



THE DEVIL IS IN THE DETAIL

2012 Compliance Hot Buttons and
Priorities for Compensation and
Benefits Professionals

Agenda

- FLSA Traps and Pitfalls

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- Notices & Form 8928

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- HIPAA Privacy & Security Enforcement Update

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- Recent Tax Developments Affecting Compensation & Benefits

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FLSA TRAPS & PITFALLS

1. Work Time / Overtime
2. Exemptions

Fair Labor Standards Act

- The FLSA establishes minimum wage, overtime pay, recordkeeping, and youth employment standards affecting employees in the private sector and in Federal, State, and local governments. Covered nonexempt workers are entitled to a minimum wage of not less than \$7.25 per hour effective July 24, 2009. Overtime pay at a rate not less than one and one-half times the regular rate of pay is required after 40 hours of work in a workweek.

FLSA Does NOT Require

- Vacation, holiday, severance or sick pay;
- Meal or rest periods, holidays off or vacations;
- Premium pay for weekend or holiday work;
- Pay raises or fringe benefits;
- A discharge notice, reason for discharge, or immediate payment of final wages to terminated employees;
- Wage payment or collection procedures for an employee's usual wages or commissions (although some state laws do regulate pay procedures).

Included in Work Time?

- Suffered or Permitted
- Waiting Time
- On-Call Time
- Training Time
- Travel Time
- Sleep Time
- Meal and Rest Periods

Meal and Rest Periods

- Meal periods are not hours worked when the employee is relieved of duties for purposes of eating a meal.
- Rest period of short duration (normally 5 to 20 minutes) are counted as hours worked and must be paid.
- Clocking in and out is **EXTREMELY IMPORTANT!!**

Overtime

For non-exempt employees, must pay 1 ½ times regular rate of pay for all hours worked over 40 in a workweek.

Excluded from “Regular Rate”

- Sums paid as gifts
- Payments for time not worked
- Reimbursement for expenses
- Discretionary bonuses
- Profit sharing plans
- Retirement and Insurance plans
- Overtime premium payments
- Stock options

FLSA Exemptions

- Exempt from both minimum wage and overtime pay
 - ❑ Executive
 - ❑ Administrative
 - ❑ Professional
 - ❑ Outside sales
 - ❑ Employees in certain computer-related occupations
 - ❑ Highly compensated

Exemptions

- **Salary Level**

- For most employees, minimum salary level is \$455 per week.

- **Salary Basis**

- Employee must receive a regular predetermined amount of compensation per pay period.
- Must be paid entire amount for any week when employee performs any work.

- **Job Duties**

Executive Exemption

- **Primary Duty**

- Managing the enterprise, or managing a customarily recognized department or subdivision of the enterprise.

- Customarily and regularly direct the work of two or more other full-time employees.

- Must have authority to hire and fire other employees.

Administrative Exemption

- **Primary Duty**
 - Performance of office or non-manual work directly related to the management or general business operations of the employer or the employer's customers.
- **Must exercise discretion and independent judgment with respect to matters of significance.**

Professional Exemption

■ Learned Professional

- ❑ Primary duty must be performance of work requiring advanced knowledge.
- ❑ Advanced knowledge is in field of science or learning.
- ❑ Advanced knowledge must be customarily acquired by a prolonged course of specialized intellectual instruction.

■ Creative Professional

- ❑ Primary duty must be the performance of work requiring invention, imagination, originality or talent in a recognized field of artistic or creative endeavor.

Other Exemptions

■ Computer Employee

- ❑ Must be employed as a computer systems analyst, computer programmer, software engineer or other similarly skilled worker.

■ Outside Sales

- ❑ Primary duty must be making sales or obtaining orders or contracts.
- ❑ The employee must be customarily and regularly engaged away from the employer's place of business.

