CHAPTER SIX

Total Rewards

Study Strategies

- On large index cards, write down the names of each of the laws, topics, and key concepts covered in this chapter. On smaller, separate index cards (ideally ones that are a different color), make notes on important facts and details relating to each of these laws, topics, and key concepts (put the name of the law or the topic on the back of the card, not on the front). Then test your memory and understanding by matching the specific facts and details (each of which you wrote on a separate index card) with the laws, topics, and key concepts that you labeled on the larger business cards. After you match them up, you can check how well you did by comparing your matches to the names of the laws and topics that you wrote on the back of the smaller index cards.

- Try writing out your own multiple choice test questions. Writing out the questions along with detailed answers can go a long way toward reinforcing what you are studying. If you've got a study partner, trade questions with that person.

- Although the PHR exam is multiple choice, try writing and answering your own essay-based questions. Write open-ended questions that require a response of at least a full paragraph—and write your answers without looking back at your study materials. The process of actually writing down your answers will reinforce what you already know and will highlight what you need to study more. It will also likely help you as you work to recall this same information when you answer related multiple-choice questions on the actual PHR exam.

- As with each of the six functional areas of HR, determine what you already know and what you don't know. Then work to prepare yourself. Conduct research. Use the Internet to find relevant articles and whitepapers. Peruse textbooks that provide guidance relative to those particular areas. Be sure to find several real-life examples of each responsibility to ensure that you gain a variety of perspectives and insights. This is particularly important for the skill-based, rather than fact-based, components of this functional area.
Introduction

In the first edition of PHR Exam Prep, we introduced this chapter with the following words:

It could be argued that the functional area titled compensation and benefits has been, in one sense, misnamed. This is because these separate areas, when joined together, represent an exponentially larger and more dynamic discipline that is often referred to as ‘total compensation.’

It appears as though our words had a fair amount of merit, for this functional area is now being referred to by HRCI as *total rewards*.

Total rewards encompasses all the rewards that an organization gives, grants, or otherwise bestows on its employees in exchange for the services those employees have rendered through their employment. It includes more obvious items—such as wages and salaries—that would fall under the subheading “compensation,” as well as mandatory and optional benefits such as social security contributions, health and welfare programs, and the like. It also includes items that some, but not all, employees enjoy, such as incentives, bonuses, stock options, and so on.

In this chapter, we’ll look at foundational questions relating to total rewards, starting with one of the most basic (and often overlooked) question: who *is* an employee? We’ll then look at the concept of total rewards before looking at its separate, more frequently recognized components—first compensation, and then benefits. In an effort to make this fact-rich chapter easier to digest, we will separate our scan of compensation-related legislation (which appears at the beginning of this chapter) from our scan of benefits-related legislation (which appears after we have completed our discussion of compensation-related items and before we begin our discussion of benefits-related items). In addition to looking at legislation, we will examine each major component of total rewards.

Total Rewards Footing #1: Employee or Independent Contractor?

As indicated previously, one of the first steps that an organization needs to take is to ensure that individuals who contribute to the attainment of organizational objectives are accurately designated as either “employees” or “independent contractors.”

As with most areas of HR, this question is not as simple as it might initially appear. There is no immediate answer—no single test to resolve the question of whether an individual is an employee or an independent contractor. To assist in this effort, the Department of Labor (DOL) has published a fact sheet citing U.S. Supreme Court rulings that offer the following seven factors, which help to appropriately resolve the seemingly perpetual employee/independent contractor conundrum (see www.dol.gov):

1. The extent to which the services rendered are an integral part of the principal’s business.
2. The permanency of the relationship.
3. The amount of the alleged contractor’s investment in facilities and equipment.
4. The nature and degree of control by the principal.
5. The alleged contractor’s opportunities for profit and loss.
6. The amount of initiative, judgment, or foresight in open market competition with others required for the success of the claimed independent contractor.
7. The degree of independent business organization and operation.

The IRS also offers guidance at its website (www.irs.gov) with respect to properly classifying employees and independent contractors. According to the IRS, it is critical to examine the nature of the relationship between the worker and the organization. Specifically, all evidence of “control” and “independence” must be carefully considered. The IRS identifies three categories of control into which facts and evidence can be divided: behavioral control, financial control, and the type of relationship.

- **Behavioral Control**—Who controls and directs how the work is done? For instance, it could be argued that the business maintains behavioral control if it provides the individual with training, instructions, and so forth.

- **Financial Control**—Does the business have a right to control the financial and business aspects of the worker’s job? More specifically
  - To what extent does the worker have unreimbursed business expenses?
  - What is the extent of the worker’s investment in the facilities used in performing services?
  - To what extent does the worker make his or her services available to the relevant market?
  - How does the business pay the worker?
  - To what extent can the worker realize a profit or incur a loss?

- **Type of Relationship**—Is there a written contract in place? If so, to what extent does it describe
  - The relationship the parties intended to create?
  - The extent to which the worker is available to perform services for other, similar businesses?
  - Whether the business provides the worker with employee-type benefits, such as insurance, a pension plan, vacation pay, or sick pay?
  - The permanency of the relationship?
  - The extent to which services performed by the worker are a key aspect of the regular business of the company?
Total Rewards Footing #2: Exempt or Non-exempt?

As mentioned earlier, Federal Labor Standards Act (FLSA) addresses four areas: minimum wage, record keeping, child labor, and overtime. In this “Footing #2” section, we will focus on the minimum wage and overtime provisions because ascertaining exempt and non-exempt status is foundational to a discussion of total compensation.

On August 23, 2004, new minimum wage and overtime regulations to the FLSA were enacted.

NOTE

Interestingly, the DOL website specifically states that these revisions pertain to the overtime and minimum wage provisions of the FLSA. However, the $455 weekly threshold is more than twice the minimum wage that was in effect at the time these regulations passed, and no increase in the minimum wage was included with these revisions (a new federal minimum wage took effect as of July 24, 2007). The focus of the 2004 revisions, therefore, seems to be more on the overtime provisions of the FLSA, which is where we will maintain our focus in this section.

TIP

These provisions were hotly debated and widely discussed before implementation. Be alert to any changes that might be implemented.

Exemptions: The Basics

Known as FairPay, the 2004 revisions marked some significant changes relative to determining whether an employee is exempt or non-exempt from the overtime provisions of the FLSA. According to these regulations, employees would be classified as exempt if they

- Meet certain tests regarding their job duties
- Are paid on a salary basis
- Earn no less than $455 per week
Salary Basis

HR professionals need to have a solid understanding of what it means when an employee works on a salary basis. According to the DOL, being paid on a salary basis means that

“An employee regularly receives a predetermined amount of compensation each pay period on a weekly, or less frequent, basis. The predetermined amount cannot be reduced because of variations in the quality or quantity of the employee’s work. Subject to exceptions listed below, an exempt employee must receive the full salary for any week in which the employee performs any work, regardless of the number of days or hours worked. Exempt employees do not need to be paid for any workweek in which they perform no work. If the employer makes deductions from an employee’s predetermined salary, i.e., because of the operating requirements of the business, that employee is not paid on a ‘salary basis.’ If the employee is ready, willing and able to work, deductions may not be made for time when work is not available.”

CAUTION

Job duties—not job titles—must be used to determine an employee’s FLSA status. (In other words, don’t use an employee’s title to determine whether the employee is eligible to earn overtime; go by the work that an employee actually performs.)

It’s important to be aware of a number of notable changes that were enacted with the FairPay provisions (see www.dol.gov/esa for more information). These changes included

- The elimination of separate “short” and “long” tests (based on what an employee earned each week).
- Any employees earning less than $455 per week (equivalent to $23,660 per year) are automatically covered by the overtime provisions of the FLSA (“non-exempt”)—regardless of the duties that they perform in their jobs. In other words, any employee who earns less than $23,660 is automatically eligible to earn overtime pay.
- The elimination of the long test resulted in the elimination of the well-known requirement that exempt employees cannot spend more than 20% of their time each week on non-exempt–level activities.

Types of Exemptions: Non-computer Employees, Non-highly Compensated Employees, and Outside Sales Employees

NOTE

One concept that is integral to a discussion of FLSA exemptions is primary duty, which refers to the principal, main, major, or most important duty that the employee performs.
Consistent with the 2004 FairPay revisions, employers must now apply one of the following four standard tests to employees (except those who do computer work) who are paid on a salaried basis and whose salaries are between $23,660 and $99,999 per year.

Please note that in order to qualify for any particular exemption, an employee must meet all of the tests listed in that exemption.

**Executive Exemption**
- The employee’s primary duty must be managing the enterprise or managing a customarily recognized department or subdivision of the enterprise.
- The employee must customarily and regularly direct the work of at least two or more other full-time employees or their equivalent.
- The employee must have the authority to hire or fire other employees, or the employee’s suggestions and recommendations as to the hiring, firing, advancement, promotion, or any other change of status of other employees must be given particular weight.

**Administrative Exemption**
- The employee’s primary duty must be the performance of office or nonmanual work directly related to the management or general business operations of the employer or the employer’s customers.
- The employee’s primary duty includes the exercise of discretion and independent judgment with respect to matters of significance.

**Learned Professional Exemption**
- The employee’s primary duty must be the performance of work requiring advanced knowledge, defined as work which is predominantly intellectual in character and which includes work requiring the consistent exercise of discretion and judgment.
- The advanced knowledge must be in a field of science or learning.
- The advanced knowledge must be customarily acquired by a prolonged course of specialized intellectual instruction.

**NOTE**

Determination of an employee’s primary duty must be based on all the facts in a particular case, with the major emphasis being on the character of the employee’s job as a whole.
Creative Professional Exemption

- The employee's primary duty must be the performance of work requiring invention, imagination, originality, or talent in a recognized field of artistic or creative endeavor.

Types of Exemptions: Computer Employees

The Computer Employee exemption is slightly different with respect to pay. To qualify for the computer employee exemption, the following tests must be met:

- The employee must be compensated either on a salary or fee basis (as defined in the regulations) at a rate not less than $455 per week or, if compensated on an hourly basis, at a rate not less than $27.63 an hour.

- The employee must be employed as a computer systems analyst, computer programmer, software engineer, or other similarly skilled worker in the computer field performing the duties described next:

  1. The application of systems analysis techniques and procedures, including consulting with users to determine hardware, software, or system functional specifications.
  2. The design, development, documentation, analysis, creation, testing, or modification of computer systems or programs, including prototypes, based on and related to user or system design specifications.
  3. The design, documentation, testing, creation, or modification of computer programs related to machine operating systems.
  4. A combination of the aforementioned duties, the performance of which requires the same level of skills.

Types of Exemptions: Outside Sales

Unlike the other types of exemptions, a minimum salary is not required to establish an exemption on the basis of outside sales. The following criteria, however, must be met:

- The employee's primary duty must be making sales (as defined in the FLSA), or obtaining orders or contracts for services or for the use of facilities for which a consideration will be paid by the client or customer.

- The employee must be customarily and regularly engaged away from the employer's place or places of business.

