HUMAN RESOURCES MANAGEMENT: BIG PROBLEM FOR SMALL BUSINESS?

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ABSTRACT

In order for a growing small business to be successful it must have highly motivated, competent, and content employees. The employee’s goals must be aligned with the business’ goals in order for the employer to foster employee motivation. For employers to grow such a workforce they need to have human resource strategies that support the alignment of business and employee goals. The business must create a win-win situation.

Frequently, small business owners have excellent knowledge of their particular field or core competency. However, research has indicated that many small business owners-managers lack important knowledge related to labor law compliance and human resources (HR) management. In addition, those who may have an adequate knowledge in the HR field do not have the structure in place to effectively support HR initiatives.

This study focuses on four HR facets of small business companies to ascertain their level of knowledge and provide suggested areas where small business owners need training. A questionnaire survey was conducted with small business owners in the southern United States. The focus of this study includes: (1) Legal Compliance – Fair Labor Standards Act; (2) Recruiting, Screening, and Hiring Employees; (3) Employee Relations, Training, and Documentation; and (4) Miscellaneous HR Questions.

HRM: BIG PROBLEM FOR SMALL BUSINESS?

Are small business owners comfortable with their level of knowledge in employment legal compliance? Overall, do they have an adequate knowledge of human resources (HR) laws and standards? Do they feel confident when they recruit, interview, hire, motivate, discipline, and even discharge employees? To answer these questions, hundreds of small business owners and managers throughout the southern United States were surveyed.

It is worth noting that small businesses create most of the nation’s new jobs, employ about half of the nation’s private sector workforce, and provide half of the nation’s nonfarm, private real gross domestic product (GDP), as well as a significant share of innovations (SBA, 2009).
Small firms also make important contributions to the economy through innovations and the creation of jobs, enterprises, and entire new industries. Small firms are still struggling mightily from the recessionary economy of 2008—and if the past is an indication, they will likely help lead the economic recovery (SBA, 2009). It is widely understood that small firms are a vital part of our nation’s economic engine. Therefore it is important that these firms operate their businesses in a legally compliant as well as profitable manner. This will improve their likelihood for success and foster lawsuit avoidance.

LITERATURE REVIEW AND RESEARCH RATIONALE

The focus of the study includes four parts: (1) Legal Compliance – Fair Labor Standards Act; (2) Recruiting, Screening, and Hiring Employees; (3) Employee Relations, Training, and Documentation; and (4) Miscellaneous HR Questions.

(1) Legal Compliance – Fair Labor Standards Act

Anne Field (1998) reported that from 1971 to 1991, the number of employment law disputes filed in federal court rose by 430%, a larger increase than for all other types of cases, according to a study by the Commission on the Future of Worker-Management Relations, an advisory body appointed by President Clinton. Steven Irwin (2007) explained that far too many small business owners wrongly assume the Fair Labor Standards Act (FLSA) does not apply to them or their employees. This mistake can be costly and often when an employer realizes the error, it is too late to avoid financial liability. Irwin (2007) also reported that the U.S. Department of Labor’s Wage and Hour Division recovered more than $212 million in back wages, a 21 percent increase over the record-setting amount in 2002. The Wage and Hour Division undertook an investigation-based compliance survey of identified low-wage industries in fiscal year 2006. The initiative was designed to measure FLSA compliance in those industries most likely to have minimum wage and overtime violations.

Richard Acello (2010) asserted that, in 2008, sales associates sued AT&T Mobility in federal court in New York City for back pay and unpaid overtime spent responding to e-mails after work hours. Acello added, with workers seeking pay for such after-hours work, companies are wrestling with policies for smartphone use. Larger employers are bracing for an onslaught of class action suits.

According to another AT&T overtime class action lawsuit, managers “were illegally and grossly under-compensated for their work” and “routinely and consistently work alongside other employees, similarly situated, who are remunerated on a basis that includes payment for hours worked in excess of 40 hours per week.” The AT&T managers are seeking three years of back pay with damages doubling that amount – a figure that could total tens of millions of dollars.
Two additional overtime class action lawsuits are currently pending against AT&T in Georgia and California. The telecom giant has settled eight overtime cases in the last four years for a combined total of $65 million, according to the plaintiff attorneys in the Connecticut case, *Sharon L. Perkins, et al. v. Southern New England Telephone Co.* (Mirando, 2011)

Although AT&T is obviously a large business, it would be logical that if large corporations with trained human resources professionals can make such errors then perhaps small businesses are making the same errors. These errors certainly could expose even small businesses to lawsuits.

