BEST PRACTICES IN
Compensation & Benefits

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Bad Economy Affects Execs, Too: What You Can Do About It

Companies are facing a problem: how to divide up a dwindling amount of money among their valued employees. Deserving workers may receive lower—or even no—raises. Rank-and-file employees are not alone in facing the problem; executives are also feeling the pinch of a poor economy.

We've explored some problems, solutions, and trends that have come to light in recent months that impact executive pay, specifically their company stocks. Information services firm Equilar (www.equilar.com) surveyed 125 of the Fortune 250 during the summer of 2008, and learned how these large companies are handling steep drops in stock prices with regard to their executives. Each company answered questions about how they pay their top 25 positions. Here are some of the findings.

Guidelines Require Holding Percent of Pay

Companies often require executives to own company stock, as a way to align their personal goals with the company's goals. David Sasaki, a senior researcher at Equilar, says that a steep drop in stock price may mean executives are no longer in compliance with their pay guidelines.

"Our results show that about 80% of ownership guidelines are defined using a multiple of base salary approach. This trend also holds for directors, where around 57.5% define their target as a multiple of base salary.

"We really want to point out that any kind of multiple of base salary or other dollar-defined ownership guideline really fluctuates as stock prices change. As stock prices have dropped over the last year, executives and directors have needed to either purchase more shares to stay in compliance with the guidelines, or make changes to the guidelines."

One solution is to require that executives hold a fixed number of shares instead of a dollar value. "One thing that could potentially address this issue before it even comes up is if companies set their ownership guidelines at a fixed number of shares, rather than a dollar value target," Sasaki says.

"Obviously, this avoids the volatility involved with setting a dollar value, while still maintaining some level of ownership for executives. About 12.8% of the surveyed companies set their executive ownership guidelines using a fixed number of shares."

Who is taking this approach? "Lear Corporation, who in 2007 recognized the difficulties with having a dollar-defined guideline and modified it into a share-defined guideline to mitigate the effect of stock price volatility," explains Sasaki.

"Before, the CEO was supposed to hold five times his base salary, which in fiscal 2007 values would have been about 225,000 shares. They changed it so [the CEO] has to hold about 125,000 shares now. If you look at the current stock price of Lear, the old policy would have required [the CEO] to hold 4 million shares."

Another solution to this problem is to suspend ownership requirements. "We've seen in the Fortune 250 about 8% of companies including what we call hardship provisions, which are cases

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where the board has the ability and can decide whether or not to suspend the guidelines, or allow exceptions to the guidelines under certain conditions," Sasaki observes.

Who is taking this approach? "R.H. Donnelley® took the approach of completely suspending their ownership guidelines for a temporary period of time," explains Sasaki. "In its proxy it disclosed a chart showing how, as the stock price declines, the number of shares the executives need to hold to comply with the guidelines is increased to a point where the executives aren't able to comply; it just isn't a reasonable option."

Margin Calls Taking Effect

Investors can buy stock using some of their own money and some borrowed from a broker. When that happens, the broker sets a minimum percentage the purchaser must invest, known as a minimum margin requirement.

When the stock price drops, the amount the purchaser has invested may drop below the minimum margin requirement, at which point the broker will ask for him or her to invest more money or sell the stock and repay the loan. This is a margin call. With the sharp decline in stock values in the latter part of 2008, margin calls began pouring in to corporate executives, who are often rewarded with the ability to buy company stock on margin.

"In the middle of October, we did an analysis for the *New York Times* where we found out that just during the first half of October, there was about $1 billion in company stock sales by insiders that were related to or caused by margin calls," says Sasaki. When the Market sees executives dumping a huge volume of shares, it causes concern among investors, further reducing the stock's price.

A solution to this problem is to prohibit margin buying. Creating a policy that specifically disallows margin buying may protect the company against a rapid drop in share value that could result from executives selling large amounts of stock.

Who is taking this approach? "We didn't find that many examples of companies including this kind of prohibition in their trading policies or ownership guidelines," said Sasaki. They did find a few. "Newfield Exploration adopted a new policy on November 7, 2008, that explicitly prohibits holding any shares in margin accounts. Reliant Energy also prohibits [margin buying]. And Dominion Resources, while they don't fully prohibit the practice, require that any shares held in margin accounts not be counted toward their ownership guidelines."

Make Execs Hold Shares Until Retirement

"This is like a holding requirement, in that it requires executives to hold a certain percentage of the shares awarded to them. But rather than holding them for 1 year or 2 years or until they reach the targeted percentage, it requires executives to hold them all the way through their tenure with the company," says Sasaki. "At the moment, this isn't a common practice, but we see it as something that is going to increase in prevalence and get a lot of attention in the upcoming proxy season.

"From the shareholder's perspective, this really drives long-term alignment of interests, because the executives know that they're going to have to hold those shares throughout their time with the company. We have seen some shareholder activist groups indicate that one of the big pushes they're going to have for the upcoming proxy season is to get proposals on the ballot for implementing 'hold until retirement' provisions."

Who is taking this approach? Executives with the Bank of New York Mellon Corp. must retain 50% of the net after-tax shares they receive during their tenure, according to their policy adopted in March 2008. Citigroup (Citi) management agreed to hold 75% of the Citi stock they acquire during their time as senior management with the company.

"We've seen a couple of companies go a little further than the standard hold until retirement provisions," Sasaki says. "Medco Health Solutions' guidelines require executives to hold, not just until retirement, but 6 months after that point."

What to Do Now

If you haven't already, now would be a good time to examine your company's executive pay/company stock guidelines to determine if any of the situations outlined here may affect you. Bear in mind, too, that performance measures created under better economic conditions may no longer be practical, or even possible, for executives or for other employees paid using performance incentives.