Types of Exemptions: Highly Compensated Employees

FairPay defines highly compensated employees as those who

- Earn $100,000 or more annually (of which at least $455 per week must be paid on a salary or fee basis).
Perform office or nonmanual work.
- Customarily and regularly perform at least one of the duties of an exempt executive, administrative, or professional employee identified in the standard tests for exemption.

**Other Key FairPay Items**

HR professionals also need to be familiar with several important considerations relative to the overtime provisions of the FLSA that were clarified in the 2004 revisions.

**Specific Non-exempt Designations**

**Non-exempt:** Manual laborers and other “blue collar” workers who perform work involving repetitive operations with their hands, physical skill, and energy cannot be exempted from the overtime provisions of FLSA, no matter how much they earn. This would include nonmanagement employees who work in maintenance or who are carpenters, electricians, mechanics, plumbers, iron workers, and so on.

**Police, Firefighters, Paramedics, and Other First Responders**

The act also specifically identifies other positions that are likely to be non-exempt (in other words, positions that are likely to be eligible for overtime pay), although a case-by-case review is still needed. These positions include the following:

- Police officers, detectives, deputy sheriffs, state troopers, highway patrol officers, investigators, inspectors, correctional officers, parole or probation officers, park rangers, firefighters, paramedics, emergency medical technicians, ambulance personnel, rescue workers, hazardous materials workers, and similar employees, regardless of rank or pay level, who perform work such as preventing, controlling, or extinguishing fires of any type; rescuing fire, crime, or accident victims; preventing or detecting crimes; conducting investigations or inspections for violations of law; performing surveillance; pursuing, restraining, and apprehending suspects; detaining or supervising suspected and convicted criminals, including those on probation or parole; interviewing witnesses; interrogating and fingerprinting suspects; preparing investigative reports; or other similar work.

**Safe Harbor Provisions (from Improper Deductions from Salary)**

Improper salary deductions can cause an employer to lose the FLSA exemption—and not just for the employee from whom the deduction was improperly made.

**EXAM ALERT**

Familiarize yourself with circumstances under which employers can make deductions from an employee’s salary.
If it is found that an employer has “actual practice” of making improper salary deductions, the employer will lose the exemption during the time period of the deductions for employees in the same job classification working for the same managers responsible for the improper deductions.

Under the new safe harbor provision, however, an employer can protect itself from losing the exemption if the employer

1. Has a clearly communicated policy prohibiting improper deductions and including a complaint mechanism.

2. Reimburses employees for any improper deductions.

3. Makes a good faith commitment to comply in the future.

C&B Footing #3: Compensation + Benefits = Total Rewards

An organization’s total rewards philosophy represents far more than just the amount of cash it pays to employees, or even the “fringe benefits” that it provides. Instead, an organization’s total rewards philosophy speaks volumes about what the leaders of that organization value, the results they want to attain, the behavior they want to encourage, and their commitment to their employees. It will also have a significant impact on the organization’s efforts to attract, motivate, and retain talent.

In many ways, an organization’s total compensation philosophy is a clear and direct expression of the organization’s mission, vision, and values—whether or not the organization intends it to be so. Even the absence of a clearly defined compensation system or philosophy says something—and nothing can stop those messages from being received, loud and clear, by employees. Just as it is impossible for a person not to communicate, so too it is impossible for an organization’s total rewards program (or absence thereof) not to send a clear message to employees and potential employees about what is important to the organization.

Objectives of a Total Rewards Program

Because an organization’s total rewards program says so much, it’s imperative that it be designed deliberately, intentionally, and with overarching as well as specific objectives in mind.

Those specific objectives will vary from organization to organization, and during different phases of the organization’s life cycle, and to some degree from position to position. Certain overarching objectives, however, should be kept in mind when crafting a total compensation program—objectives that can be addressed, at least initially, by asking the following questions:
How can—and will—we design a total rewards system that
- Supports and reinforces the mission, vision, and values of the organization?
- Is consistent with the culture of the organization?
- Attracts, motivates, and retains targeted/appropriate employees?
- Ensures internal equity between positions within the organization?
- Supports our philosophy toward the external labor market?
- Is affordable, sustainable, and cost effective?
- Is legally defensible in the event of a challenge?
- Is appropriate for the organization’s current position in its life cycle?
- Is flexible and easily adaptable?

In an effort to better appreciate the nuances that need to be considered when crafting a total rewards philosophy, let’s take a closer look at two of these questions.

**Attracting, Motivating, and Retaining Targeted/Appropriate Employees**

For some organizations, there may be great value in attracting, motivating, and retaining high-performing employees who (hopefully) are “in it for the long haul.” In these situations, important considerations may need to be factored in, such as long learning curves, maintaining sensitive and critical client relationships, and so on. For these organizations, there may be a strong focus on designing a total compensation system that would be perceived as very competitive in the relevant labor market and that would encourage high-performing employees to stay with the organization for the long term.

Conversely, some organizations are perfectly comfortable with relatively high (or just plain high) levels of turnover. Although these organizations might be interested in developing a total rewards program that will attract employees, motivating and retaining their employees might be of far less importance. Alternatively, those organizations whose employees do not require much training and/or whose employees form only transient relationships with customers might develop a total rewards philosophy that positions them less competitively in the relevant labor market. By itself, neither approach is right nor wrong. However, if you were to switch the two total rewards systems for these two types of organizations, the mismatch could create a significant disconnect—rendering both philosophies ineffective and even counterproductive.

**Supporting the Philosophy Toward the Relevant Labor Market**

There are three primary approaches from which organizations choose when deciding how they want to position themselves relative to the external labor market with respect to total rewards. We’ll look at those three approaches in a moment. First, however, it’s necessary to understand the meaning of the term *relevant labor market*.
The relevant labor market relates to the size and scope of the geographic area within which an organization would seek to attract qualified candidates. Even within the same organization, the relevant labor market for different positions can vary widely depending on the knowledge, skills, abilities, and behavioral characteristics required to perform each position successfully. Other factors that impact how an organization defines the relevant labor market might be the degree of competition that exists among employers for particular skills and/or knowledge and the degree to which certain skills and/or knowledge requirements are industry specific.

### NOTE

Depending on the size and scope of the relevant labor market, you may need to take geographic differentials in pay into consideration. For instance, the same position could be compensated significantly differently in different parts of the nation, particularly if the relevant labor market for that position is relatively small. Conversely, if a relevant labor market for a particular position is truly nationwide in scope, it is possible there may be relatively little difference in pay rates regardless of where the position is geographically based.

After the relevant labor market has been defined for a particular position, the organization must choose between the three approaches alluded to earlier—leading, lagging, or matching the market.

### NOTE

It’s critical to note that any of these three approaches could be adopted across an entire organization or just for certain positions within an organization. It’s important, however, to ensure that internal equity is consistently maintained if different approaches (lead, lag, or match) are applied to different positions within the same organization.

#### Lead the Market

Organizations may choose to offer total compensation packages that are “better” than packages being offered by their labor market competitors. Organizations that lead the market may believe that higher compensation packages will attract higher-performing employees who will, in turn, “pay for themselves,” and then some. In short, these organizations want the “best of the best” and are willing to pay for it.

#### Lag the Market

Organizations may choose—by design, or simply because of budgetary constraints—to offer total rewards packages that are “less attractive” than the total rewards packages that are being offered by their labor market competitors. Organizations that lag the market might offset this potential disadvantage by reinforcing and maximizing the intrinsic rewards that it offers—long-term potential growth opportunities, the ability to contribute to a particularly significant organizational mission, and so on.
Match the Market

Organizations may choose to offer total rewards packages that are comparable to the total rewards packages being offered by their labor market competitors. Organizations that match the market make a conscious choice to be “externally competitive” with respect to total compensation.

NOTE

It’s important to keep in mind that how an organization addresses even the most overarching questions can vary considerably, depending on the organization itself, the phase of the business life cycle in which the organization finds itself, and even the positions under consideration. As with all other areas of HR, therefore, there are no simple answers. (If you’re tempted to say that any situation in which you find yourself as an HR professional is a “no brainer,” look again—you may have overlooked something.)

Elements of a Total Rewards Program

Total rewards consists of a variety of elements, all of which can be divided into direct compensation and indirect compensation.

Direct compensation refers to components that are presented to employees in the form of cash, and indirect compensation refers to components that are presented to employees in forms other than cash (noncash).

Some examples of direct compensation are

- Hourly wages/base salary
- Shift differentials
- Overtime pay
- Commissions
- Sign-on bonuses
- Variable pay (such as short-term and long-term incentives)

Some examples of indirect compensation are

- Legally mandated benefits (such as social security)
- Medical insurance
- Dental insurance
- Long-term disability insurance
- Vision coverage
- Vacation time
- Holiday time
Recognition programs (such as peer recognition programs, noncash spot awards, achievement awards, “pizza parties,” desirable parking, and so on)

Perquisites (also known as “perks,” such as a company car, club memberships, financial planning, and so on)

NOTE
In addressing problems and questions that might come up, it's important to keep in mind that what may initially appear to be a compensation problem may in fact not be one. It is very possible that the problem under consideration is unrelated to compensation, or that it is related to compensation as well as other issues. Although it is also possible that the problem under consideration might truly be a compensation problem, even then, it's important to think in terms of “total rewards” instead of just automatically “throwing money” at a problem. Without a doubt, your internal consulting skills will really come in handy here as you work to identify the true root causes of your clients’ challenges with them.

Communicating the Total Rewards Program
It's not enough to “walk the walk”—you’ve also got to “talk the talk.”

Often, when we look around our organizations, our country, or even our world, we see people who “talk the talk” but don’t “walk the walk.” Or, to put it differently, people don’t always “put their money where their mouths are.” Interestingly, when it comes to total rewards programs, the opposite tends to be true. Organizations often don’t communicate enough with employees about the total compensation/benefits programs that they have in place, the benefits of these programs, or about what those programs really cost.

For a number of reasons, it's important to change this practice, and to communicate with employees. Most employees simply do not know the real costs—let alone the actual value—of the benefits they receive. Also, in a very real sense, employees earn benefits, just like they earn cash compensation—and it's important to ensure that employees understand and recognize that. This holds true for benefits that are voluntarily provided by employers, as well as for benefits programs that are mandated by the government. Otherwise, even those benefits that are not entitlements may ultimately begin to feel like entitlements to employees.

There are myriad ways to communicate with employees about the benefits they receive, just a few of which are

- Employee meetings
- Newsletters
- DVDs
- Employee handbooks
- Annual total rewards statements
- Personal letters/emails
- Internet/intranet

Communicate early, and communicate often. Perhaps most important, don’t rely on any single method of communication to get your message across. Just as people learn differently in training programs (see Chapter 5, “Human Resource Development”), people also process and absorb information differently. Finally, always make sure that at least one of your methods of communication is in writing—something that employees can refer to after-the-fact.
REVIEW BREAK

At this point, we’ve established a strategic and theoretical foundation that will provide us with a context within which to consider some of the fact-based and practical elements of total rewards. Next, let’s review some key compensation-related legislation.