According to the Department of Labor’s Bureau of Labor Statistics, approximately 10.3 million workers, representing 7.4 percent of the American workforce, were treated as independent contractors in 2005. Many of these individuals may have been misclassified as independent contractors, either intentionally or as a matter of genuine confusion, by the employer about how to classify the particular worker. The classification issue is important to employers as well as the government, since independent contractors are not entitled to the protection of federal laws such as FLSA or Title VII of the 1964 Civil Rights Act, and other statutes.

(2) Recruiting, Screening, and Hiring Employees

Small businesses continue to face challenges in the current climate, including accessing capital in the midst of financial instability. Over the longer term, small firms face concerns about the cost and availability of health insurance, attracting a quality work force, meeting global competition, and perennial concerns about regulation, taxes, and government procurement opportunities (SBA, 2009). Small businesses must compete effectively for labor with their larger counterparts. This is more difficult in light of the disparity in total compensation, especially benefits. This disparity results in greater employee turnover. Firms that offer benefits have a 26.2 percent lower probability of having an employee leave in a given year (SBA, 2009).

Kotey & Slade (2005) reported that it is expected as firms grow, the skills and abilities required to perform various functions and activities no longer would be available from the familiar and informal recruitment sources preferred by the owner-manager. Thus, a greater variety of formal recruitment sources would be used to attract suitable candidates. As firms grow, multiple selection techniques would be used, in addition to interviews, to reduce errors in selecting employees recruited from sources unfamiliar to the owner-manager.

Heneman and Berkley (1999) studied the application practices and outcomes among small businesses. The content domain of attraction practices included ten areas: (1) methods to establish job requirements; (2) recruitment sources and methods; (3) recruitment communication; (4) selection methods; (5) who takes part in evaluation of applicants; (6) method of making job offers; (7) methods of determining starting pay; (8) special pay systems; (9) benefits; and (10) special inducements.
The above-mentioned application attraction practices and their linkages to four attraction outcomes (applicants/vacancy, days-to-fill, acceptance rate, and retention rate) were investigated. Use of previous practices as well as many others (special hiring inducements, for example) were found and these varied according to company size, industry, and presence of an HR department. Another example, using both past applications and newspaper ads as recruitment sources resulted in fewer days-to-fill vacancies providing promotion possibilities. New employee training programs resulted in higher acceptance rates.

Heneman and Berkley (1999) reported a major knowledge gap regarding the attraction practices actually used by small businesses and the effectiveness of those practices. At a time when small businesses need strong human resources management practices to manage their growth, the HR function is typically an underdeveloped functional area in the organization. This important void needs to be filled if small businesses are to learn how to effectively attract a more a qualified workforce, which is a key component of overall management of the firm’s human resources.

Glenn McEvoy (1984) sought information about usage of HRM practices in HR policy and strategy, staffing, performance evaluation, motivation, compensation and benefits, job satisfaction, and turnover. McEvoy found that job advertisements and walk-ins were the most widely used (67 percent) recruitment methods, and that interviews and application blanks were the most widely used (90 percent) selection techniques. In addition, while most firms (90 percent) conducted performance appraisals, relatively few attempted to relate pay raises to appraisal results.

Hornsby and Kurato (1990) found that firms of all sizes used primarily informal and inexpensive recruitment and selection techniques with employee referrals and the interview process being the most highly used and rated of the recruitment and selection techniques. Deshpande and Golhar (1994) discovered that the results of nine recruitment sources yielded almost identical results for both small and large firms. Specifically, job posting was used most frequently, followed by promotion, employee referral, temporaries, transfers, advertisements, employment agencies, educational institutions, and previous applicants. Both large and small firms used interviews extensively (90 percent).

Demographic trends in the coming years may exacerbate the challenges for small businesses in employee recruitment and retention. The Baby Boom generation comprises 78.2 million Americans born between 1946 and 1964, and the first wave of this group has already begun to retire, a process that will accelerate over the next decade. These retirements pose two problems for businesses large and small. First, firms will see a mass exodus of institutional knowledge that will be hard to replace in certain fields. Second, the departure of this large generation from the workforce could lead to labor shortages in some industries. Labor shortages mean that firms may need to compete for skilled workers, and small businesses are sometimes at a competitive disadvantage in outbidding larger firms (SBA, 2009).
(3) Employee Relations, Training, and Documentation

Many new employees come equipped with most of the KSAs (knowledge, skills, and abilities) needed to start work. Others require extensive training before they are ready to make much of a contribution to the organization. The term training is often used casually to describe almost any effort initiated by an organization to foster learning among its members. However, many experts distinguish between training, which tends to be more narrowly focused and oriented toward short-term performance concerns, and development, which tends to be oriented more toward broadening an individual’s skills for future responsibilities. The two terms tend to be combined into a single phrase – training and development – to recognize the combination of activities organizations use to increase the knowledge and skills of employees. (Snell and Bohlander, 2010)