Examine the measures and the targeted bonus amounts to make sure they remain viable. One way companies are tackling this situation, says Sasaki, is to lower potential bonuses and replace them with a bonus plan that vests over a longer period:

"This is an example of a company switching from cash-based incentives to longer-term incentives that vest over time. We really think this could be an opportunity, and we think companies are seeing it as an opportunity, to adjust their compensation towards more long-term timelines," Sasaki maintains.

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Long-Standing Profit-Sharing Bonus Continues Despite Economy

When the Lincoln Electric Company first distributed profit-sharing bonuses to its employees in the 1930s, the average bonus was $350, says Roy Morrow, the company's director of corporate relations. In December 2008, Lincoln Electric reached a significant milestone when it distributed profit-sharing bonuses for the 75th consecutive year—this time for an average individual bonus of about $28,873.

Record High Bonuses Paid

Lincoln Electric (www.lincolnelectric.com), the North American subsidiary of Lincoln Electric Holdings, Inc., is a global leader in the brazing and soldering alloys market and the design, development, and manufacture of arc welding products, robotic arc-welding systems, and plasma and oxyfuel cutting equipment.

Eligible employees at Lincoln Electric's major operations in northeast Ohio received a total of $89 million in profit-sharing bonuses late last year, according to Morrow. "The profit-sharing bonus is a Lincoln U.S. program, specifically Lincoln Cleveland, its major domestic subsidiary and largest single manufacturing operation. Although other Lincoln subsidiaries outside the United States have profit-sharing programs, none operates exactly like the U.S.- or Cleveland-based program," he says.

In general, the bonus is paid to full-time employees hired before October 31 of the bonus year, he says. The specific amount paid to each eligible individual varies. "The bonus is a merit-based system, so the amount of an individual's bonus is based on his or her merit or performance rating and base wages."

Despite the economy, the bonus pool and the average individual bonus set records in 2008, and the Cleveland company's guaranteed employment policy remained in place, Morrow says. Officially in effect since the early 1950s, the guaranteed employment policy "guarantees a minimum number of hours for Lincoln employees with 3-plus years of continuous service who meet our performance standards," he explains. "It does not guarantee a specific job, so, as a result, employees must be willing to move into a job based on company needs. The job assigned may or may not be at the same base wage and may or may not include the same or different responsibilities. The policy enables the company to have a flexible compensation system by lowering wages and work hours down to 30 hours per week. On the upside, the policy also includes mandatory overtime."

Morrow credits this program with "preserving job security for our workforce and most importantly, maintaining the investment in a skilled and productive workforce."

"Guaranteed employment can be eliminated by the board of directors with 6 months' notice, but has been in effect since the early '50s," he says.

During the company's annual bonus ceremony in December, Chairman and CEO John M. Stropki pledged to work diligently to keep the company strong. "No one is certain as to how long the current recession will last or how severe it will be," he said. "In anticipation of a long, deep recession, we will continue to look for ways to reduce our overall costs and do it in a way that protects our long-term financial viability and preserves our long-standing and very successful guaranteed employment policy."

The profit-sharing bonus and guaranteed employment policy have helped Lincoln Electric achieve low turnover, high morale, increased productivity, and lower training costs, Morrow says. "Turnover rates for employees with more than 3 years of continuous service are way below industry averages."

Who: Lincoln Electric Company

What: Has offered a profit-sharing bonus to employees in the Cleveland area for 75 consecutive years. Also guarantees a minimum number of hours of employment for eligible workers.

Results: Low turnover, high morale, increased productivity, and lower training costs.

Tips to Consider

The success of an individual business will determine whether it can continue offering, or introduce, a profit-sharing bonus or implement a guaranteed employment policy. For companies where those are viable options, Morrow offers some advice to consider:

Put the bonus in perspective. A profit-sharing bonus is an effective incentive to boost worker productivity and profitability, "but is it not the only way and must be implemented in an intelligent and equitable way," Morrow says.

Customize your bonus program. "The secret to success is implementing a program that fits your workplace culture," he says.

Remember that people are key. "Guaranteed employment is not a simple program to implement. The journey can determine the end result," Morrow explains. "A policy is nothing without the people and their belief in it, and in our case, a supportive management and board of directors. People make it work through their engagement, productivity, and dedication to the success of the company or enterprise.

"The key to success for guaranteed employment is a recognition that it takes a very big commitment from a company but just as big a commitment from each employee (to be flexible about work arrangements and to perform at high levels in order to sustain the program)."

Employment Tax Policies Among Gravest Problems

In her annual report to Congress, National Taxpayer Advocate Nina E. Olson identified employment taxes as the fourth most serious problem encountered by taxpayers.

"The National Taxpayer Advocate is concerned that IRS employment tax policies may overreach and undermine some of the important protections enacted in the Taxpayer Bill of Rights and the IRS Restructuring and Reform Act of 1998," the report states. Although approximately 88 percent of all employment tax returns are filed and fully paid, the report estimates that $58 billion in employment taxes are not paid.

Olson recommends "applying different treatments to taxpayers based on their levels of and reasons for noncompliance, encouraging prospective voluntary compliance by helping taxpayers who are attempting to follow complex rules and procedures, concentrating sufficient resources on early intervention techniques to prevent the accumulation of substantial employment tax liabilities, and building a local compliance presence that balances enforcement with outreach and education."

Another serious problem is inefficiencies in the administration of the Combined Annual Wage Reporting (CAWR) program that burden employers and waste IRS resources, according to the report.