Related Legislation: Compensation

Although many laws have some relevance to compensation, the following are some of the most important ones with which HR professionals need to be familiar.

Davis-Bacon Act, 1931

The Davis-Bacon Act was the first piece of legislation to consider the topic of—and actually establish—a minimum wage. Davis-Bacon, however, was and still is limited to the construction industry, specifically those contractors and subcontractors on

- Any and all federal government construction contracts
- Nonfederal government construction projects in excess of $2,000 that receive federal funding

Contractors and subcontractors who meet either of these criteria are required to provide laborers and mechanics who are employed at the actual worksite with wages and benefits that are equal to (or better than) what workers on similar local projects receive.

Walsh-Healey Public Contracts Act (PCA), 1936

The next significant piece of compensation-related legislation was the Walsh-Healey Public Contracts Act (PCA), enacted in 1936.

The Walsh-Healey PCA requires contractors who have contracts with the federal government that exceed $10,000 to pay an established minimum wage to workers employed through that contract. In addition to minimum wage, Walsh-Healey PCA also addressed issues including overtime pay and safe and sanitary working conditions.

Fair Labor Standards Act (FLSA), 1938

NOTE

In the section titled “Total Rewards Footing #2: Exempt or Non-exempt?,” we explored the overtime provisions of the FLSA, particularly with respect to the 2004 FairPay revisions. Here we’ll focus on the other three provisions of the law, as well as some of the more technical aspects of the overtime provision.

Although it was initially enacted in 1938, the Fair Labor Standards Act (FLSA) still has a profound impact on employees today because of its wide scope and the degree to which it directly impacts the lives of nearly every American worker.
The FLSA covers full-time and part-time workers in the private sector and in federal, state, and local governments. It addresses minimum wage, overtime, equal pay, record keeping, and child labor standards (referred to by the government now as “youth employment standards”). For private enterprise employees, it is administered by the Wage and Hour Division of the DOL. For federal employees, the FLSA is administered either by the Wage and Hour Division or the U.S. Office of Personnel Management (which, interestingly, refers to itself as “The Federal Government’s Human Resources Agency” on its website).

In looking at the FLSA, let’s take a look at each of the areas it covers, in the following order:

- Minimum wage
- Overtime pay
- Child labor standards (youth employment standards)
- Record keeping

**Minimum Wage**

The FLSA established a federal minimum wage for private sector employees and for all other employees covered by the act. From time to time, minimum wage has become a hotly debated issue in Congress, because Congress has the responsibility for introducing legislation that will change the federal minimum wage. In our nation’s system of checks and balances, however, that hotly debated congressional issue quickly becomes a hotly debated presidential issue, because it is the president who must either sign or veto legislation to increase the minimum wage.

In May of 2007, the federal minimum wage was increased for the first time in 10 years from $5.15 to $7.25 per hour in stages over two years, as shown in Figure 6.1.

**EXAM ALERT**

Be familiar with government-sponsored programs that enable employers to pay certain employees (full-time students, certain people with disabilities, and so on) at an hourly rate of pay that is less than the federal minimum wage.

**NOTE**

Many states have established a minimum wage that is higher than the federally established minimum wage. In these circumstances, employees would be entitled to the state minimum wage (because in this case, the state law is more generous than the federal law, and thus supersedes the federal law).
## EMPLOYEE RIGHTS
UNDER THE FAIR LABOR STANDARDS ACT
THE UNITED STATES DEPARTMENT OF LABOR WAGE AND HOUR DIVISION

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### OVERTIME PAY
At least 1½ times your regular rate of pay for all hours worked over 40 in a workweek.

### YOUTH EMPLOYMENT
An employee must be at least 16 years old to work in most non-farm jobs and at least 18 to work in non-farm jobs declared hazardous by the Secretary of Labor.

Youths 14 and 15 years old may work outside school hours in various non-manufacturing, non-mining, non-hazardous jobs under the following conditions:

- No more than
  + 3 hours on a school day or 18 hours in a school week
  + 8 hours on a non-school day or 40 hours in a non-school week

- Also, work may not begin before 7 a.m. or end after 9 p.m., except from June 1 through Labor Day, when evening hours are extended to 9 p.m. Different rules apply in agricultural employment. For more information, visit the YouthRules! Web site at www.youthrules.dol.gov.

### TIP CREDIT
Employers of "tipped employees" must pay a cash wage of at least $2.13 per hour if they claim a tip credit against their minimum wage obligation. If an employee’s tips combined with the employer’s cash wage of at least $2.13 per hour do not equal the minimum hourly wage, the employer must make up the difference. Certain other conditions must also be met.

### ENFORCEMENT
The Department of Labor may recover back wages either administratively or through court action, for the employees that have been underpaid in violation of the law. Violations may result in civil or criminal action.

Civil money penalties of up to $11,000 per violation may be assessed against employers who violate the youth employment provisions of the law and up to $1,000 per violation against employers who willfully or repeatedly violate the minimum wage or overtime pay provisions. This law prohibits discriminating against or discharging workers who file a complaint or participate in any proceedings under the Act.

### ADDITIONAL INFORMATION
- Certain occupations and establishments are exempt from the minimum wage and/or overtime pay provisions.
- Special provisions apply to workers in American Samoa and the Commonwealth of the Northern Mariana Islands.
- Some state laws provide greater employee protections; employers must comply with both.
- The law requires employers to display this poster where employees can readily see it.
- Employees under 20 years of age may be paid $4.25 per hour during their first 90 consecutive calendar days of employment with an employer.
- Certain full-time students, student learners, apprentices, and workers with disabilities may be paid less than the minimum wage under special certificates issued by the Department of Labor.

For additional information:

**1-866-4-USWAGE**
(1-866-487-9243)  TTYY: 1-877-889-5627

WWW.WAGEHOUR.DOL.GOV

U.S. Department of Labor | Employment Standards Administration | Wage and Hour Division

WHD Publication 1318 (Revised June 2007)

Want a Good Tip?

Here’s one—be sure your tipped employees earn at least the minimum wage.

The FLSA specifically addresses the question of employees who receive tips. According to the act, an employer of “tipped employees” must pay those employees for every hour worked, even if the employees’ tips alone would result in them earning more than the minimum wage. The minimum rate of pay that can be paid to tipped employees (available at www.dol.gov/esa), however, is substantially less ($2.13 as of the date this book was printed) than the minimum wage that must be paid to employees who do not receive tips. To be eligible to pay tipped employees this lower hourly rate, the employer must meet certain conditions, including (but not limited to) the following:

- The employer must claim a tip credit against its minimum wage obligation.
- Each employee’s tips combined with the hourly rate that the employer is paying must meet or exceed the federal minimum hourly wage. Otherwise, the employer must make up the difference.

Overtime Pay

According to the FLSA, non-exempt employees must be paid at least the minimum wage for the first 40 hours worked during the workweek. If an employee works more than 40 hours during the workweek (commonly referred to as “overtime”), he or she must be paid those overtime hours at a rate that is at least 150% (commonly referred to as “time and a half”) of his or her regular rate of pay per hour—which may be different from the employee’s stated hourly wage rate.

In addition to the all-important questions of who is (and isn’t) exempt from the overtime provisions of the FLSA, at least two additional pivotal questions related to overtime must be addressed:

1. How is the number of hours worked calculated?
2. What rate of pay must be used to determine the regular rate of pay per hour (which will, in turn, be used to calculate the overtime pay rate)?

Calculating the Number of Hours Worked During the Workweek

To calculate the number of hours worked during the workweek, it’s first necessary to understand the government’s definition of and rules regarding workweeks (as published at www.dol.gov):

- A workweek is any fixed and regularly recurring period of 168 hours (24 hours in a day, seven days a week).
- The employer can select any day (and any hour) of the “calendar week” on which to begin the “workweek.” Once chosen, however, that day (and hour) must remain constant (hence the “fixed” and “recurring” requirement).
- The employer can establish different workweeks for different employees or groups of employees.
- The hours that an employee works during different workweeks cannot be “averaged” (to avoid overtime payments, or for any other reason).
After you've got a handle on what a workweek is, the next step is to understand how to determine what “hours worked” really means.

First of all, “hours worked” means “hours worked”—not “hours paid.” In other words, according to the FLSA, hours that have been paid but not worked (vacation time, sick time, holiday time, jury duty time, and the like) do not count toward the 40-hour threshold (although some organizations may voluntarily choose to count these hours toward the 40-hour threshold).

**CAUTION**

“Hours worked” also doesn’t mean “hours approved to work.” If an employer “suffers or permits” a non-exempt employee to work, that employee must be compensated for time worked. So, whether the employer requires the employee to work or simply allows the employee to work, the time counts as “hours worked” and must be compensated accordingly.

**Calculating the Regular Rate of Pay**

An employee’s regular rate of pay includes more than just his or her hourly rate of pay; it would also include any incentives and commissions. It would not, however, include bonuses (which, unlike incentive programs, are discretionary), pay for time not worked, premium pay for weekend or holiday work, and the like.

**CAUTION**

It is critical that employers calculate overtime payments on the basis of each employee’s regular rate of pay, not on each employee’s hourly rate of pay.

**NOTE**

As with minimum wage, some states have established more generous overtime laws—for instance, laws that require overtime pay after an employee has worked eight hours in any one day, regardless of how many hours the employee works during the entire workweek. As is also the case with minimum wage, a more generous state law would supersede the federal law.

**Child Labor Standards**

The child labor provisions of the FLSA restrict the number of hours (and the times of the day) that children under the age of 16 can work, as well as the types of work that children under the age of 18 can perform.

Under the Fair Labor Standards Act (FLSA)

- Children under the age of 14 years cannot be employed (different guidelines exist for certain jobs, such as for farm work or work performed for the child’s parent).
- Hours worked by 14- and 15-year-olds are limited to
  - Nonschool hours
  - 3 hours in a school day
- 18 hours in a school week
- 8 hours in a nonschool day
- 40 hours in a nonschool week
- Hours between 7 a.m. and 7 p.m. (except from June 1 through Labor Day, when evening hours are extended to 9 p.m.)
- Youth who are under 18 years of age may perform nonhazardous jobs. Youth who are 14 and 15 years of age are also restricted from performing manufacturing, mining, and hazardous jobs.
- Youth who are 16 years of age and older (and adults) may work an unlimited number of hours per day.
- The FLSA does not require work permits or working papers, but certain states do.

**Record Keeping**

Employers must maintain accurate and complete records for each non-exempt employee of hours worked and wages earned. Certain identifying information (such as social security number, address, and so on) is also required. No specific method of timekeeping is required. See the act for more specific information about these record-keeping (and retention) requirements.

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**NOTE**

Employers are required to post the provisions of the FLSA.

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**Portal-to-Portal Act, 1947**

In May of 1947, the FLSA was amended by the Portal-to-Portal Act. Section 254(a) of the Portal-to-Portal Act offered clearer definitions of “hours worked” for purposes of minimum wage and overtime payments. According to the act, employers are required to compensate workers only for working time that they spend on activities that relate to the performance of their job.