Training is time consuming, but an investment in training can result in increased worker competence and motivation. The business benefits through increased productivity and profitability. Training is not always the answer to a performance problem. There may be other causes such as poor management or conditions beyond the employee’s control. For these reasons it is important to approach training as a systematic process. (Stetar, 2005)

Research shows that an organization’s revenues and overall profitability are positively correlated to the amount of training it gives its employees. According to Training magazine’s ongoing industry report, U.S. businesses spend about $50 billion annually to provide each of their employees with about 25 hours of training annually (Bohlander & Snell, 2010). By contrast, the 100 best U.S. companies to work for, as cited by Fortune magazine, provide their employees with approximately double that amount of training and sometimes even more. New employees hired by the Ritz Carlton hotel chain get over 200 hours of training (Bohlander & Snell, 2010).

King, Solomon, and Fernald Jr. (2001) stated that previous literature on family businesses suggests family businesses have difficulty managing their human resources, especially when it concerns a family member or the transition from the founder to the successor. Their study examined the correlation between the subjects’ potential capability (PC) and the supervisors’ assessment of the managers’ performance, additional analyses were conducted to determine which subjects had a PC rating that did not align with the complexity of their assigned roles (King et al., 2001). With few exceptions, the borderline individuals are functioning at levels lower than or barely equal to the complexity level of their position. Thus it appears that the organization is not effectively managing its human resources. Specifically, managers are not placed in positions for which they qualify.

Terry Wager (1998) asserted that relatively little research has focused on human resource management practices in small firms. His study investigated the incidence of ten human resource management practices. Respondents were most likely to report sharing business information with employees and having an orientation program for new employees. The study
also examined whether the presence of such practices was related to characteristics of the organization. The most dominant finding was the very strong relationship between human resource practices and progressive decision-making ideology.

Wager (1998) suggested firms that encouraged open communication, participation in management decisions, and a systematic search for opportunities were more likely to have implemented practices. The relationship between progressive decision-making ideology and each of the practices was highly significant. A conclusion was that firm size was an important predictor of human resource management practices. Very small firms were much less likely to have adopted most of the human resource management practices examined in this study. The presence of a formal performance appraisal system and an HRM department were significantly more likely to exist in firms with a minimum of 100 employees.

Kotey and Slade (2005) used data to demonstrate a move toward division of labor, hierarchical structures, increased documentation, and more administrative processes as the number of employees increase. The adoption of formal employment procedures at the managerial level will lag behind that at the operational level for small firms, as owner-managers prefer to employ the few managers required from family and friends. Few owner-managers have formal and professional policies on human resource-related issues such as promotions, incentives, and disciplinary action.

Carlson, Upton, and Seaman (2006) suggested that training and development, recruitment package, maintaining morale, use of performance appraisals, and competitive compensation were more important for high sales-growth performing firms than for low sales-growth performing firms. They found that these activities do in fact have a positive impact on performance. In addition, they suggested that high sales-growth performing firms used more cash incentive compensation at every level in the organization.

Heneman and Berkley (1999) found in their study of 117 small businesses that providing cost-of-living increases, promotion possibilities, and having the HR manager evaluate job applicants lead to higher retention rates. Desphande and Golhar (1994) asserted the ratings of importance of numerous HRM practices to the firms’ operations revealed that the top five practices for both large and small firms were open communication, pay based on performance, competitive wages, training new employees, and job security.

(4) Miscellaneous Hr Questions

Deshpande and Golhar (1994) summarized to be successful in a global market, a small firm needs a highly motivated, skilled and satisfied workforce that can produce quality goods at low costs. However, to develop such a workforce, a firm has to implement an appropriate human resources management (HRM) strategy. In practice, other functional management areas such as finance, production, and marketing usually get preference over personnel management. This lack of understanding of HRM issues and their importance in the operation of a successful
business has impacted many small firms. Deshpande and Golhar (1994) determined that HR managers of both types of firms preferred to fill vacancies from within the organization and used job posting and bidding extensively. While one-on-one interviews and written tests were popular among both large and small firms, small firms made more extensive use of job tryouts.