"From fiscal year 2003 to fiscal year 2006, IRS eventually abated 81 percent of the penalty dollars it previously assessed" against employers for discrepancies in wage and tax data. Olson "recommends that IRS provide specific information about the wage reporting discrepancy on notices, include the phone number for a live assistant in the CAWR unit on notices, and continuously train its employees about when it is appropriate to assess CAWR penalties."

OFCCP Enforcement Breaks Records

More than 24,500 U.S. workers who had been subjected to unlawful employment discrimination received in excess of $67.5 million in back pay, salary, and benefits during fiscal year 2008, according to the U.S. Department of Labor's (DOL) Office of Federal Contract Compliance Programs (OFCCP). The latter figure is up 133 percent over financial remedies won by OFCCP in fiscal year 2001.

In the past 8 years, there has been a 14 percent increase in the total number of compliance reviews completed, a 92 percent jump in the number of job applicants and employees who financially benefited from OFCCP investigations, and more than $50 million in additional back pay, salary, and benefits compared to the previous 8-year period, OFCCP reports.

Final Reg Issued On Civil Penalties Under the PPA

Plan administrators who fail to disclose certain documents to participants, beneficiaries, and others may face up to $1,000 per day per violation in civil penalties, according to a final regulation recently released by DOL.

The regulation, which was published in the *Federal Register* on January 2, 2009 (Vol. 74, No. 1), implements the department's authority to assess civil penalties for those who violate certain disclosure requirements outlined in the Employee Retirement Income Security Act as amended by the Pension Protection Act of 2006 (PPA).

Under the PPA, new disclosure provisions were established relating to:

- Funding-based limits on benefit accruals and certain forms of benefit distributions,
- Plan actuarial and financial reports,
- Withdrawal liability of contributing employers, *and*
- Participants' rights and obligations under automatic contribution arrangements.

The final regulation outlines administrative procedures for assessing and contesting related civil penalties.

For example, after receiving a written notice of the DOL's intent to assess a penalty, a plan administrator has 30 days to explain in writing why the proposed penalty should be reduced or not assessed at all.

IRS Update

Relief for 403(b) Written Plan Requirements

The Internal Revenue Service (IRS) recently announced that it has extended until December 31, 2009, the deadline for 403(b) plan sponsors to adopt a written plan. The previous deadline was January 1, 2009.

In Notice 2009-3, IRS explained that a 403(b) plan will not fail to satisfy the relevant requirements during calendar year 2009, as long as the plan sponsor:

- Adopts a written 403(b) plan on or before December 31, 2009, that is intended to satisfy the pertinent requirements as of January 1, 2009,
- Operates the plan during 2009 in accordance with a reasonable interpretation of section 403(b) and the final regulations, *and*
- "Makes its best efforts" before the end of 2009 to retroactively correct any operational failure during 2009 to conform to the terms of the written plan.

Among other things, IRS plans to publish a draft revenue procedure on obtaining approval of prototype 403(b) plans and on sample plan language for drafting prototype plans. For more details on the extension, see our coverage on page 10 of this issue.

Experts' Forum

Why You Should Maintain Your Investment In Benefits Communication During a Down Time

By Jennifer Benz, Benz Communications

Benefits are a major company expense accounting for 20 percent of all compensation spending. And, in stressful times, you may feel pressure to cut back on benefits communication, even as you cut back on the benefits themselves.

This is the wrong approach for your employees and for your company. Employees who value their benefits are more loyal and more productive—and more likely to stay with your company through good times and bad. Companies that prove they care for their employees during tough economic times are the ones that will come out on top when times are good.

The *right* benefits communication can be a strategic lever, helping your company do more with less. With strategic benefits communication, you can manage benefit changes while also increasing employee retention and engagement. In times like these, successful companies don't stop investing in benefits communication. Rather, they make their investment more effective.

Reasons to Invest

An investment in benefits communication is one of the best ways to show employees how much the company values them—in good times and in bad. And, it can improve the return on your investment in benefits programs, making sure the programs you're paying for are being used and being used well. During uncertain economic times the two most important reasons to invest in benefits communication are to improve retention of key talent and to inspire trust.

Boost Retention. Many employers underestimate just how important benefits are in creating and maintaining employee loyalty. According to Prudential, 85 percent of workers rate a company's benefits package as "highly important to their decision to change employers or remain with their current company."

But, loyal employees aren't necessarily those with the most expensive benefits. Rather, they're employees who understand how to get the most value out of their benefits because they've received clear, open communication throughout the year.

Effective communications help employees choose their benefits and use them well. These communications help employees appreciate how much is invested in their long-term growth and security. When employees understand their whole package, they are better equipped to weather year-over-year changes.

Inspire Trust, Which Increases Shareholder Returns. Benefits are more than a company policy. They're a big component of employees' personal lives. Benefits affect just about everything that matters, from how employees care for their health and their families, to how they save for retirement, to how they protect themselves from major illnesses and accidents.

Building trust means going beyond what something means to your company. It means acknowledging what it means to *your employees*.

Great communication builds that kind of trust. And trust drives employee engagement, commitment, and profits. According to Watson Wyatt, "Where employees trust leaders, shareholder returns are 42 percent higher than where distrust abounds."

How to Make the Most From Your Investment

The most effective way to improve employees' perceptions of their benefits is to get them to use them more. This shows them the value of the programs and proves the investment their company is making in their lives. Use these steps to immediately improve the effectiveness of your benefits communication.