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**EXAM ALERT**

This statement, while accurate, is also incomplete, in that it does not even begin to address the nuances of the Portal-to-Portal Act. The act, for instance, addresses travel time (on public transportation, on private transportation, during work hours, outside work hours), pre-shift work, post-shift work, idle waiting time, overnight travel, training time, and many other considerations. Familiarize yourself with this act before paying your employees and before taking the PHR exam.
Equal Pay Act (EPA), 1963

The EPA prohibits discrimination on the basis of sex in the payment of wages or benefits to men and women who perform substantially equal (but not identical) work, for the same employer, in the same establishment, and under similar working conditions. (An “establishment” generally refers to one specific physical location.) Similar to the way in which FLSA status is determined, “substantial equality” is determined by job content, not job titles. More specifically, the substantial equality of job content is assessed on the basis of the following four factors:

- **Skill**—The amount or degree of experience, ability, education, and training required to perform the job. Comparisons must be made on the basis of the skills that are required to perform the job—not on the skills that the incumbents happen to possess.
- **Effort**—The amount of physical or mental exertion required to perform the job.
- **Responsibility**—The degree of responsibility and accountability that an employer entrusts to and expects from a particular person in a specific position.
- **Working Conditions**—The physical surroundings of the position, as well as any hazards associated with a particular position.

Employers can, however, set forth “affirmative defenses” to explain inequities in pay between men and women. These arguments can be based on—and must be proven to be—a function of

- Seniority
- Merit
- Quantity or quality of production
- Any factors other than sex

REVIEW BREAK

This section has provided an overview of some of the laws that are most relevant to compensation-related topics. Now let’s take a look at the actual building blocks that you can use to bring compensation principles to life within your organization.

Compensation: Job Evaluation

Job evaluation is the process through which every job in an organization is assessed and compared to other jobs in the organization. At the conclusion of the job evaluation process, you will be able to ascertain the relative worth of each job within the organization. When this is done, you will have generated an overall job-worth hierarchy.

Job evaluation techniques fall into two categories: nonquantitative and quantitative.
Nonquantitative Job Evaluation Techniques

Nonquantitative job evaluation techniques, as the name implies, determine the relative value of jobs within the organization without using mathematical techniques. Instead, these methods focus on the “whole job” (which is why these techniques are also referred to as whole job methods).

Whole Job Ranking

In whole job ranking techniques, jobs are ranked from lowest to highest, according to the importance that each job holds (or, stated differently, the value that each job brings) to the organization. In essence, a list is generated that reflects which jobs are more important to the organization, and which jobs are less important to the organization, in ranked order.

Whole job ranking is easy to perform and is also relatively inexpensive to maintain. It fails, however, to establish specific factors about each job that would need to be taken into consideration when comparing jobs to each other, and it can be prone to rater subjectivity. It is also limited to a job-to-job comparison, rather than to any specific competencies or responsibilities that are universally valued throughout the organization. Also, if more than just a few positions need to be ranked, this system may prove to be unwieldy within the organization. Finally, although the list that is generated through whole job ranking will show which jobs are most and least important, it will not demonstrate the relative worth of one job to another.

Job Classification

Job classification is a nonquantitative job evaluation technique that categorizes jobs into broad categories, or levels, based on the level—and, ultimately, value to the organization—of the work that is performed by jobs within each level. Each level incorporates specific responsibilities and “benchmark statements” that describe the nature, complexity, autonomy, and so on of the work that is performed by positions in that level.

In addition to being inexpensive, job classification is relatively simple to implement and administer. One potential disadvantage, however, is that jobs may not match perfectly with the benchmark statements listed in each category. In such cases, the evaluator would use his or her judgment (which can, of course, be imperfect and/or subjective at times) to choose the best possible classification. Another potential weakness of the job classification method is that raters are also more likely to evaluate jobs on the basis of the current incumbent, rather than on the basis of the jobs themselves, thus violating a key principle of sound job evaluation.

Job Slotting

Job slotting incorporates (or “slots”) newly created or revised positions into an existing job hierarchy. This process of slotting is accomplished by comparing the new or revised job descriptions to jobs (and job descriptions) that have already been evaluated and slotted within the hierarchy.
Like the other nonquantitative job evaluation methods, job slotting is relatively inexpensive and simple to administer and implement. Job slotting can be used, however, only when a job structure is already in place. As with the other nonquantitative job evaluation methods, there is an increased possibility that rater error and subjectivity can taint the job evaluation process. It is also more likely that jobs will be evaluated on the basis of the current incumbent, rather than on the basis of the jobs themselves, thus violating a key principle of sound job evaluation.

**Quantitative Job Evaluation Techniques**

Quantitative (or *factor based*) job evaluation methods identify the degree to which each position is responsible for or requires specific compensable factors. *Compensable factors* are those skills, abilities, characteristics, or areas of responsibility that an organization values, and for which it is willing to pay. Some sample compensable factors include education, experience, financial responsibility, responsibility for contacts, and so on.

Factor-based methods generate a mathematical score that reflects each position’s relative worth to the organization.

**Point Factor**

Point factor systems first identify specific compensable factors and then establish levels of performance *within* each of those compensable factors. The relative importance of each compensable factor to the organization is then weighted. A different point value is then assigned to each level within each compensable factor.

After a point factor system has been established, each job is evaluated according to this system by determining which level within each compensable factor is most reflective of the position being evaluated, thus generating a point value for each compensable factor. The evaluator then adds up the points associated with each compensable factor to calculate a total point value. When the point values associated with each job are compared to each other, a mathematical depiction of the relative and absolute value of the jobs will emerge, thus indicating where the job falls within the established job worth hierarchy.

The point factor system affords greater reliability between different raters and minimizes the potential impact of evaluator error or subjectivity. Developing a point factor system, however, can be time consuming and difficult—and purchasing one can be expensive. In addition, using it properly requires some measure of training.

**Factor Comparison**

Factor comparison is a quantitative job evaluation technique that involves the ranking of each compensable factor of each job. A corresponding monetary value for each level with each factor is subsequently identified. Similar to the point factor method, each job is evaluated with respect to each compensable factor. The appropriate level is selected. Unlike the point factor method, however, a “dollar value” is associated with each level with each compensable factor. When all the levels that have been selected are added together, a pay rate will emerge for each job.
Although this system affords a degree of objectivity and reliability across raters, it is difficult and expensive to develop. It also requires a great deal of monitoring and updating to ensure that the dollar value associated with each level remains appropriate, in a relative as well as in an absolute sense.

**Compensation: Market Pricing**

Market pricing involves looking at the relevant labor market to ascertain what the “going rate” or “market rate” is for a particular position. Market pricing can yield valuable pay data about “benchmark” jobs—jobs for which close matches can be identified in the relevant labor market.

Data collected through market pricing can be used in a number of ways. For example, market data can be obtained about a number of benchmark positions as part of a larger initiative. Market data can also help in the building of a job-worth hierarchy, around which other positions can be placed using a whole job slotting technique. Market data can also be used to obtain information for one particular job, in combination with other job evaluation techniques that might be used.

**Market Data Considerations**

In preparing to collect market data, there are a number of considerations that need to be taken into account and a number of decisions that need to be made. Let’s take a look at some of the questions that might be relevant.

**What Is the Relevant Labor Market?**

We first looked at the topic of relevant labor markets when we started considering the importance of the organization's total rewards philosophy. Within the context of collecting market data, determining an appropriate relevant labor market for each position is foundational to ensuring that the market data we collect—and about which we will be making decisions—is truly relevant.

**Who Are Our Labor Market Competitors in General, and for Specific Jobs?**

Determining who your labor market competitors are within the relevant labor market is also critical. One important consideration is whether you are competing only within your industry for talent, or whether you are also competing for talent with organizations in different industries or sectors.

**What Sources of Market Data Are Currently Available to You, and What Sources Could You Secure?**

Pay surveys provide one important source of market data. Pay surveys can be developed internally or secured externally (either by purchasing existing survey data or by contracting with an outside organization to develop a customized survey).
Market data can also be obtained through:

- Government resources (the Bureau of Labor Statistics—www.bls.gov—is one excellent resource)
- Websites designed for this purpose (for example, go to your favorite search engine and type in "competitive salaries", or similar language)
- Local economic development councils
- Professional associations
- Career development offices at college, universities, and/or tech training schools
- Employees (including departing employees) and managers
- Search firms and employment agencies

**EXAM ALERT**

Be familiar with the advantages and disadvantages associated with each of the different methods of securing market data—in particular, the advantages and disadvantages of survey-based methods.

**Which Matches Are Appropriate?**

As mentioned earlier, matching benchmark positions to available market data provides valuable information. Note that the positions within any organization, however, are benchmark positions. It simply won’t be possible to find market data for some positions, in which case you may want to consider other options (for instance, internal job evaluation or a combination of job slotting with benchmark market data).

**CAUTION**

Match jobs on the basis of the duties and responsibilities that are performed—not on job titles. Job titles can be misleading or even inaccurate, which could in turn corrupt your analysis and recommendations.

**Does the Data Need to Be Adjusted in Any Way?**

There are a number of ways to adjust market data, including:

- **Aging**—Ideally, market data should be collected from multiple sources. It is likely that the dates on which these salaries were “effective” will be different for each source of data, so it’s necessary to adjust all the data to a common date (usually the date on which the market analysis is being conducted).

- **Quality of job match**—Sometimes (perhaps even often), it’s impossible to make a perfect job match, especially for positions that are not benchmark jobs. This can occur because of differences in scope, work conditions, financial responsibility, or a variety of other factors. In situations like this, the best choice you can make is to find the best possible match, even if it is not ideal. After you’ve made the best
possible match, you can then “weight” different market data differently as a way of reflecting each source’s relative value. “Weighting” market data means putting greater importance on certain data you’ve collected, and less importance on other data you’ve collected, when you use that data to perform calculations or formulate recommendations. This can help account for the inevitable imperfections that you’ll come across during the process of job matching.

After the market data has been collected and appropriately adjusted, the recommendations that you’ll make on the basis of that data can support sound decision making. Those recommendations may pertain to one particular position, or they may make a broader contribution toward developing a job-worth hierarchy. It’s also important to recognize that market data does not stand alone as the only factor that should be taken into consideration—ideally, it should be used in conjunction with existing job evaluation methods, pay structures, and so on. It is also quite possible that externally generated data may present a different perspective than internally generated data, and it is important to consider and reconcile the two.

**Compensation: Base Pay and Variable Pay**

After the overall compensation strategy is established, the next step is to determine how that strategy will come to life within the organization. As we discussed earlier, total compensation (rewards) can be divided into direct (cash) and indirect (noncash) elements. In this section, we’ll consider two critical elements of direct compensation: base pay and variable pay.