For the past course of four years, we have partnered with a Small Business & Technology Development Center to offer business owners HR and OSHA reviews. We have partnered with students in Human Resources Management courses to perform these small business reviews. The student group, along with one of authors as the facilitator, reviews the required HR labor law postings, potential safety or OSHA violations, fire protection, personal protective equipment, general work environment, walkways, stairs, exits, and power sources looking for opportunities for improvement for the small business owner. In addition, the student groups interview the business owner asking questions about staffing, equal employment opportunity, compensation, benefits, training, employee appraisal and development, safety, documentation, and labor relations. The students provide recommendations and supporting documentation of any applicable laws or standards supporting their recommendations.

Many students groups found that small business owners did not properly display the required labor law postings. Many small business owners did not have sufficient knowledge of the Fair Labor Standards Act. Many owners had little structure or documentation practices regarding recruiting, hiring, and training employees. In addition, many owners do not have a policy manual or handbook, employee files, or performance indicators for employees.

**WHY CONDUCT THE SURVEY?**

Through these HR reviews, we saw first-hand that many small business owners are lacking knowledge in various areas of the HR realm. Although many small business owners are superb in their particular craft or field, they could use additional training regarding HR best practices. The questionnaire survey was developed to target the particular facets of HR management that the small business owners need training in the most. In essence, the questionnaire survey allowed us to develop a needs assessment for small business owners related to HR in order to develop specific training to address those needs.

Secondary research was performed to determine what information was readily available to compare with the current findings on HR training needs. Primary research was conducted in the form of the questionnaire survey. Eighty small business owners in the southern United States that were emailed the survey anonymously responded. Local Chamber of Commerce organizations were supportive and emailed the questionnaire surveys from their area Chamber offices which provided additional credibility and they supported that there was a need to conduct the survey.
ANALYSIS OF RESULTS

The survey results allowed us to identify the HR training needs that small business owners’ need. Additional HR management training programs were developed to offer regional small business owners. Of the 80 businesses that responded, 87 percent were the owner of the business, 7 percent were the manager, and 6 percent were an employee of the business other than an owner and manager.

Regarding Part One of the study (Legal Compliance – Fair Labor Standards Act), of the respondents asked to answer, “My employer/business is required to follow Family & Medical Leave Act (FMLA) standards,” 39 answered TRUE and 41 answered false. Interestingly enough, on the next question, “My employer/business has fifty or more employees,” only seven answered TRUE and 73 answered FALSE. This leaves a discrepancy of 32, or 40 percent, of respondents that believe their employer/business is required to follow FMLA standards that actually do not meet with requirement of a minimum of 50 employees. It is unknown whether the seven that answered TRUE to the prior question have 50 or more employees. The discrepancy could actually be greater than 40 percent.

When asked to answer, “My employer/business is required to post the Employee Polygraph Protection Act Notice in a conspicuous area for employees,” 45 percent answered TRUE and 55 percent answered FALSE. This is a 55 percent error rate. All small businesses who have employees on payroll must post this notice in a conspicuous area. This question was intended to indicate whether or not the employer is aware of the labor law posting requirements of their business.

When asked to answer, “My employer/business is required to follow many of the regulations listed in the Fair Labor Standards Act,” 85 percent answered TRUE and 15 percent answered FALSE. This is a 15 percent error rate. This error rate indicates that 15 percent of the respondents are either not aware of what the Fair Labor Standards Act encompasses, such as minimum wage and overtime pay legal requirements, or they are not aware that their business is required to follow the Fair Labor Standards Act. All employers are required to adhere to the Fair Labor Standards Act.

When questioned if employers were required to excuse an employee's absence while they are on military leave, 91 percent answered a correct TRUE response. This was a promising result. However, when asked the question regarding their hourly compensated workforce, “Employers are required to pay overtime (at 1 1/2 times the hourly rate) for employees who work more than 40 hours in a work week,” only 79 percent answered TRUE. This result was truly alarming, indicating that 21 percent are not aware of this legal requirement. When asked, “Employers are required to pay overtime (at 1 1/2 times the hourly rate) for employees who work more than 8 hours in a one day,” fourteen percent of the respondents answered this incorrectly with a TRUE response.
To further alarm us when asked, “The Fair Labor Standards Act states that employers must provide a lunch break for employees who work an eight hour shift,” almost all, 96 percent, of the respondents answered incorrectly with a TRUE response. However, although it is not required under the FLSA to provide breaks during an eight-hour shift, many would argue that providing periodic breaks to employees is a good employer policy and would typically result in reduced fatigue and associated affects such as a reduction in employee quality, efficiency, and safety due to fatigue.

Our conclusion to this section of the questionnaire is that there is a sufficient need for small business employers to receive training on labor laws and the required labor law posters, with specific attention to training regarding what is, and is not, required under the FLSA.