■ Highly Compensated

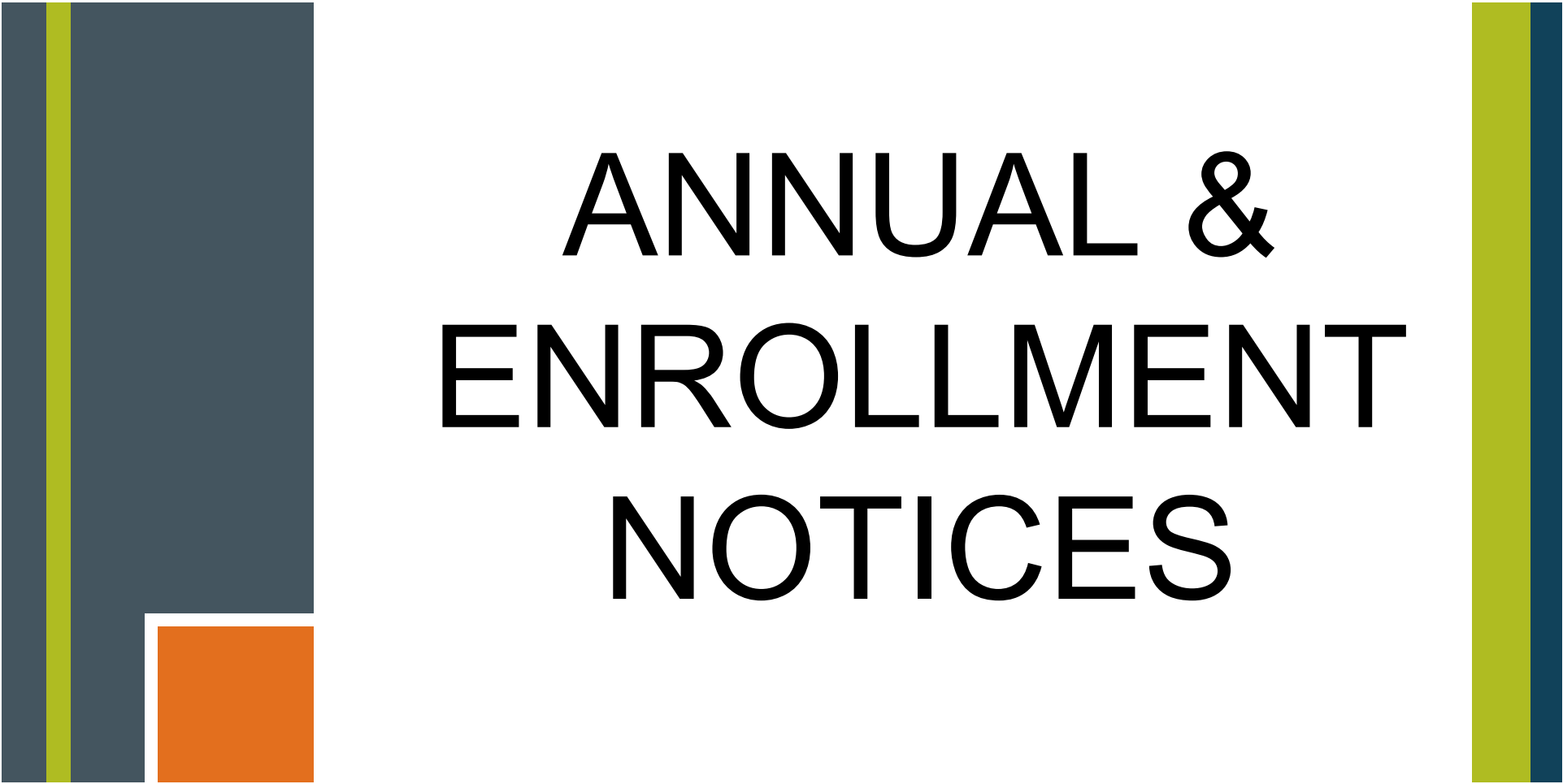
- ❑ An employee making more than \$100,000 per year is exempt if he customarily and regularly performs at least one of the duties of an exempt executive, administrative, or professional employee.

FLSA Recordkeeping Requirements

- Records do not have a required format, but must include accurate information about the employee and data about the hours worked and wages earned.
 - ❑ Employee's full name, as used for Social Security purposes, and on the same record, the employee's identifying symbol or number if such is used in place of name on any time, work, or payroll records
 - ❑ Address, including zip code
 - ❑ Birth date, if younger than 19
 - ❑ Sex and occupation
 - ❑ Time and day of week when employee's workweek begins
 - ❑ Hours worked each day and total hours worked each workweek
 - ❑ Basis on which employee's wages are paid (e.g., "\$9 per hour", "\$440 a week", "piecework")
 - ❑ Regular hourly pay rate
 - ❑ Total daily or weekly straight-time earnings
 - ❑ Total overtime earnings for the workweek
 - ❑ All additions to or deductions from the employee's wages
 - ❑ Total wages paid each pay period
 - ❑ Date of payment and the pay period covered by the payment

FLSA Penalties

- The Department of Labor uses a variety of remedies to enforce compliance with the Act's requirements.
 - ❑ Recommend changes in employment practices to bring the employer into compliance.
 - ❑ Request the payment of any back wages due to employees.
 - ❑ Willful violators may be prosecuted criminally and fined up to \$10,000.
 - ❑ A second conviction may result in imprisonment.
 - ❑ Employers who willfully or repeatedly violate the minimum wage or overtime pay requirements are subject to civil money penalties of up to \$1,100 per violation.
 - ❑ Liquidated damages equal to backpay
 - ❑ Injunctions to restrain persons from violating the Act.