**Base Pay**

Base pay refers to the fixed rate of pay that an employee receives for performing his or her job. Base pay does not, however, include earnings obtained through shift differentials, benefits, overtime, incentive premiums, or any pay element other than the employee’s fixed rate of pay.

A number of factors go into setting base pay rates, including the relative worth of the job to the organization, the market rate for a particular position, and other special circumstances (for instance, unique skills that are in great demand—also sometimes referred to as “hot skills”).

**Variable Pay**

Sometimes, organizations choose to compensate employees through variable pay programs in addition to base pay programs. Variable pay is also known as “at risk” pay (but is not often referred to in those terms when such pay programs are being discussed directly with employees, in that “risk” is not universally embraced).
There are a variety of variable pay programs, each of which can be used on a standalone basis, combined with other variable pay programs, or customized to meet the needs and objectives of an organization’s own unique compensation and total rewards philosophy.

**Incentive Plans**

Incentive plans establish specific financial and nonfinancial goals and targets for individuals, groups, and organizations. For incentive programs to be effective, employees need to believe that they can attain the goals that have been set as part of the incentive program, and that the reward that they would earn by attaining those goals is “worth it” (see “Vroom’s Expectancy Theory,” in Chapter 2, “HR: A Body of Underlying Knowledge and Principles”).

Incentive plans also need to be designed with an awareness of how much downside risk—as well as upside potential—exists for incentive plan participants. It’s also critical to look at the design of the incentive program and the accompanying message that it sends to employees. For instance

- Are there “thresholds” in place, so that a partial incentive will be paid even if the goal is not fully attained? Or will employees/teams be paid only for meeting or exceeding objectives?
- Is the incentive program an “add on” to a current base pay program, or does it truly constitute earnings that are “at risk”? For instance, will participants’ base pay be reduced, now or at some point in the future, as a result of participating in the incentive program?
- What is the overall degree of upside potential, and what is the overall degree of downside risk?

Regardless of the answers to these and many other questions, one thing is certain—any incentive program will speak volumes to employees about what the organization values.

There are many types of incentive programs, a few of which are described here.

**Short-term Incentives—Individual**

Short-term individual incentive programs are used to financially motivate individual employees to attain specific financial or nonfinancial objectives. Short-term incentive programs are usually one year or less in duration.

**Short-term Incentives—Team/Group**

Short-term team/group incentive programs are similar to short-term individual incentive programs, except that targets are set for groups of people instead of for individual employees. These incentive programs are intended to foster collaborative efforts and synergies among employees who are pursuing a common goal.

**Gainsharing**

Gainsharing incentive plans are designed to motivate (or, you could say, to “incent” or “incentivize”) employees to reach specific goals relating to cost cutting or revenue
generation, by offering to share a portion of that savings (or that increased revenue) with the employees who helped to generate it. Gainsharing plans are based on team/group performance, rather than on individual performance.

**Profit Sharing**

Profit-sharing plans are organizationwide plans that establish an organizationwide profit goal. If the goal is reached, the profits are shared with employees. Profits can either be shared immediately (cash profit sharing plans) or at a later time (deferred profit sharing plans).

### Compensation: Building and Using Pay Structures

After an organization has identified a total rewards philosophy, it can productively turn its attention to building a compensation system to support that philosophy.

The overarching and specific objectives that the organization has established relative to total are brought to life through the organization’s pay structures. Pay structures provide direction relative to wage and salary rates, pay increases, and incentive programs. They operationalize the organization’s philosophies relative to internal equity and external competitiveness. In a very real sense, the pay structures that an organization puts in place make the organization's total rewards strategy tangible.

**EXAM ALERT**

Pay structures provide a reminder about the criticality of effectively communicating with employees about the organization’s total rewards philosophy and programs. Familiarize yourself with ways to engage in meaningful and effective communication with employees around these all-important topics.

### Elements of Pay Structures

Two important elements of pay structures are grades and salaries, both of which are often referred to as elements of a “salary administration” system.

**Grades**

Grades (also referred to as "job grades") represent a hierarchy of levels into which jobs of similar internal worth can be categorized. It may be helpful to liken job grades to school grades—just as students within a particular grade demonstrate similar levels of academic accomplishment, jobs within the same grade share a similar level of value or worth to the organization.

Different organizations will have different numbers of pay grades, with differing degrees of distinction between each of those grades.
Ranges

If grades provide the framework for clustering positions in accordance with their relative value to the organization, ranges provide corresponding compensation levels for each of those clusters.

Ranges specify the lowest (minimum) and the highest (maximum) compensation rates for which positions within each grade are generally paid. The halfway point between those two figures is known as the *midpoint* and is calculated as follows:

\[
\frac{\text{Maximum} + \text{Minimum}}{2}
\]

**NOTE**

As is often the case, exceptions can exist, for a variety of reasons. Employees who are paid above the maximum of the range are considered to be “red-circled”; employees who are paid below the minimum of the range are considered to be “green-circled.”

The *range spread* is a percentage that is calculated by subtracting the minimum of the range from the maximum of the range and dividing that number by the minimum of the range. For instance:

- **Range Minimum:** $40,000
- **Range Maximum:** $60,000
- **Range Spread:**
  \[
  \frac{\text{Range Maximum} - \text{Range Minimum}}{\text{Range Minimum}}
  \]
  \[
  \frac{60,000 - 40,000}{40,000} = 0.5 \text{ or } 50\%
  \]

Range spreads allow organizations to recognize and compensate employees within the same job and within jobs that are in the same grade, for different levels of skill, experience, tenure (if appropriate and consistent with organizational culture) or performance. Of course, how an organization compensates employees within each range will, to a degree, depend on the total rewards philosophy of the organization.

There is no one “right” percentage for range spreads. Range spreads do, however, tend to grow wider at higher grade levels. Traditionally, range spreads are approximately

- 35% for non-exempt positions
- 50% for exempt positions
- 60% + for senior leadership positions

A series of ranges, along with their accompanying minimums, maximums, and midpoints, is known as a *range table*. For identification purposes, numbers or letters are often assigned to each grade in a range table.
Broadbanding

Sometimes, organizations choose to use a relatively small number of grades, an approach known as broadbanding. Organizations might choose to use broadbands to bring about a cultural change (for instance, to support the implementation of a “flatter” organization), or to shift employees’ focus away from traditional promotions and place it instead on professional growth. Broadbands typically have range spreads of 100% or more.

Using Pay Structures for Decision Making

Although it’s important to build pay structures, building them—by itself—isn’t enough. Organizations also need to develop the policies that will guide day-to-day decisions regarding pay. As alluded to earlier, these policies are a reflection of the overarching total rewards philosophies of the organization.

Pay guidelines can be based on performance, experience, seniority, effort, and a variety of other factors. One important consideration to keep in mind is that whatever factor(s) is used to determine how day-to-day pay-related decisions are made will be viewed as having great importance—and will likely become a key driver of employee efforts.

Pay guidelines also need to be developed to guide other types of increases (promotions, adjustments, general increases, cost-of-living increases, and so on) as well as the amount and timing of those increases.

Compa-ratio

Another important tool that can provide valuable information for decision making is the compa-ratio.

The compa-ratio for each employee is calculated by dividing the employee’s pay rate by the range midpoint for his or her position. For example, if an employee earns $40,000 per year, and the midpoint of his or her range is $50,000, the compa-ratio is calculated as follows:

\[
\frac{40,000}{50,000} = 80\%
\]

Compa-ratios can be a particularly valuable measure for organizations that seek to match the market, because in such systems midpoints are often considered to be a close approximation of the “market rate” for a position. By calculating the compa-ratio, therefore, it is possible to compare the employee’s rate of pay with the market rate for his or her position. If you take this percentage in combination with length of service, time in job, performance level, and other employees’ earnings, you’ll end up with a significant amount of information to help you manage employee compensation.
At this point, we’ve covered a lot of ground, including the question of who is (and who is not) an employee; FLSA status; total rewards; and a host of issues relating to compensation. Now let’s move into the other part of the total rewards equation—benefits.

As mentioned at the beginning of the chapter, we’re going to take a slightly different approach to the way we look at benefits-related legislation. Instead of looking at it all together, we’re going to divide benefits-related laws into two categories:

1. Laws that exist for the purpose of regulating, governing, or guiding optional benefits programs
2. Laws that actually created specific mandatory and optional benefits programs

In this way, we hope to make it easier for you to navigate the (relatively) heavily legislated discipline of benefits.

**Related Legislation: Benefits—Laws That Regulate, Govern, and Guide Optional Benefits Programs**

Many laws have an impact on the benefits that employers offer to their employees. Let’s take a look at some of the most significant ones.

**Employee Retirement Income Security Act (ERISA), 1974**

The Employee Retirement Income Security Act is perhaps better known by its acronym, ERISA. ERISA’s overall purpose is to protect the interests of those who participate—and the beneficiaries of those who participate—in employee benefit plans. ERISA applies only to programs established by private industry employers.
ERISA established minimum participation and vesting standards for retirement
programs (ERISA covers defined benefit plans and defined contribution plans; see
“Defined Benefit Plan”). ERISA also established minimum standards for welfare benefit
(including health) plans.

NOTE
It is important to note that the private industry plans that ERISA is designed to regulate are voluntary.
ERISA does not require private industry employers to establish any pension or health plans. It does,
however, impose minimum standards on those employers who choose to do so—all in the interest of
protecting plan participants and their beneficiaries.

A Few Words About Vesting: Cliff and Graded

Vesting is the process by which an employee earns a nonforfeitable right to the employer’s contribution
of his or her defined benefit/defined contribution plan. Organizations can choose between two vesting
options for defined benefits and defined contribution plans: cliff vesting or graded vesting.

In 2002, separate vesting rules were enacted for plans that provided for matching employer contributions,
such as 401(k) plans, as shown in Table 6.1.

| TABLE 6.1 Vesting Schedule for Defined Benefit/Defined Contribution Plans as of 2002 |
|------------------------------------------|------------------|-----------------|
| 401(k) Plans*                           | All Other DB and DC Plans** |
| Cliff Vesting                           | 100% after 3 years| 100% after 5 years |
| Graded Vesting                          | 20% after 2 years | 20% after 3 years |
|                                          | 40% after 3 years | 40% after 4 years |
|                                          | 60% after 4 years | 60% after 5 years |
|                                          | 80% after 5 years | 80% after 6 years |
|                                          | 100% after 6 years| 100% after 7 years |

Participants are always 100% vested in their own contributions.
*Includes other plans with matching contributions.
**Includes plans without employer matching contributions, such as profit-sharing arrangements.

The Protective Nature of ERISA

The safeguards established by ERISA have a strong, but not exclusive, focus on
protecting participants with respect to the financial dimensions of plans. Here are two
examples of requirements established by ERISA that demonstrate this effort to protect
participants:

- Under ERISA, participants must be provided with plan information, specifically about the
  features and funding of the plan—For instance, when an employee (or beneficiary)
  becomes a participant in a retirement plan that is covered under ERISA, he or she
  is entitled to receive a summary plan description (SPD), at no cost, from the plan
  administrator. The SPD describes what the plan provides and how it operates. It
  also provides information relative to when an employee can begin to participate in
  the plan, how service and benefits are calculated, when benefits becomes vested,
when and in what form benefits are paid, and how to file a claim for benefits. In addition to the SPD, the plan administrator must automatically provide participants with a copy of the plan’s summary annual financial report, which includes the same information that employers are required to file with the government on Form 5500.