Regarding Part Two of the study (Recruiting, Screening, and Hiring Employees), 77 percent of the respondents were aware that it was inappropriate to ask an applicant their age during an interview. It is appropriate to ask the applicant if they meet the age requirements for a particular position, such as serving alcoholic beverages. However, 89 percent of the respondents realized that an employer has a legal right to ask if the applicant meets the key physical requirements of the job. A disappointing 63 percent of the respondents actually utilized written job applications when screening and interviewing potential employees. Fifty-four percent use a prepared standard list of interview questions they ask during interviews; and 86 percent of respondents conduct reference checks.

Although a large percentage of small business employers seem not to utilize employment applications, they seem to have a relatively decent grasp of recruiting, hiring, and screening. Due to the poor response regarding application usage, a need is identified for training on the importance of employment applications. It must be explained that employment applications are critical to providing documented prior employment data and determining if the applicant has the needed knowledge, skills, and abilities, needed for the position. In addition, accepting applications is a good practice in regards to avoiding perceived or actual discriminatory practices in recruiting and hiring employees.

Let us now embark on Part Three of the study (Employee Relations, Training, and Documentation). Only 51 percent of respondents indicated having a policy booklet or handbook. However, a promising 81 percent of businesses maintained a personnel file for each employee. A meager 44 percent of respondents had a documented new-hire orientation process or new job training program. Furthermore, a dismal 30 percent of respondents shared performance measures with employees such as production, customer service, safety, quality, productivity, sales, or any other company goals. It is widely accepted that sharing company performance measurements and goals with employees is critical to success. When employees’ pay is based on their performance, being measured and tied to company goals, this is typically rewarding for both the employee and the company. This in turn aligns the goals of the employee and the employer creating a win-win scenario that all employers should seek.
In contrast to the documenting performance measures, 52 percent of respondents document when an employee is rewarded. Furthermore, 69 percent of those businesses who responded documented when performing disciplinary action. It is noteworthy to mention that 26 percent of respondents have a documented drug testing policy of any kind.

Finally, Part Four of the study (Miscellaneous HR Questions). This line of questioning indicated that the vast majority of respondents categorized themselves as having average or below average knowledge of HR laws and standards. When asked what aspects of HR training would provide their organization the most benefit, “Legal Compliance” (FLSA, EEOC, payroll, etc.) came in first place by several responses with “Employee Relations / Retention / Motivation / Discipline” coming in second place. “Recruiting, Interviewing, and Hiring Employees” trailed closely in third place.

A BIT ABOUT THE SBTDC

The Small Business and Technology Development Center (ASBTDC) is funded by the Small Business Administration (SBA) and a southern state. The SBTDC conducts several training seminars each year to assist small businesses with planning, implementing, and improving business operations. These seminars are designed to provide entrepreneurs with information that will assist in strengthening their businesses which are the backbone of the economy and provide jobs in increasing numbers each year. This study was undertaken for the purpose of improving the effectiveness of these seminars, which in turn should help to enhance the small business operations in the southern United States. In order to ensure that these training seminars meet the needs of small businesses in our state, we surveyed SBTDC entrepreneurs to gather information on HR topics about which we believe more training is needed.

CONCLUSIONS

This study focused on HR facets in small business in the southern United States by questionnaire. The focus of the study included four parts (1) Legal Compliance – Fair Labor Standards Act; (2) Recruiting, Screening, and Hiring Employees; (3) Employee Relations, Training, and Documentation; and (4) Miscellaneous HR Questions.

In order for a growing small business to be successful it must have highly motivated, competent, and content employees. The employee’s goals must be aligned with the business’s goals in order for the employer to foster employee motivation. In order for employers to foster such a workforce, employers need to have human resource strategies that support these initiatives. Frequently, small business owners have an excellent knowledge of their particular field or core competency. However, our research has indicated that many small business owners-managers lack important knowledge related to labor law compliance and human
resources (HR) management. In addition, those who have an adequate knowledge in the HR field do not have the structure in place to effectively support HR initiatives.

**RECOMMENDATIONS**

The U.S. Department of Labor has an online reference service called eLaws Advisors which is designed to provide an easy-to-use reference tool to help employers and employees better understand federal labor laws. The free service offers help and information on complying with federal rules and regulations, including the Family and Medical Leave Act, the Fair Labor Standards Act, the Occupational Safety and Health Act, Small Business Retirement Savings Programs and Poster Requirements.

Small businesses throughout the United States can contact their local Small Business Development Center to receive free consulting and low cost training on matters related to HR, or many other facets of small business management.

**REFERENCES**