ANNUAL & ENROLLMENT NOTICES

Retirement Plan Notices

- Safe harbor 401(k) notice
- QDIA notice
- Automatic enrollment notice
- Generally due 30 - 90 days prior to start of plan year

Retirement Plan Notices

- Summary Annual Report
- Annual/Quarterly Participant Statements
- Beginning in 2012 – participant fee disclosures for participant directed plans

Group Health Plan Notices

- Both initial and annual notices
- Most can be combined in the SPD, but then SPD must be given each year
- Must now self-report failure and pay penalty to IRS for failure to provide many of the notices

Group Health Plan Enrollment Notices

- Initial COBRA notice
- HIPAA notice of privacy practices
- HIPAA special enrollment notice
- HIPAA preexisting condition notice
- Summary plan description
- Grandfathered plan notice
- WHCRA notice

Grandfathered Plan Notice

- Only applies to plans who are intending grandfathered status
- Must provide notice on all plan materials given to participants/beneficiaries
- Failure to provide notice could cause loss of grandfather protection

Medicare Part D Reporting - participants

- Must disclose to Part D eligible individuals whether prescription coverage is “creditable”
- Applies to all group health plans that provide prescription drug coverage
- No monetary penalty for failure to provide notice

Medicare Part D Reporting - participants

- Notice provided upon 5 events:
 - ❑ Prior to each October 15th (previously 11/15)
 - ❑ Prior to individual's initial enrollment period
 - ❑ Prior to enrollment for Part D eligible individuals
 - ❑ Whenever coverage is no longer creditable or employer no longer offers coverage
 - ❑ Upon request by Part D eligible individual

Medicare Part D Reporting - CMS

- Must also notify CMS if coverage is creditable
- All group health plans are required to comply, unless Part D plan or approved for the retiree drug subsidy
- Also do not have to file with CMS if no Part D eligible individuals are enrolled on first day of plan year

Medicare Part D Reporting - CMS

- Disclosures to CMS submitted electronically through CMS website
- Disclosure required upon:
 - ❑ Annually within 60 days after beginning of plan year
 - ❑ Within 30 days after termination of Rx drug plan
 - ❑ Within 30 days after any change in creditable status of plan

CHIPRA Notice

- Conveys basic information on premium assistance programs through Medicaid or state Children's Health Insurance Programs
- Must explain special enrollment rights under HIPAA
- Model on DOL's website

CHIPRA Notice

- Group health plans must provide CHIPRA notice to any employee who resides in a state that provides Medicaid/CHIPRA subsidies
 - ❑ Ohio – No
 - ❑ Kentucky & Indiana - Yes
- Irrelevant where the employer is located or does business

CHIPRA Notice - Example

- XYZ Co. is located in Columbus, OH
- XYZ sponsors a group health plan in which 25 employees participate. All 25 people reside in Ohio
- Widget has 1 employee who works remotely in Indiana. He doesn't participate in the health plan
- Does XYZ have a notice requirement?

CHIPRA Notice

- First required on first day of plan year beginning on or after 5/1/10, except 5/1/2010 for plan years beginning between 2/4/10 and 5/1/10
- Annually must be given prior to first day of plan year
- Penalty - \$100 per day per individual

WHCRA Notice

- Women's Health and Cancer Rights Act – notice must be given explaining rights to breast reconstruction post-mastectomy
- Annually and at initial enrollment
- Penalty - \$100 per day per individual



FORM 8928

Form 8928 – Self-Reporting

- Requires employers/plan administrators to self-report failures of certain health plan requirements
- Effective beginning 2010 plan year or tax year

Form 8928 – Excise Taxes

- COBRA – § 4980B
- HIPAA Portability, Access, Renewability, and Market Reforms - § 4980D
- Archer MSAs – § 4980E
- HSAs - § 4980G