1. **Create a communication strategy** that ties your business objectives to the needs of your employees—and includes measuring results. Changing employees' behaviors and improving their benefits use takes time. But having a strategy in place ensures all efforts work toward the same goals.
2. **Communicate to families, too.** Families make up 60 percent to 70 percent of your healthcare costs and are often the ones making the benefits decisions. Get your benefits information into the hands of the people—spouses and families—who will use it. And make sure it's tailored to them.
3. **Make it easy for employees to take action** with tip sheets, simple checklists, and information tailored to age and family situation. Don't assume that your employees will go through the effort to figure out how programs work—make sure it is easy for them to get what they need.
4. **Integrate your vendors**, plans, processes, and channels so your employees can navigate it all and communicate to them year-round, not just during open enrollment.
5. **Give managers a preview and give employees a way to talk back**. Empowering your managers by asking them to play a role in benefits communication connects them to the company, and helps keep employees engaged, too. Make sure employees have a way to respond to all information (whether from their manager or the Intranet) with feedback and questions.

Jennifer Benz is an award-winning communication consultant and writer based in San Francisco. Her firm, Benz Communications, provides full-service employee communication services to 100 Best Companies to Work For and Fortune 500 leaders. She can be reached at jen@benzcommunications.com.

From the Courthouse

HMO Has No Duty to Inform Provider About COBRA Election Rights

An HMO was not liable to pay for medical services provided to a terminated employee during her COBRA election period because she was given her Consolidated Omnibus Budget Reconciliation Act (COBRA) election notice, but did not elect or pay for coverage. Even though the provider inquired about the employee's coverage, the court ruled that the HMO had no duty to give the provider information about the employee's COBRA election rights (*Tenet Healthcare LTD. v. UniCare Health Plans of Texas, Inc.,* U.S. District Court for the South District of Texas, Civil Action No. H-0703534 (11/26/08)).

Facts. As an employee of Sheltering Arms Senior Services, "Sharon" was covered by Unicare Health Plans of Texas, Inc., a health maintenance organization (HMO). UniCare had entered into an agreement with Tenet Healthcare LTD. d/b/a/ Park Plaza Hospital under which UniCare would pay negotiated rates for Tenet to provide covered hospital services to UniCare members.

On June 14, 2005, Sharon was admitted and hospitalized by Tenet for medical treatment, and a representative of Tenet contacted UniCare to verify that Sharon was covered by the HMO. UniCare's records showed that Sharon was an enrolled employee as of June 14, 2005. UniCare did verify Sharon's coverage and provided preauthorization to Tenet to treat her. UniCare admitted that it verified Sharon's inpatient benefits but also stated that all charges were subject to medical necessity, member eligibility, and all plan provisions in effect at the time services were rendered. Sharon assigned her rights to medical benefits available under the terms of the HMO agreement, if any, to Tenet.

Tenet provided approximately $241,000 worth of medical services to Sharon based on UniCare's representation that Sharon was covered. However, on August 5, 2005, Sheltering Arms informed UniCare that Sharon had been terminated from employment on May 11, 2005, and that her coverage under the HMO terminated on June 1, 2005. After terminating her, Sheltering Arms sent Sharon notification of her right to elect COBRA which Sharon received on June 1, 2005. Sharon did not elect coverage during the 60-day election period.

Tenet eventually filed suit against UniCare and Sheltering Arms alleging they had failed to inform Tenet that Sharon "was or may have been in an election period," during which she could have elected continuing coverage under COBRA. If Tenet had been properly notified of the potential for a COBRA election, it said, it could have made payment on behalf of Sharon of the COBRA premiums or arranged another method of payment for the premiums.

Ruling. The court's ruling on the COBRA issues was very simple—that Tenet had failed to show it had any rights under COBRA vis-à-vis Sharon. Tenet was not a plan participant. In addition, Tenet failed to direct the court to any authority establishing that UniCare or Sheltering Arms had an obligation to notify Tenet that Sharon was in a COBRA election period.

Election period duties. It is clear that an indemnity or reimbursement plan has a duty when asked by a provider about the coverage of a qualified beneficiary during a COBRA election period to give a complete response about the qualified beneficiary's COBRA rights during the election period.

The subparagraph of the Internal Revenue Service regulations that deals with election periods for HMOs does not include this requirement. While there are valid reasons why the regulations provide different procedures for administering the election period for indemnity and reimbursement plans versus HMOs, there is no reason why COBRA qualified beneficiaries covered by an HMO should not have the same protections as those covered by an indemnity or reimbursement plan to give providers information about COBRA rights.

The LAW

A qualified beneficiary who makes a timely election of COBRA continuation coverage must be provided with coverage during the COBRA election period (IRS Reg. Sec. 54.4980B-6, Q&A-3). The coverage during the election period can be provided in several ways depending on the type of benefit plan involved.

In the case of an indemnity or reimbursement arrangement, the employer can provide for plan coverage during the election period, or, if the plan allows retroactive reinstatement, the employer can terminate the coverage of the qualified beneficiary and reinstate her or him when the election is made. Claims incurred during the election period do not have to be paid before the election is made.

If a healthcare provider contacts an indemnity or reimbursement plan to confirm coverage of a qualified beneficiary during the election period, the plan must give a complete response about the qualified beneficiary's COBRA rights. For example, if the plan provides coverage during the election period, but cancels coverage retroactively if COBRA continuation coverage is not elected, the plan must inform a provider that a qualified beneficiary for whom coverage has not been elected is covered but that the coverage is subject to retroactive termination. Similarly, if the plan cancels coverage but then retroactively reinstates it once COBRA continuation coverage is elected, the plan must inform the provider that the qualified beneficiary currently does not have coverage but will have coverage retroactive to the date coverage was lost if COBRA continuation coverage is eventually elected.