**EXAM ALERT**

Be aware of ERISA participation rules for defined benefit and defined contribution plans. In general, an employee must be allowed to participate in a qualified plan after meeting the following requirements:

- **The employee is at least 21 years old**—Note that an employee can be excluded for not having reached a minimum age (which cannot exceed age 21) but cannot be excluded for having reached a maximum age. In other words, no matter how old an employee is, he or she can still—and always—participate in the plan.

- **The employee has at least one year of service**—For qualified plans, a year of service is generally 1,000 hours of service performed during the plan year. Employees who do not perform 1,000 hours of service are not considered to have performed one year of service, even if services were performed for a 12-month period. (Note: For plans other than 401(k), this requirement is two years, as long as the plan has fully vested after not more than two years of service.)

An employer may, however, choose to implement less-restrictive eligibility requirements, such as a minimum age requirement that is younger than 21 or a service requirement of less than one year.

- **ERISA provides fiduciary responsibilities for those who manage and control plan assets**—ERISA establishes fiduciary responsibility for “persons or entities who exercise discretionary control or authority over plan management or plan assets, have discretionary authority or responsibility for the administration of a plan, or provide investment advice to a plan for compensation or have any authority or responsibility to do so are subject to fiduciary responsibilities” (www.dol.gov). Plan fiduciaries could include, for example, plan trustees, plan administrators, and members of a plan’s investment committee.

Fiduciaries are charged with running the plan(s) for which they are responsible solely in the interest of participants and beneficiaries. They must ensure that the sole purpose of the plan is—and remains—providing benefits to participants and beneficiaries and paying plan expenses.

Fiduciaries must also act with “skill, care, prudence, and diligence.” For instance, they must protect plan participants by diversifying plan investments (in other words, just like any of us, they can’t keep all of their financial “eggs in one basket”). In addition, they must follow the terms of plan documents to the extent that those terms are consistent with ERISA. They also must avoid conflicts of interest—and, many would argue, even the possibility of an appearance of a conflict of interest (the same standard to which HR professionals should hold themselves, as well).

All of this may sound simple—perhaps as though it should be common sense. Common sense, however, is often somewhat uncommon. All it takes is a quick scan of recent headlines trumpeting the news of unethical behavior and defunct pension...
plans to appreciate the fact that fiduciary responsibility is not something to be taken for granted. According to the Employment Benefits Security Administration (EBSA), ERISA enforcement yielded the following results, as shown in Table 6.2.

<table>
<thead>
<tr>
<th>TABLE 6.2 ERISA Enforcement</th>
<th>FY 2002</th>
<th>FY 2003</th>
<th>FY 2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Prohibited Transactions Corrected</td>
<td>$398M</td>
<td>$460M</td>
<td>$2388.3M</td>
</tr>
<tr>
<td>Plan Assets Restored</td>
<td>$189.7M</td>
<td>$169.8M</td>
<td>$199.7M</td>
</tr>
<tr>
<td>Participant Benefits Restored</td>
<td>$125.3M</td>
<td>$105.4M</td>
<td>$47.8M</td>
</tr>
<tr>
<td>Plan Assets Protected</td>
<td>$168.2M</td>
<td>$662.1M</td>
<td>$141.6M</td>
</tr>
<tr>
<td>Voluntary Fiduciary Correction Program</td>
<td>$1.9M</td>
<td>$8.7M</td>
<td>$264.6M</td>
</tr>
<tr>
<td>Total Monetary Results</td>
<td>$883M</td>
<td>$1.4B</td>
<td>$3042M</td>
</tr>
<tr>
<td>Individuals Indicted</td>
<td>134</td>
<td>137</td>
<td>121</td>
</tr>
</tbody>
</table>

A sample of civil violations included:

- Failing to operate the plan prudently and for the exclusive benefit of participants.
- Using plan assets to benefit certain related parties to the plan, including the plan administrator, the plan sponsor, and parties related to these individuals.
- Failing to properly value plan assets at their current fair market value, or to hold plan assets in trust.
- Failing to follow the terms of the plan (unless inconsistent with ERISA).
- Failing to properly select and monitor service providers.
- Taking adverse action against an individual for exercising his or her rights under the plan (for example, being fired, fined, or otherwise being discriminated against).

**CAUTION**

Plan administrators can be held personally liable for losses that result from breaching their fiduciary responsibility.

**NOTE**

ERISA also requires plans to establish a grievance and appeals process for participants and gives participants the right to sue for benefits and for breaches of fiduciary duty.

**Administrative Responsibility for ERISA**

Administrative responsibility for enforcement of ERISA is divided among three government agencies:

- **IRS**—The IRS focuses on tax-related dimensions of ERISA.
- **DOL**—Within the DOL, ESBA focuses on fiduciary responsibility and transactions that are prohibited by ERISA. Within the DOL, Employee Benefits Security
Administration is responsible for administering and enforcing the fiduciary, reporting, and disclosure provisions of ERISA.

- **Pension Benefit Guaranty Corporation (PBGC)**—The PBGC—a government corporation created by ERISA—functions as an insurer that provides a minimum guaranteed benefit for certain pension plans. PBGC protects participants in most defined benefit plans and cash balance plans (within certain limitations). So, for instance, if a covered plan is terminated, PBGC ensures that participants will receive payment of certain benefits.

PBGC is funded by insurance premiums that are paid by plan sponsors—not by general tax dollars. Funding also comes from investment income, assets from underfunded pension plans it has taken over, and recoveries from companies formerly responsible for those plans.

**EXAM ALERT**

ERISA is highly detailed and complex. If you do not have recent, in-depth, and first-hand experience with the application of ERISA, be sure to dig deeper. Be familiar with the rules under ERISA, the enforcement of ERISA, administrative requirements placed on employers by ERISA, the role of the PBGC, vesting guidelines, and so on.

**Retirement Equity Act (REA), 1984**

The Retirement Equity Act (REA), an amendment to ERISA, incorporated a number of key revisions, many of which addressed the concerns of former (in the event of divorce) and surviving (in the event of death) spouses. Specifically, REA enacted a number of important provisions, seven of which are that the REA

1. Lowered the minimum age requirement for pension plan participation.
2. Increased the years of service that “count” for vesting purposes.
3. Allowed for longer breaks in service (with respect to vesting rules).
4. Prohibited plans from counting maternity and paternity leaves as breaks in service for participation and vesting purposes.
5. Required qualified pension plans to provide automatic survivor benefits and allow for waiver of survivor benefits only with the consent of the participant and the spouse.
6. Clarified that pension plans may obey certain qualified domestic relations (court) orders (QDROs) requiring them to make benefit payments to a participant’s former spouse (or another alternative payee) without violating ERISA’s prohibitions against assignment or alienation of benefits.
7. Expanded the definition of accrued benefits that are protected against reduction.
Consolidated Omnibus Budget Reconciliation Act (COBRA), 1985

The Consolidated Omnibus Budget Reconciliation Act (COBRA) is technically an amendment to Title I of ERISA and is thus administered by EBSA. COBRA requires employers who employed 20 or more people during the prior year to offer continuation of group health care coverage to employees and their family members who experience certain “qualifying events”—events that would have otherwise resulted in the discontinuation of their health insurance benefits.

COBRA places certain requirements on plan participants who want to extend coverage, and it places certain requirements on the plan provider—in particular with respect to notification requirements.

COBRA Qualifying Events

Employees, their spouses, and their dependent children can experience qualifying events that would immediately entitle them to continue group health insurance coverage under COBRA.

NOTE

Those who choose to extend coverage are responsible for paying the full cost of the health premium, plus a 2% administrative fee (if the plan sponsor chooses to charge one).

COBRA Qualifying “Life Events” for Employees

The following table describes the different type of life events that would trigger COBRA coverage, as well as the corresponding length of time that COBRA can be continued for the employee.

COBRA qualifying events for employees are shown in Table 6.3.

<table>
<thead>
<tr>
<th>COBRA Qualifying Event</th>
<th>Length of Continuation Coverage Eligibility</th>
</tr>
</thead>
<tbody>
<tr>
<td>Voluntary or involuntary termination of the covered employee’s employment for any reason other than gross misconduct</td>
<td>18 months</td>
</tr>
<tr>
<td>Reduction in the hours worked by the covered employee</td>
<td>18 months</td>
</tr>
</tbody>
</table>

COBRA Qualifying “Life Events” for Employees’ Spouses

The following table describes the different type of life events that would trigger COBRA coverage, as well as the corresponding length of time that COBRA can be continued for the employee’s spouse.
COBRA qualifying events for employees’ spouses are shown in Table 6.4.

### TABLE 6.4 COBRA Qualifying Events for Employees’ Spouses

<table>
<thead>
<tr>
<th>COBRA Qualifying Event</th>
<th>Length of Continuation Coverage Eligibility</th>
</tr>
</thead>
<tbody>
<tr>
<td>Voluntary or involuntary termination of the covered employee’s employment for any reason other than gross misconduct</td>
<td>18 months</td>
</tr>
<tr>
<td>Reduction in the hours worked by the covered employee</td>
<td>18 months</td>
</tr>
<tr>
<td>Covered employee’s becoming entitled to Medicare</td>
<td>29 months</td>
</tr>
<tr>
<td>Divorce or legal separation of the covered employee</td>
<td>36 months</td>
</tr>
<tr>
<td>Death of the covered employee</td>
<td>36 months</td>
</tr>
</tbody>
</table>

**COBRA Qualifying Events for Employees’ Dependent Children**

The following table describes the different type of life events that would trigger COBRA coverage, as well as the corresponding length of time that COBRA can be continued for the employee’s dependent children.

COBRA qualifying events for employees’ dependent children are shown in Table 6.5.

### TABLE 6.5 COBRA Qualifying Events for Employees’ Dependent Children

<table>
<thead>
<tr>
<th>COBRA Qualifying Event</th>
<th>Length of Continuation Coverage Eligibility</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loss of dependent child status under the plan rules</td>
<td>18 months</td>
</tr>
<tr>
<td>Voluntary or involuntary termination of the covered employee’s employment for any reason other than gross misconduct</td>
<td>18 months</td>
</tr>
<tr>
<td>Reduction in the hours worked by the covered employee</td>
<td>18 months</td>
</tr>
<tr>
<td>Covered employee’s becoming entitled to Medicare</td>
<td>29 months</td>
</tr>
<tr>
<td>Divorce or legal separation of the covered employee</td>
<td>36 months</td>
</tr>
<tr>
<td>Death of the covered employee</td>
<td>36 months</td>
</tr>
</tbody>
</table>

**NOTE**

Extensions of the length of continuation coverage may be available under certain circumstances, such as when a second qualifying event occurs.