Form 8928 – Amount of Taxes

- § 4980B & § 4980D – \$100 per day per individual
- § 4980E & § 4980G – 35% of the aggregate amount contributed by employer that year

Form 8928 – Filing Due Date

- For 4980B & D failures – on or before the due date for federal income tax return
- For 4980D & E failures – before the 15th day of the fourth month following the calendar year of error
- Sixth month extension – Form 7004

Form 8928 – Exceptions to Tax

- No tax is due if no one liable for the tax knew or exercising reasonable diligence should have known that the failure occurred
- Form 8928 still must be filed

Form 8928 – Exceptions to Tax

- No tax is due if failure was due to reasonable cause and not willful neglect and
- Failure is corrected within 30 days
- Form 8928 still must be filed

Form 8928 – Exceptions to Tax

- Where reasonable cause but not corrected before notice of examination, tax is minimum of:
 - ❑ \$2,500 per affected individual if de minimis violation
 - ❑ \$15,000 per affected individual if violation more than de minimis

Form 8928 – Exceptions to Tax

- Failures due to reasonable cause are capped at the lesser of:
 - ❑ 10% of aggregate amount spent by group health plan during prior year
 - ❑ \$500,000
- No cap when failure due to willful neglect

Form 8928 – Example

- ABC Co. fails to provide CHIPRA annual notice prior to 1/1/11
- ABC Co. had 20 employees residing in states that provide CHIPRA/Medicaid subsidy
- ABC Co. realizes the error and send a notice on 11/1/11 (304 days)

Form 8928 – Example (continued)

- $\$100 * 20 \text{ Ees} * 304 \text{ days} = \$608,000$
- If error was reasonable cause and corrected within 30 days = \$0
- If error was reasonable cause and not corrected within 30 days = lesser of \$500,000 or 10% of prior year costs

Form 8928 – Action Steps

- Create an action plan for dealing with Form 8928
- Perform an overall compliance review of your benefit operations
- More frequent “audits” of your third-party administrators

Form 8928 – Preemptive Use

- IRS statute of limitations (“SOL”) is generally 3 – 6 years
- No SOL if a return is not filed
- May want to file a blank 8928 each year to start the SOL clock



HIPAA PRIVACY & SECURITY ENFORCEMENT UPDATE

Summary of Recent Developments

- Impact of HITECH Act
- Criminal Enforcement by DOJ
- HHS Civil Enforcement Activities
- HHS Audit Program

Impact of HITECH Act – Background

- HITECH amended the HIPAA privacy and security rules effective February 17, 2010
 - ❑ Expanded requirements for business associates
 - ❑ Added breach notification requirements
 - ❑ Enhanced individual rights
 - ❑ Strengthened enforcement

Impact of HITECH Act – Strengthened Enforcement

- Makes business associates directly accountable to HHS for failure to comply
- Increased civil monetary penalties
 - ❑ Range from \$100 to \$50,000 per violation and from \$50,000 to \$1,500,000 for similar violations in the same year.
 - ❑ Amount depends on degree of culpability (*i.e.*, no knowledge, reasonable cause, or willful neglect)
 - ❑ Penalty collections are allocated to HHS for enforcement purposes
 - ❑ Individuals harmed by violation may also be able to share in penalty collections
- Criminal sanctions can apply to individuals, including employees of covered entity or business associates

Criminal Enforcement by DOJ

- Where HIPAA privacy violations involve criminal activity, HHS refers the case to the DOJ
- HITECH clarified that individuals who are not covered entities may be criminally liable, including employees and business associates
- Criminal prosecutions have involved either:
 - ❑ Sale of PHI for personal gain
 - ❑ Use of PHI for identity theft

HHS Civil Enforcement Activities – Process

- Most HHS investigations begin with a complaint
- Complaint triggers an investigation
- If investigation indicates there have been violations, HHS will try to negotiate a settlement called a Resolution Agreement. Resolution Agreement may include payment of a Resolution Amount
- If settlement cannot be reached, HHS may issue a formal finding of a violation and impose monetary civil penalties

HHS Civil Enforcement Activities – What is a Resolution Agreement?

