaluate their compensation systems.

Initial compensation setting and annual merit increases are not made at a systemic level. Typically, an employer examines other employees in the same or similar jobs in the same or similar departments to set the initial salary and also to determine how to allot pay increases.

For initial salary, the employer often asks what the employee was making at his or her prior job and what the market demand is for the employee's skill set at the time of hire. It follows that contractors should evaluate their employees' compensation for pay equity in the same way they look at compensation when hiring and making annual pay adjustments. The contractor that vigilantly does this type of analysis will generally avoid systemic problems.

More importantly, by looking at compensation on a more individualized basis, the contractor avoids opening a Pandora's box filled with exposure to systemic compensation discrimination claims from various actors, be it the OFCCP or private litigants. A federal contractor's multiple-regression analyses are a roadmap for adverse parties on how to bring systemic compensation claims. If the contractor endorses the analyses, it will be substantially more difficult for the employer to discredit the use of these or similar analyses in other contexts.

By looking at compensation on a more individualized basis, the contractor avoids opening a Pandora's box.

Outside of defending litigation specifically alleging compensation discrimination, there are, however, two instances in which an employer might want to evaluate its compensation practices to ensure pay equity:

- In preparation for or in response to an OFCCP audit.
- As part of the employer's annual merit increase process.

OFCCP Audits

The OFCCP's initial audit scheduling letter requests only total compensation and total number of employees categorized by either salary range, rate, grade or level and broken out by race and gender.

Obviously the OFCCP cannot develop a multiple-regression analysis from only this information. Accordingly, the OFCCP has put in place a three-tiered approach to its compensation investigations.

- The first tier involves looking at the contractor's desk audit submission to see if a disproportionate percentage of females or minorities are in groups

where their average compensation is below that of their male and nonminority counterparts, respectively. If the OFCCP finds a substantially greater proportion of females or minorities are disfavored in the information provided in the desk audit submission, it typically seeks from the contractor additional information, which the OFCCP will use to develop cluster regression equations.

- The cluster regression analysis is the OFCCP's way of developing employee groupings to perform multiple-regression analyses without having all the information it needs to develop legitimate SSEGs. If the cluster regression still reveals indicators of systemic compensation discrimination, the OFCCP will gather the detailed information it needs to develop legally defensible SSEGs and to determine what variables influence compensation.
- This final step in the OFCCP's investigation is time-consuming and involves reviewing volumes of documents and interviewing managers, employees and compensation personnel. In addition, it typically takes several months before the OFCCP ever gets to this point in its investigation, because the first two tiers usually occur over that period of time.

Often, the investigation into compensation will end at the desk audit submission because there will be no indicators that would cause the OFCCP to request follow-up information for a systemic compensation case.

In those instances where a federal contractor finds that the OFCCP has moved to the third tier of its investigation, a contractor will still have ample time to develop its own multiple-regression analyses to counter any analyses that the OFCCP is developing. It is our view that this is perhaps the only instance when it makes sense for a contractor to evaluate its compensation systems through a systemic lens: when the OFCCP itself is engaging in such an analysis.

Otherwise, regularly evaluating individual pay practices for internal equity will more than suffice to meet the contractor's regulatory obligations and, if done vigilantly and correctly, should work to eliminate any systemic problems. Moreover, a contractor will not establish a systemic framework for others to use against it in an audit or litigation context.

Responding to Class Actions

In addition, there may be instances where an employer is faced with a class action alleging systemic discrimination in compensation. Obviously in defending such a lawsuit, it makes eminent sense to look at compensation on a systemic level, investing the appropriate resources to make sure that all the relevant variables influencing compensation are accounted for and that employees are grouped appropriately.

This is expensive. The effort is worthwhile in defending a class action because the very concerns that have been raised regarding looking at compensation on a systemic level are immaterial once the lawsuit has been filed.

The Little Picture

Simply developing multiple-regression analysis to see if there is any exposure to such lawsuits may in fact be the very thing that puts the company in a difficult position in defending such lawsuits. It is not in the contractor's interest to look at this on a systemic basis.

When an employer ensures pay equity on a micro level, it has the corresponding effect of avoiding systemic compensation disparities without presenting the multitude of risks associated with developing a multiple-regression analysis. The OFCCP's voluntary self-audit guidelines offer too little incentive and too much risk to be attractive to federal contractors. ◆

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