**CAUTION**

COBRA is not available to employees, their spouses, or their dependent children when an employee is terminated for gross misconduct.

### Older Worker’s Benefit Protection Act (OWBPA), 1990

The Older Worker’s Benefit Protection Act (OWBPA), passed in 1990, is an amendment to the ADEA that makes it illegal to discriminate against older workers with respect to benefits or to target older workers for layoffs.
Title 2 of OWBPA prohibits individuals from waiving rights or claims under ADEA unless such a waiver is “knowing and voluntary.” OWBPA established nine specific criteria for ensuring that such waivers are knowing and voluntary. One particularly important criterion states that employers must allow employees at least 21 days to consider any right-to-sue waivers that the employer offers in exchange for early retirement benefits.

**Health Insurance Portability and Accountability Act (HIPAA), 1996**

The Health Insurance Portability and Accountability Act (HIPAA) was a more recent amendment to ERISA. HIPAA has two main areas of focus: the security and portability of health care coverage, and privacy considerations.

**Security and Portability of Health Care Coverage**

One of HIPAA’s two key purposes was to help workers experience greater security and portability with respect to health care coverage—even when an employee changes jobs. HIPAA also afforded significantly greater protections for employees who have or who have a family member with a preexisting medical condition.

**NOTE**

Under HIPAA, a preexisting condition is defined as one for which medical advice, diagnosis, care, or treatment was recommended or received during the 6-month period prior to an individual’s enrollment date.

Under HIPAA, in the worst-case scenario, employees (or their family members) with preexisting health conditions can have those conditions excluded from coverage for no more than 12 months (18 months for late enrollees). If an employee maintains health coverage continuously, he or she can reduce or even eliminate this period of exclusion.

HIPAA also prohibited employers from denying certain employees coverage—or from charging them higher premiums—because of preexisting health conditions. HIPAA affords protection to employers, as well, by mandating that health insurance providers must renew coverage for employers (as long as premium payments are made).

**HIPAA Privacy Rule**

HIPAA also addresses the issue of privacy for patients and health-care consumers. Although this rule is not specifically directed at employers, employers who offer group health insurance to employees may be considered a “covered entity” and thus be required to comply with HIPAA’s privacy rule.

The primary purpose of the HIPAA privacy rule is to protect patients and other consumers of health care services from the unauthorized disclosure of any personally identifiable health information (also referred to as protected health information, or PHI).
Health information is considered to be personally identifiable if it relates to a specifically identifiable individual. The following items would generally be considered PHI (whether communicated electronically, on paper, or verbally):

- Health care claims or health care encounter information, such as documentation of doctor’s visits and notes made by physicians and other provider staff
- Health care payment and remittance advice
- Coordination of health care benefits
- Health care claim status
- Enrollment and disenrollment in a health plan
- Eligibility for a health plan
- Health plan premium payments
- Referral certifications and authorization
- First report of injury
- Health claims attachments

If it is determined that an employer is a “covered entity” under the HIPAA privacy rule, the employer would need to take specific actions, some of which would include

- Enact written PHI privacy procedures.
- Designate a privacy officer.
- Require business associates to sign agreements stating that they will respect the confidentiality of PHI.
- Train all employees in HIPAA privacy rule requirements.
- Establish a complaint handling and resolution process for issues related to the HIPAA privacy rule.
- Ensure that PHI is not used for making any employment-related decisions.

EXAM ALERT

Like ERISA and COBRA, HIPAA is a highly complex and involved law. Don’t let the apparent simplicity of the information presented here mislead you; it’s necessary to dig much deeper to truly understand the nuances and subtleties of this law.

CAUTION

Employers should consult with counsel relative to compliance with the HIPAA privacy rule.
Mental Health Parity Act (MHPA), 1996

The Mental Health Parity Act (MHPA) prohibits group health plans providers, insurance companies, and HMOs that offer mental health benefits from setting annual or lifetime dollar limits on mental health benefits that are lower than any such dollar limits for medical and surgical benefits. This means that plans that don’t impose annual or lifetime monetary caps on medical and surgical benefits cannot impose annual or lifetime caps on mental health benefits, either (benefits for substance abuse or chemical dependency are exempted). MHPA is under the jurisdiction of the Departments of Labor, Treasury, and Health and Human Services.

NOTE

MHPA does not require health plans to offer mental health benefits. It only applies to plans that voluntarily choose to offer mental health benefits.

Under MHPA, plans can still dictate/define the terms and conditions of benefits provided under mental health plans (for instance, cost sharing, limits on the number of visits or days of coverage, and so forth).

There are certain circumstances under which plan providers that offer mental health benefits are exempt from MHPA, including

- Small employers who have fewer than 51 employees
- Any group health plan whose costs increase 1% or more because of the application of MHPA’s requirements (the increased cost exemption must be based on actual claims data, not on an increase in insurance premiums)

Sarbanes-Oxley Act (SOX), 2002

The Sarbanes-Oxley Act (SOX) was created in the wake of huge corporate accounting scandals, including Enron and Tyco, to name just two. Designed to protect investors, SOX enacted reforms designed to enhance corporate responsibility and financial disclosures and to combat corporate and accounting fraud. For more information on the Sarbanes-Oxley Act, see Chapter 8, “Risk Management.” There are a number of SOX provisions that HR professionals needs to be particularly concerned with, four of which are

- Prohibition against insider trading during certain pension plan blackout periods—section 306(a).
- Requirement that plan administrators must provide 30-day written notice in advance of blackout periods to individual account plan participants and beneficiaries—section 306(b).
Requirement to disclose whether the company has adopted a code of ethics that applies to the company’s key officers (at a minimum, this code must apply to the company’s principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions)—section 406.

Establishment of whistleblower protection in a wide variety of situations for employees who report fraud against shareholders—section 806(a).

REVIEW BREAK

At this point, we’ve completed a review of the major benefits-related laws that govern—rather than created—voluntary benefits programs. As you continue your review and test preparation, be sure to review other benefits-related laws that are less prominent than these (COBRA, Tax Reform Act, and so on).

Now let’s turn our attention to laws that actually created benefits programs—optional benefits programs, as well as mandatory benefits programs.

Related Legislation: Benefits—Laws That Created Mandatory and Optional Benefits Programs

Some of the laws that we’ll look at created benefits programs that are optional, whereas others created benefits programs that are mandatory.

Worker’s Compensation—Mandatory Benefit Program

Worker’s compensation (also known as “worker’s comp”) laws were adopted at the state level between 1911 and 1940. These laws were designed to provide medical care to injured employees and death benefits to families of those who lost their lives in the performance of their jobs. Worker’s comp is a “no fault” system—injured workers receive medical and/or compensation benefits regardless of who caused the injury or death.

Social Security Act (SSA), 1935—Mandatory Benefit Program

In August of 1935, President Franklin D. Roosevelt signed the Social Security Act into law. Social security is a social insurance program (although some would define it differently) that is funded through payroll taxes. Approximately 96% of all workers are covered under the Social Security Act.
Social security is also known as the Old Age, Survivors, and Disability Insurance program (OASDI), in reference to its three primary components, which are now referred to as retirement income, disability benefits, and survivor’s benefits.

**Retirement Income**

Workers earn credits toward social security benefits. As of 2005, workers earned one credit for each $920 in earnings—up to a maximum of four credits per year. (The amount of money that a worker must make to earn one credit generally increases each year, but the four-credit-per-year maximum remains the same.) Workers born in 1929 or later need 40 credits to earn retirement benefits. Younger people need fewer credits to be eligible for disability benefits or for their family members to be eligible for survivors’ benefits.

Social security tracks each worker’s earnings throughout his or her lifetime. It is the employee’s record of earnings—combined with the age at which he or she retires—that will determine the monetary amount of each worker’s monthly benefit.

**NOTE**

Since the program’s inception, social security has been designed so that employers and the workers they employ contribute equal dollar amounts each pay period (originally 2% of the first $3,000 of the employee’s earnings. That cap, along with that percentage, has been raised significantly over the decades). Independent contractors and self-employed individuals are required to pay both the employer and the employee portions.

**Disability Benefits**

Disability benefits were added to the social security program in 1956. Under social security, workers who become “totally disabled” can receive benefits under social security. Total disability, however, can be a fairly strict standard to meet. Total disability cannot begin until after five full calendar months of continuous disability. Even then, to be considered totally disabled, the worker must be unable to continue in his or her previous job and unable to adjust to other work; in addition, the disability must be expected to last for at least one year or to result in the worker’s death.

In addition to being deemed to have a total disability, the disability eligibility formula requires that the worker has earned a certain number of credits (during his or her entire working life), and that the worker must have earned a certain number of credits within
the 10 years preceding the disability (younger workers who haven't had a chance to earn as many credits are held to more lenient requirements than older workers). Similar to the way in which retirement benefits are calculated, the actual disability benefit that the worker would receive depends on the worker's age and how many credits the worker has earned.

**Survivors’ Benefits**

When a person who has worked and paid social security taxes dies, his or her family members may be eligible to receive survivors’ benefits. Depending on the person's age at the time of death, up to 10 years of work is needed for survivors to be eligible for benefits.

As described at www.ssa.gov/pubs, social security survivors’ benefits can be paid under the following conditions:

- Your widow or widower may be able to receive full benefits at age 65 if born before January 1, 1940. (The age to receive full benefits is gradually increasing to age 67 for widows and widowers born January 2, 1940, or later.) Reduced widow or widower benefits can be received as early as age 60. If your surviving spouse is disabled, benefits can begin as early as age 50.

- Your widow or widower can receive benefits at any age if she or he takes care of your child who is entitled to a child’s benefit and is age 16 or younger or who is disabled.

- Your unmarried children who are under age 18 (or up to age 19 if they are attending elementary or secondary school full-time) also can receive benefits. Your children can get benefits at any age if they were disabled before age 22 and remain disabled. Under certain circumstances, benefits also can be paid to your stepchildren, grandchildren, or adopted children.

- Your dependent parents can receive benefits if they are age 62 or older. (For your parents to qualify as dependents, you would have had to provide at least one-half of their support.)

**Medicare**

Passed in 1965 as an amendment to the Social Security Act, Medicare provides hospital and medical insurance for the elderly and people with disabilities.

There are four parts to Medicare: hospital insurance (sometimes called Part A), medical insurance (sometimes called Part B), Medicare offered through private health insurance companies (Part C), and prescription benefits (sometimes called Part D).

**NOTE**

Neither Part A nor Part B pays for all of a covered person’s medical costs. In addition, the program contains deductibles and copays (payments due from the covered individual).
Medicare—Part A: Hospital Insurance

Part A helps pay for inpatient hospital care, skilled nursing care, and other services.