- A Resolution Agreement is a settlement agreement that incorporates a Corrective Action Plan
- Includes compliance monitoring for a specified time (generally 3 years)
- Does not include a finding or admission of a violation
- Resolution Amount is generally less than potential civil monetary penalties

HHS Civil Enforcement Activities – Recent Resolution Agreements

■ CVS Pharmacy Resolution Agreement

- ❑ Source of complaint: media investigative reports
- ❑ Covered Conduct: PHI, including used prescription bottles, disposed of in dumpsters accessible to the public
- ❑ Corrective Action Plan:
 - ❑ Adopt policies on proper disposal of PHI
 - ❑ Training of pharmacy staff on policies
 - ❑ Internal monitoring of compliance
 - ❑ Engage external assessor to evaluate compliance and report to HHS
- ❑ Resolution Amount: \$2,250,000 payable in a single lump sum

HHS Civil Enforcement Activities – Recent Resolution Agreements

■ Rite Aid Corporation

- ❑ Source of complaint: media investigative reports
- ❑ Covered Conduct: PHI, including used prescription bottles, disposed of in dumpsters accessible to the public
- ❑ Corrective Action Plan:
 - ❑ Adopt policies on proper disposal of PHI
 - ❑ Training of pharmacy staff on policies
 - ❑ Internal monitoring of compliance
- ❑ Resolution Amount: \$1,000,000 payable in three equal annual installments

HHS Civil Enforcement Activities – Recent Resolution Agreements

■ Massachusetts General Hospital

- ❑ Covered Conduct: Employee removed paper medical billing records for 192 patients from the workplace to work on at home. Employee left the medical billing records on the subway and they were never recovered
- ❑ Corrective Action Plan:
 - ❑ Adopt policies on proper removal and transport of PHI to and from the workplace, including physical and technical safeguards to protect PHI
 - ❑ Training of staff on policies
 - ❑ Internal monitoring of compliance
- ❑ Resolution Amount: \$1,000,000 payable in a single lump sum

HHS Civil Enforcement Activities – Recent Resolution Agreements

■ UCLA Medical Center

- ❑ Covered Conduct: Unauthorized employees accessed medical records of “celebrity” patients
- ❑ Corrective Action Plan:
 - ❑ Adopt policies on authorized access to patient records, including physical and technical safeguards to protect PHI
 - ❑ Adopt policies on sanctions for violation of privacy policies
 - ❑ Training of staff on policies
 - ❑ Internal monitoring of compliance
- ❑ Resolution Amount: \$865,500 payable in a single lump sum

HHS Civil Enforcement Activities – Cignet Health Hit with Civil Monetary Penalties

- Source of complaint: 41 Patients whose requests for medical records had been ignored
- Cignet did not cooperate with HHS investigation of complaint and failed to produce records for investigation even after subpoena issued
- Instead of Resolution Agreement, HHS imposed first civil monetary penalties under HIPAA privacy rule
- Penalty of \$4.3 million assessed
 - ❑ \$1,300,000 for failure to provide records to patients
 - ❑ \$3,000,000 for failure to cooperate with HHS investigation

New HHS Audit Program

- HHS to begin conducting HIPAA audits in November 2011
- Who will be subject to audit:
 - ❑ Health care providers
 - ❑ Group health plans
 - ❑ Business associates are not being audited at this time
- Pilot program of 150 audits to be completed by December 2012
- Results will be used to design future audits
- Audit process
 - ❑ Document request (policies, notices, plan provisions, etc.)
 - ❑ On site visit with interviews of key personnel
 - ❑ Could result in Resolution Agreement



RECENT TAX DEVELOPMENTS AFFECTING COMPENSATION & BENEFITS

409A Trap - Release of Claims

- Benefits under employment, change of control, and severance agreements often are contingent on employee signing a general release of claims
- IRC § 409A regulates deferred compensation arrangements
- 409A is extremely broad
- Often applies to above agreements

409A Trap (con't.)

For example, 409A applies:

- ❑ If severance agreement applies to voluntary termination
- ❑ If total of benefits could exceed \$490,000 or payable more than 2 years after termination

If 409A applies:

- ❑ Agreement must contain certain terms, including time and form of payment provisions
- ❑ Otherwise, 20% additional tax, plus interest, apply to employee (and possibly under withholding penalties and interest apply to employer)

409A Trap (con't.)