If group healthcare coverage is provided through direct provision

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Benefits Corner

'Lost' Participants Create Liability for Retirement Plans

Employees move on. They pack up their desks, eat a little cake, and say goodbye. Sometimes friends in the workplace stay in touch, but often, former co-workers fade into memory. It seems to be the natural order of things.

But when it comes to the retirement plan, fading away is a problem. The first and best choice for plan administrators is to send participants on their way with a distribution check, say Keane Retirement Services' Mary G. Steigerwalt and Dave McCrystal.

While you can automatically cash out some participants, such as those with small account balances, those with higher balances may choose to continue participating in the plan. When they do, you run the risk of losing track of them.

"If participants are no longer active employees, and they stay in the plan, they are a cost to the plan," says McCrystal, Keane's director of marketing. "You are obligated to maintain communication with them, but you run the risk of becoming disconnected, and then having a fiduciary obligation that you have difficulty meeting."

And the problem is worse when a former employee dies. "Death is a distributable event in a defined contribution plan," says Keane President Steigerwalt. "If you think about what's happened in the stock market in the last couple of months, you'll see the problem. If somebody died last year, and their beneficiary should have received their distribution but the plan sponsor did not know they had died, there could be a substantial change in the value of that asset." Keane (www.keaneqps.com) suggests that plan sponsors work to prevent that situation before it arises.

How? By thinking like a risk manager. "As data ages, it will develop errors of one type or another," McCrystal says. "We as a company believe in the philosophy of measuring, managing and monitoring to identify risks. We recommend a similar strategy for plan sponsors. It's very simplistic on its face. But putting into place a procedure—a systematic way of assessing the data quality, looking at the errors or outdated information and then correcting it—is a best practice for a plan administrator who wants to keep costs contained, keep themselves in compliance and keep fulfilling the obligation they have to the participants to keep them abreast of all the pertinent plan information."

Bad data is an ongoing issue for most plans, says McCrystal. "Everybody has it. It's not something that makes you unique, something you should be afraid of, or even something you could do much about if you're just operating normally. You just have a situation, and you have to deal with it. The question is whether you will deal with it poorly, or effectively."

Potential Lawsuits

When a retirement plan loses track of participants because they moved or died, fiduciaries may find themselves in the awkward position of having to explain why former participants' account balances declined between the time they or their beneficiaries were due a distribution and the time they actually received it.

Keane Retirement Services President Mary G. Steigerwalt says a recent court case, *LaRue v. DeWolff, Boberg & Associates*, could open the way for legal trouble in such instances. Former employee LaRue instructed the plan to make changes in his retirement plan investments. Those instructions were not followed. When the value of his account declined as a result of the plan's inaction, LaRue filed suit.

Under the federal Employee Retirement Income Security Act, participants have generally only been allowed to sue as part of a class, rather than individually, but the U.S. Supreme Court allowed LaRue's action.

The decision impacts plan sponsors by clearing the way for individual participants in other plans to sue when they believe fiduciaries acted improperly. Steigerwalt says, "This decision opened the door for individuals to go back to their plan sponsors or their employers when certain steps have not been taken, and there was a negative impact on the participant's opportunity to earn money in the retirement plan."

ABOUT THIS NEWSLETTER

This newsletter is devoted to sharing compensation and benefits ideas that have worked for HR professionals striving to make a strategic difference in their companies. If you have a story you'd like to share, send us a fax at 860-510-7224.

If you have a question about one of the newsletter stories or want more information, call 800-727-5257, ext. 2194, or e-mail equayle@blr.com.

CASE Study

'Green' Colors Sustainable Practices at The Standard

Who:	The Standard
What:	Allowed employees to create a green team, a group of employee volunteers who steer the company in a sustainable direction
Result:	Implementation of an alternative transportation program, including Zipcars, means employees who value sustainability are more likely to come to work for the company, and stay employed longer

When Standard Insurance Company added Zipcars as a benefit for employees, no one was terribly surprised. The Standard is headquartered in Portland, Oregon, where green is considered a primary color.

And while Zipcars are a fun and convenient way for people to reduce their impact on the environment, it turns out that they are only one way The Standard is thinking green in an effort to benefit their communities and their employees.

Carrie Farrar, The Standard's sustainability coordinator, reports that the company also offers a comprehensive alternative transportation program. And while Farrar is responsible for overseeing the 3,400-employee company's sustainability programs, she doesn't do it alone; she has the help of the company's volunteer "green team."

"We have a base of passionate employees who care about sustainability and want to see green initiatives move forward within the organization," says Farrar. "I feel like that's essential to businesses just starting out thinking about sustainability, because there is a group of employees who will be the champions of new programs. They will be the word of mouth, and things really grow when you have an excited group of employees working on these sorts of things."

Green Is the Word

Of course, we all understand that taking care of our environment is a positive thing to do, but Farrar believes there are really two reasons to do so. First and foremost, reducing the impact of businesses (and individuals) on the environment can only contribute to the health of the planet and the people on it. Also important, though, is creating a competitive edge in hiring new employees. Companies like The Standard tend to attract employees who share their vision.

"I think (sustainability) is more and more becoming something that employees are looking for," Farrar says. For example, subsidized transportation benefit programs, like the one The Standard offers, allow employees to ride transit to work rather than bringing their own automobiles.

"That way, they ease the burden of the costs for themselves, and they reduce their own personal carbon footprint," she explains. "The younger generations are becoming more and more concerned about these issues, and they want to do everything they can. Just as important, they want to make sure their employer is making the right choices and is supportive of that kind of structure. It has to do with employee recruitment and retention."