- 409A limits employee discretion over time of payment
- Agreement covered by 409A may permit payment at any time within 90 days following date of termination, but employee may not have discretion as to timing within the 90-day period

409A Trap (con't.) - Example

- Bob's severance agreement is subject to 409A and contains release provision
- He is involuntarily terminated on November 15, 2011
- He has 45 days to consider signing the release and 7 days to revoke it after signing
- Depending on when Bob signs the release, he could push payment (and taxation) into 2012
- This is prohibited discretion under 409A

409A Trap (con't.) - Solution

- Review all severance, change of control, etc. agreements to identify any 409A issue
- If release issue is present:
 - Amend agreement to provide specific payment date (or otherwise eliminate employee discretion)
 - May have to comply with IRS document correction and operational failure procedures under IRS Notices 2010-6 and 2010-80

162(m) Trap - Stock Options

- Existing final regulations under IRC § 162(m) provide detail on “performance-based” compensation exception to nondeductibility under 162(m) of compensation over \$1 million
- Stock options are deemed performance-based if:
 - (1) Grant is made by the compensation committee
 - (2) Amount of compensation the employee could receive is based solely on value of the stock after the date of grant; and
 - (3) Plan under which options are granted states a maximum number of shares that may be granted to any covered employee

162(m) Trap (con't.)

- Recent proposed IRS regulations clarify that the option plan must specify the maximum number of shares that may be granted per employee in a given period, and not just the aggregate number of shares that may be granted under the plan
- Many public companies believed maximum limit requirement could be satisfied by the plan stating the aggregate number of shares that may be granted in a given period
- Review the plan and amend if necessary

Worker Classification - Good News!

Background

- IRC § 3509 softens otherwise harsh treatment resulting from reclassifying independent contractors as employees (i.e., substantially reduces income tax, FICA, FUTA owed)
- Employer must meet several requirements to take advantage of § 3509 relief

Worker Classification (con't.)

More Background

- IRS established the Classification Settlement Program (CSP) several years ago to allow businesses and IRS to resolve reclassification cases
- CSP is only available for employers under IRS examination
- If CPS requirements met, assessment is computed at 25% of § 3509 rates

Worker Classification (con't.)

New Voluntary CSP

- New program to encourage voluntary correction of misclassification
- To be eligible for VCSP, the business:
 - ❑ Must have filed all Forms 1099 for affected workers in previous 3 years
 - ❑ Cannot currently be under examination by IRS, DOL or any state government agency

Worker Classification (con't.)

Benefits of VCSP

- Only pay 10% of employment tax liability that may have been due on compensation paid to workers in most recent tax year
- But based on reduced rates under § 3509
- No interest and penalties
- Will not be subject to employment tax examination for worker classification for prior years

Worker Classification (con't.)

Accessing VCSP

- Submit application using Form 8952 at least 60 days before business wants to treat workers as employees
- All workers in same class of workers must be treated as employees
- If application accepted, must enter into a closing agreement with IRS → must treat the class as employees for future years, and must extend statute of limitations on assessment of employment taxes for 3 additional years for each of the 3 calendar years beginning after the date reclassification begins

Deductibility of Bonuses—IRS Does an About-Face

General Rule – The “All Events Test”

- Bonuses payable to a group of employees are deductible by an accrual basis taxpayer in the year in which:
 - ❑ All events have occurred that establish the liability
 - ❑ The amount can be determined with reasonable accuracy, and
 - ❑ Economic performance has occurred
- Through a series of revenue rulings and cases, IRS position has been that the all events test requires each individual’s bonus amount to be fixed by end of accrual year

Deductibility of Bonuses (con't.)

Rev. Rul. 2011-29

- Accrual basis employer may deduct fixed amount of group bonuses payable if:
 - ❑ Employer is obligated to pay the fixed amount which is determined by the end of the year;
 - ❑ Bonuses are paid to the individuals within the first 2½ months of the following year;
 - ❑ Identity of recipients need not be known, nor specific amount per person, by the end of the tax year
 - ❑ Any forfeited bonus must be re-allocated to other bonus recipients

- Change in treatment of bonuses to conform to Rev. Rul. 2011-29 is a change in accounting method

W-2 Reporting Under Health Care Reform (HCR)

- Under the new Health Care Reform law, employers that issue 250 or more Forms W-2 must report the aggregate cost of employer-sponsored coverage on Forms W-2
- Effective for W-2s issued in January 2013
- Employers must begin to program payroll systems and/or work with providers to accurately gather and report the value

Other 2012 HCR Requirements

- Summary of Benefits and Coverage (SBC)
 - ❑ SBC must be given to enrollees prior to enrollment or re-enrollment
 - ❑ Was to be effective on or before March 23, 2012, but recently postponed until final regulations issued
 - ❑ Applies regardless of grandfathered plan status
 - ❑ No more than 4 pages
- Nondiscrimination testing of fully insured plans → effective date also delayed pending further guidance



Questions?

Thank you!