Not only does The Standard's emphasis on green initiatives make it easier to hire and retain like-minded employees, Farrar believes that employees who are enthusiastic about their company's values produce more and better results.

"When employees are engaged in the company they work for," she says, "it increases the amount of effort that they are putting into their work. Of course we as a company want to do the right thing in our communities, especially in Portland where we have our corporate headquarters. But employee engagement really helps reduce turnover. The environment, sustainability, and "going green" are things that Portlanders really care about. This is an opportunity to differentiate ourselves from other companies in the area, to attract top talent."

Green is also a favorite color at The Standard wherever they have employees, Farrar says. "This (kind of movement) is something that's happening everywhere. Portland certainly has a lead on it. But the benefits that we're offering to Portland employees, those are available for the most part to employees across the nation. Of course, that depends on the infrastructure that's available in their city, and we can't really influence that. But where alternatives are available, we encourage them."

Commuting Subsidies, Zipcars Are Benefits

The Standard's transportation benefits program includes a subsidized transit pass. "It could be the Max (Portland's light rail system) or it could be a public transit system in another city or another state. It's a national system that we honor," Farrar explains. "We also subsidize carpooling nationwide. We have it structured in such a way that we are promoting more than just two people per car. Each of the individuals riding in the carpool receives a subsidy, and the subsidy is higher if there are three or more people in the car."

Mass transit is great, but what happens when an employee needs to travel during the day for business or personal reasons? In the past, employees would have to bring their car to work on days they need to travel away from the city center. Not anymore. The most recent addition to The Standard's package of transportation benefits is the "Zipcar®."

Zipcar (www.zipcar.com) is the world's largest car-sharing service, offering memberships in many large cities across the country, including many of those in which The Standard operates. "Zipcars are a great, low-cost employee transportation option, and The Standard is proud to contribute to city efforts to help ease congestion and pollution in the area," said Mike Winslow of The Standard at the launch of the partnership. "With more than 3,400 employees working in 27 states across the country, the Zipcar partnership presents an opportunity to make a real difference in the communities where our employees work and live."

Portland's mayor, Sam Adams, is also enthusiastic about the Standard/Zipcar partnership. "The Standard is creating a complete transportation package for its employees," he said. "Providing real alternatives and making it easier for people to exercise Earth-friendly options is the kind of thinking that will lead to solutions for our transportation system."

With purchase of an annual membership, which is paid by The Standard, Zipcar users are free to use a car to travel to and from business meetings, medical appointments, or other places during the workday.

Travel for business purposes is paid by The Standard, and employees can take advantage of reduced rates for personal trips in the Zipcars. Do employees like them? "We had over 150 sign up on our account, just in the first month and a half," says Farrar.

Start Small, Stay Green

As you would when beginning any new program, Farrar recommends starting small if you want to go green. "Start with small steps and reach out to employees to encourage participation," she says. "Enable employees to begin, like we did, a volunteer green team. Then you can see where the energy exists within the organization. In different companies people may be passionate about different things. Maybe an organization already has certain things set up, but the green team could identify where there is room for improvement, and work with the right folks within the organization to help move them forward.

"This is a way for employees to remain engaged. And it's a differentiator in employers. If one employer is offering a subsidized bus pass, and they have different volunteer opportunities at work, that employer may rise to the top of someone's search list if they're looking for a new job, and it may retain them longer while they're on board."

Farrar suggests checking in with your city's transportation office for guidance on how to begin thinking green: "There are tons of resources that cities have on transportation options. The conversation can begin there, and the company can get connected with the local transit authority. The city's office of transportation has access to all of those resources."

The Law *(continued from page 6)*

of health services, such as a health maintenance organization or a walk-in clinic, then the plan can require a qualified beneficiary who has not yet elected and paid for COBRA continuation coverage to choose between:

- Electing and paying for the coverage; *or*
- Paying the reasonable and customary charge for the plan's services if he or she will be reimbursed for that payment within 30 days after the election of COBRA continuation coverage (and the payment of any balance due for the coverage).

The plan also has the option of treating the qualified beneficiary's use of the facility as a constructive election. In that case, the qualified beneficiary is obligated to pay any applicable charge for the coverage, but only if the individual has been informed beforehand that use of the facility will be a constructive election. This information should be provided in the initial COBRA notice when coverage under the plan begins and again in the COBRA notice informing the individual of the qualifying event to ensure that the qualified beneficiary is informed of the meaning of constructive election before using the health facility.

The regulations do not require that a direct provision plan such as an HMO provide information about coverage during the election period to healthcare providers.

Q&A

Q: Losses suffered by our 401(k) plan participants in recent months have us feeling nervous. Do we, as the owners of our small company, need to purchase fiduciary liability insurance?

A: Under the Employee Retirement Income Security Act of 1974 (ERISA), retirement plan fiduciaries can be held personally responsible for breaching their fiduciary duty. With that in mind, here are a few things to think about when considering whether or not you need to buy insurance against any potential breach or your responsibility as plan fiduciaries.

First, realize that fiduciary liability insurance covers plan sponsors and trustees for penalties they may incur when a participant, or a group of participants, sues them. Lawsuits can stem from participants' beliefs that the sponsor misrepresented their benefits, or that they could have enjoyed higher rates of return if the plan sponsor had made different decisions. Fiduciary liability insurance can also cover the cost of defending against such a lawsuit.

You may be wondering how that fits in with your plan's ERISA-required fidelity bond. The fidelity bond protects the plan's assets when the plan is sued. It doesn't protect the fiduciaries. We suggest that you discuss this very important issue with legal counsel.

Nonprofits Catch a Break on 403(b) Compliance

If the end of 2008 saw you feverishly trying to comply with the new 403(b) rules, you likely breathed a sigh of relief when the Internal Revenue Service (IRS) decided to delay the requirement to adopt your new plan by the end of the year (See the IRS Update on page 4 of this issue). While you now have until December 31, 2009 to adopt the new plan, nonprofits must still comply with other facets of the law. A few highlights:

- 403(b) plans must now have a written plan document. The document should contain the terms and conditions of the plan, like eligibility, benefits, investments, and how and when distributions occur;
- The plan may not delegate administrative responsibilities to employees, but they may use third parties to provide administration and compliance services;
- Employers have a "reasonable time" to forward plan contributions to the proper investment companies. According to the regulations, "reasonable time" could mean within 15 days following the end of the month in which the salary reduction amounts would have otherwise been paid;
- Groups of employees may not be excluded from participating in the plan by classification, unless they are eligible for another salary reduction plan, they normally work fewer than 20 hours per week for the employer, or they are unwilling to contribute at least $200 per year to the plan; *and*
- A "meaningful notice of their right to participate in the 403(b) plan" must be provided to employees at least once a year.

IRS Notice 2009-3 extended the date by which the plan document must be adopted to December 31, 2009. Be aware, though, that IRS expects nonprofits to comply with the law in the interim, using a reasonable interpretation of the rules.

Good-faith effort seems to be important here. IRS says it will view the plan as compliant during 2009 if the submitted document is written as if it is "intended to satisfy" the requirements of the final regulations.

Before the end of 2009, employers must make reasonable efforts to correct any deficiencies in the operation of the plan, based on the written document. It is likely that IRS will issue a draft revenue procedure on the subject of 403(b), and request public comments on it.

"The IRS extension should be viewed for what it is—an extension that makes it clear that the expectation is that nonprofits generally must comply with the 403(b) regulations during 2009, even though they now have until December 31, 2009, to adopt a written plan," said David Ray, vice president at Diversified Investment Advisors. "The objectives of the 403(b) regulations are still the same, which is to shift compliance responsibilities squarely on the backs of plan sponsors and to eliminate differences between 403(b) plans and their more popular cousins, 401(k)s."

What Happened to the Glass Ceiling?

Better cover your head; some researchers at the Tepper School of Business at Carnegie Mellon University claim that the glass ceiling has shattered—for some women, anyway.

Researchers at the school studied the career paths and pay of more than 16,000 executives over a 14-year period. They found that female executives who break through the glass ceiling in corporate America are rewarded with higher overall compensation than their male counterparts, and benefit from the same rate of promotion.

On the other hand, the researchers found that the number of females in top executive positions remains a mere fraction of business leadership overall, largely due to the tendency of women to leave the workforce earlier than men.

The findings show that, among the group studied, female executives earn about $100,000 more per year than do men of the same age, educational background, and job experience. On average, total compensation for all of the executives—about 5 percent were female—was about $2.46 million, including nearly $461,000 in salary and bonus. On average, the executives were 53 years old, and about 23 percent of them held an MBA.

Women within the sample were younger on average than were the men, and had less job experience. Women were better represented at lower executive levels than they were at the very top of the corporate ladder. For example, only 2 percent of executives at the CEO or chairman level were female, while women represented almost 6 percent of CFOs or vice presidents.

"Women aren't climbing as many rungs on the executive ladder because they are more likely than males to retire earlier or switch careers," said Robert A. Miller, professor of economics and strategy at the Tepper School and one of the study's co-authors. "Although women may still be likely to face gender discrimination through unpleasant work environments or tougher, less rewarding assignments, our results find that there does appear to be equal pay and equal opportunity for women if they stay in the workforce and get to the executive level."

If you'd like to learn more, you can download a PDF of the working paper at www.comlabgames.com/ramiller/working_papers/GC100708.pdf.

Don't 'Borrow' Tax Money You're Required to Deduct from Wages

The Internal Revenue Service (IRS), in view of the nation's perilous economic situation, recently urged tax practitioners to remind their clients who are employers to resist the temptation to "temporarily" use for their own purposes money they deduct from their employees' wages for the purpose of paying payroll taxes and retirement plan contributions.

When employers deduct income and Social Security taxes from their employees' wages, the money is not theirs to use as they please, not even for a short period of time.

The employer's failure to remit payroll taxes and retirement plan contributions in a timely manner violates the employer's legal obligation to do so and subjects the employer to heavy penalties (See *IRS Employee Plans News*, p. 6, Fall 2008).

Federal Employment Tax Obligations

If a worker is an employee, rather than an independent contractor, the employer is required to deduct from the employee's "wages" the federal income taxes owed by the employee for those wages and remit them to the IRS in time to meet the next scheduled Federal Tax Deposit deadline.

Employers must also deduct and remit from employee wages Federal Insurance Contributions Act (FICA) taxes and The Federal Unemployment Tax Act (FUTA) taxes.

The FICA requires that wages be taxed to pay for Social Security and Medicare. The FUTA requires that wages be taxed to pay for unemployment compensation.

FICA taxes are costly to the employer as well as the employee. The employer, in addition to having to withhold and remit what the employee owes, also has to pay the government an amount equal to the FICA tax owed by the employee.

Employers are required to remit FICA taxes to IRS every quarter and report the amount of withheld taxes on a quarterly tax return.

Moreover, employers who maintain a retirement plan and allow their employees to make elective deferrals have fiduciary obligations under the Employee Retirement Income Security Act of 1974 (ERISA) to deposit the deducted amounts as soon as these amounts can be segregated from their own general assets, but no later than the 15th business day of the month immediately after the month in which they withheld the contributions. Employers can't use money deducted to pay other business expenses.

Employers' Potential Liability

Employers that fail to timely remit taxes it deducted from their employees' wages could possibly find themselves subject to various penalties, such as:

- Deposit penalties for making late deposits and for not depositing the proper amounts;
- Penalties for failing to file returns and pay taxes when due; *and*
- Penalties for filing false returns and submitting bad checks

The rate of these penalties increases with each passing day until the employer has made the required deposits to IRS. Interest is charged on the total unpaid taxes and the penalties. These penalties and interest can add up quickly.

Personal Liability

And liability can even be "personal." Section 6672 of the Internal Revenue Code (IRC) provides that when an employer fails to properly pay over its payroll taxes, IRS can seek to collect a penalty equal to 100 percent of the unpaid taxes from any *person* who:

(1) is responsible for collecting, accounting for, and paying over payroll taxes and
(2) willfully fails to meet this responsibility.

U of Chi Says, 'Fie on FICA!'

Even great brains can misunderstand the law in this area. For instance, consider the recent case of *University of Chicago v. U.S.* (U.S. Court of Appeals for the 7th Circuit, No. 07-3686 (10/29/08)) which concerned the University's 3-year failure to acknowledge FICA tax responsibilities with respect to employee contributions to two annuity-based retirement plans the University administered for its employees. Participation in the plans was mandatory for all eligible employees as a condition of employment.

The plans required employees to "contribute" to the plans specified percentages of their salaries; the University, in turn, contributed amounts, specified as percentages of the employees' salaries. The University honestly believed that employee contributions did not fall within the Internal Revenue Code's (IRC) definition of "wages" and paid no FICA tax on these contributions.

Definition of 'Wages'

IRC Section 3121(a) defines "wages" as "all remuneration for employment, including the cash value of all remuneration (including benefits) paid in any medium other than cash." Section 3121 further provides that certain kinds of payments are not included in the definition of wages; these exceptions are found in Section 3121(a)(1)-(23).

Section 3121(a)(5)(D) excepts from the definition of wages "any payment made to, or on behalf of an employee or his beneficiary … under or to an annuity contract described in section 403(b) …"

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Section 3121 (a) (5)(D) goes on to state that the exception does not include "*a payment for the purchase of such contract which is made by reason of a salary reduction agreement (whether evidenced by a written instrument or otherwise)"* (italics added).

Therefore, contributions to an annuity-based retirement plan are not "wages" *unless* they were "made by reason of a salary reduction agreement." But what does "salary reduction agreement" mean?

The University believed that it referred only to individually negotiated salary reduction agreements, not to salary reduction agreements made through a retirement plan.

Therefore, reasoned the University, the contributions made by employees were not "wages" because they were made "to an annuity contract described in section 403(b)" and not made "by reason of a salary reduction agreement."

To make a long litigious story short, IRS said the University owed the FICA taxes and 7th Circuit (which covers IL, IN, and WI) held that the contributions were within the exception to the exception despite the mandatory nature of the retirement plans. So, the University had to pay up what it owed, including large failure-to-deposit penalties.

Point to Remember

Employers who resist the temptation to "temporarily" use money withheld from wages to pay employment taxes may nevertheless be in danger of incurring huge potential tax liability if they decide, even on the basis of good-faith reasoning, that they were never required under the IRC to make the deductions in the first place and so refuse to make such deductions.

By the numbers…

	Latest Period	Current	Prior Report	A Year Ago	12-Month % Change
CPI-U	Dec/08	210.2	212.4	210.0	0.1%
CPI-W	Dec/08	204.8	207.3	205.8	-0.5%
ECI EMPLOYMENT COST INDEX					
Total Compensation	3Q/08	108.7	108.0	105.7	2.8%
Wages and Salaries—Metro	3Q/08	109.0	108.4	105.9	2.9%
Wages and Salaries—Nonmetro	3Q/08	109.9	108.9	106.2	3.5%
Benefits	3Q/08	107.5	107.0	105.0	2.4%
Average Weekly Gross Wages*	Dec/08	$611.39	$613.39	$598.26	2.2%
Average Hourly Wages					
All*	Dec/08	$18.36	$18.31	$17.70	3.7%
Construction	Dec/08	$22.48	$22.32	$21.38	5.1%
Manufacturing	Dec/08	$18.03	$17.94	$17.51	3.0%
Trade/Transp./Utilities	Dec/08	$16.17	$16.30	$15.89	1.8%
Wholesale Trade	Dec/08	$20.27	$20.40	$20.10	0.8%
Retail	Dec/08	$12.83	$12.92	$12.64	1.5%
Financial Activities	Dec/08	$20.51	$20.54	$19.97	2.7%
Other Services	Dec/08	$16.02	$15.97	$15.75	1.7%
Unemployment Rate*	Dec/08	7.2%	6.8%	4.9%	2.3%

*seasonally adjusted
(Source: Bureau of Labor Statistics, Washington, D.C.)
All figures are national.

CPI-U: Consumer Price Index for all urban consumers; the newer index representative of the buying habits of about 87% of the total U.S. population. (1982–84=100)

CPI-W: Consumer Price Index for urban wage earners and clerical workers; the older index covering only about 32% of the U.S. urban population.

ECI: Measures change in compensation per hour worked, including wages, salaries, and employer costs of benefits. (6/89=100)

Average Weekly Gross Wages and Average Hourly Wages: Data related to production workers in manufacturing and mining; construction workers; nonsupervisory workers in transportation, public utilities, and wholesale/retail trade; also finance, insurance, real estate, and other services. Accounts for approximately 80% of the total employees on private, nonfarm payrolls.