People age 65 or older are eligible for benefits under Part A of Medicare if they meet any of the following criteria:

- Receive social security or railroad retirement benefits
- Are not getting social security or railroad retirement benefits, but have worked long enough to be eligible for them
- Would be entitled to social security benefits based on a spouse's (or divorced spouse's) work record
- Worked long enough in a federal, state, or local government job to be insured for Medicare

People under age 65 are eligible for Part A Medicare benefits if they experience certain disabilities (for instance, Lou Gehrig's disease, permanent kidney failure, and so on) and meet other specified criteria (for instance, having worked long enough to receive disability benefits under social security).

Medicare Medical Insurance (Also Known as Part B)

Part B helps pay items such as doctor's fees, outpatient hospital visits, and other medical services and supplies.

Almost anyone who is 65 or older or who is under 65 but eligible for hospital insurance can enroll for Medicare medical insurance by paying a monthly premium. People over age 65 don't need any social security or government work credits for this part of Medicare.

Medicare Part C: Medicare Offered Through Private Health Insurance Companies

Part C of Medicare is available to persons who are eligible for Part A and enrolled in Part B. It is a program through which private health insurance companies can contract with the federal government to offer Medicare benefits through their own policies.

Medicare Prescription Benefits (Also Known as Part D)

In December of 2003, the Medicare Prescription Drug, Improvement, and Modernization Act (also known as the Medicare Modernization Act, or MMA) was signed into law. This law, which became effective on January 1, 2006, added prescription drug benefits for all individuals eligible for Medicare Part A and enrolled in Medicare Part B.
Although additional information about this plan is available at www.medicare.gov, be certain to familiarize yourself with (at least) basic information about this important new protection (as provided at www.medicare.gov):

**What is Medicare prescription drug coverage?**
Medicare prescription drug coverage is insurance that covers both brand-name and generic prescription drugs at participating pharmacies in your area. Medicare prescription drug coverage provides protection for people who have very high drug costs or from unexpected prescription drug bills in the future.

**Who can get Medicare prescription drug coverage?**
Everyone with Medicare is eligible for this coverage, regardless of income and resources, health status, or current prescription expenses.

**When can I get Medicare prescription drug coverage?**
You may sign up when you first become eligible for Medicare (three months before the month you turn age 65 until three months after you turn age 65). If you get Medicare due to a disability, you can join from three months before to three months after your 25th month of cash disability payments. If you don’t sign up when you are first eligible, you may pay a penalty. If you didn’t join when you were first eligible, your next opportunity to enroll will be from November 15, 2007 to December 31, 2007.

**How does Medicare prescription drug coverage work?**
Your decision about Medicare prescription drug coverage depends on the kind of health care coverage you have now. There are two ways to get Medicare prescription drug coverage. You can join a Medicare prescription drug plan or you can join a Medicare Advantage Plan or other Medicare Health Plan that offers drug coverage.

Whatever plan you choose, Medicare drug coverage will help you by covering brand-name and generic drugs at pharmacies that are convenient for you.

Like other insurance, if you join, generally you will pay a monthly premium, which varies by plan, and a yearly deductible (between $0–$265 in 2007). You will also pay a part of the cost of your prescriptions, including a payment or coinsurance. Costs will vary depending on which drug plan you choose. Some plans may offer more coverage and additional drugs for a higher monthly premium. If you have limited income and resources, and you qualify for extra help, you may not have to pay a premium or deductible. You can apply or get more information about the extra help by calling Social Security at 1-800-772-1213 (TTY 1–800–325–0778) or visiting www.socialsecurity.gov.

### Unemployment Insurance—*Mandatory Benefit Program*

The Federal-State Unemployment Insurance Program was established as part of the federal Social Security Act of 1935 and is administered at the state level. Federal rules are developed by the DOL.

In general, the maximum period for receiving benefits is 26 weeks, although the federal government may (and sometimes does) choose to extend the benefit period during difficult economic times.
Unemployment insurance is funded through employer taxes (except in three states, where employees contribute as well). Unemployment insurance is intended to help employees financially “bridge” the time between positions, when a position has been lost through no fault of their own.

**Unemployment Insurance—Eligibility**

There are a number of requirements for establishing eligibility, two of which are

- You must meet the state requirements for wages earned or time worked during an established (one year) period of time referred to as a *base period*. (In most states, this is usually the first four out of the last five completed calendar quarters prior to the time when your claim is filed.)
- It must be determined that you were unemployed through no fault of your own (as determined under state law) and meet other eligibility requirements of state law.

Unemployment benefits are subject to federal income taxes.

**Revenue Act, 1978—Optional Benefit Program**

The Revenue Act brought with it many changes, including a reduction in individual income taxes, a reduction in corporate taxes, and so on. It also added two sections to the tax code that essentially resulted in the creation of two new—and ultimately very important—employee benefits.

**Section 125**

Section 125 created flexible benefits plans (often referred to as “cafeteria” plans). Section 125 plans can help employers as well as employees save money by reducing payroll taxes.

Before looking at the three types of Section 125 plans, let’s consider some of the reasons that an organization might have for implementing a section 125 plan.

**Reasons for Considering Section 125 Plans**

Thinking back to where we started in this chapter, recall that each organization’s total compensation program communicates a great deal to employees—and to potential employees—about what the organization values. As such, Section 125 plans might be one way of communicating some of the following messages (to the degree they are appropriate) to employees:

- “We recognize that not everyone’s life is the same, and that everyone has different needs. Because of that, different employees may want to allocate—or spend—the money they earn in different ways.” (Section 125 plans are one way to acknowledge and support these different and changing employee needs.)
- “When it comes to benefits, we may not always know what’s best for you, but you do. In this sense, our goal becomes to give you tools and information with which you can make benefits-related decisions that are right for you.”
“We know you have a choice regarding the company for which you will work. Every day that you choose to remain employed with us, you are casting a vote. We know this, and we appreciate it. Giving you some choice regarding the benefits you select is one way we can say ‘thanks’.”

Types of Cafeteria Plans

There are three types of cafeteria plans:

- **Premium Only Plans (POPs)**—With POPs, the simplest and most transparent (from employees’ perspectives) of the three Section 125 plans, employees pay for their portion of certain insurance premiums (health, dental, and so on) on a pretax basis. The net effect is that each employee’s taxable income is reduced, which is how employers and employees can reduce taxes—and save money.

- **Flexible Spending Accounts (FSAs)**—FSAs take POPs one step further. With FSAs, employees can set aside pretax dollars to pay for medical expenses that are not covered by insurance. FSAs can also be set up for dependent care. Employees decide how much money to set aside for the following year, and that amount is automatically deducted from the employee’s pay on a pretax basis. After incurring and paying for eligible expenses, employees apply for reimbursement from the FSA.

**EXAM ALERT**

FSAs offer distinct advantages as well as potentially distinct disadvantages for employers as well as for employees. Look into the rules governing FSAs before instituting this plan at your organization—and before taking the PHR exam.

- **Full Cafeteria Plans**—Employers who offer full cafeteria plans provide their employees with a specific amount of money they can use to pick and choose from a variety of benefits.

Although they offer distinct advantages, especially for employees, full cafeteria plans are the most administratively burdensome of the three Section 125 options.

**Section 401(k)**

The second employee benefit that was created by the Revenue Act is the 401(k) plan. A type of defined contribution plan, 401(k) plans allow employees to set aside pretax dollars to save for their retirement. This can be done through salary deduction, which may or may not be matched in part or (less frequently) in whole by employer contributions. 401(k) dollars can also be set aside through deferral of profit-sharing income.
Family and Medical Leave Act (FMLA), 1993—Mandatory Benefit Program

The Family and Medical Leave Act (FMLA) (see www.dol.gov) entitles eligible employees (who work for covered employers) up to 12 weeks of unpaid, job-protected leave during any 12-month period for one or more of the following reasons:

- For the birth and care of the newborn child of the employee
- For placement with the employee of a son or daughter for adoption or foster care
- To care for an immediate family member (spouse, child, or parent) with a serious health condition
- To take medical leave when the employee is unable to work because of a serious health condition

Under some circumstances, leave can be taken intermittently.

The FMLA is administered and enforced by the DOL.

Employee Eligibility for FMLA

To be eligible to take FMLA leave, an employee must

- Work for a covered employer (public agencies, state, local, and federal employers, local education agencies [schools], and private-sector employers with 50 or more employees)
- Have worked for the employer for a total of at least 12 months (this time does not have to have been uninterrupted)
- Have worked at least 1,250 hours over the previous 12 months
- Work at a location in the United States or in any territory or possession of the United States where at least 50 employees are employed by the employer within 75 miles
FMLA—Employer Requirements

As described at www.dol.gov, the FMLA places specific requirements upon employers before and during FMLA leaves. Specific requirements pertain to

- Posting requirements
- Notifying employees of their rights under FMLA
- Designating use of leave as FMLA leave
- Maintaining group health benefits
- Restoring an employee to his or her original job, or to an equivalent job with equivalent pay, benefits, and other terms and conditions of employment

According to the DOL, all covered employers are required to display and keep displayed a poster summarizing the major provisions of the FMLA and telling employees how to file a complaint. The poster must be displayed in a conspicuous place where employees and applicants for employment can see it—even if there are no FMLA-eligible employees at a particular location. The following is the DOL-approved poster, as shown in Figure 6.2.

FMLA—Employee Requirements

Employees are also subject to certain requirements under the FMLA:

- 30-day advance notice (when foreseeable and practicable).
- Employers may also require employees to provide the following:
  - Medical certification.
  - Second or third medical opinions (at the employer’s expense) and periodic recertification.
  - Periodic reports during FMLA leave regarding the employee’s status and intent to return to work.
  - For intermittent leaves, employees must try to “work around” the needs of the workplace.

FMLA Specific Terms

There are many terms used in FMLA, the definitions of which need to be carefully reviewed to ensure compliance with the law (and solid preparation for the PHR exam). For instance, be certain that you are familiar with the following terms:

- Job-protected leave
- 12-month period
- Health care provider
- Key employee
- In loco parentis
Your Rights under the Family and Medical Leave Act of 1993

FMLA requires covered employers to provide up to 12 weeks of unpaid, job-protected leave to "eligible" employees for certain family and medical reasons. Employees are eligible if they have worked for their employer for at least one year, and for 1,250 hours over the previous 12 months, and if there are at least 50 employees within 75 miles. The FMLA permits employees to take leave on an intermittent basis or to work a reduced schedule under certain circumstances.

Reasons for Taking Leave:

Unpaid leave must be granted for any of the following reasons:
- to care for the employee's child after birth, or placement for adoption or foster care;
- to care for the employee's spouse, son or daughter, or parent who has a serious health condition; or
- for a serious health condition that makes the employee unable to perform the employee's job.

At the employee's or employer's option, certain kinds of paid leave may be substituted for unpaid leave.

Unlawful Acts by Employers:

FMLA makes it unlawful for any employer to:
- interfere, restrain, or deny the exercise of any right provided under FMLA;
- discharge or discriminate against any person for opposing any practice made unlawful by FMLA or for involvement in any proceeding under or relating to FMLA.

Enforcement:

- The U.S. Department of Labor is authorized to investigate and resolve complaints of violations.
- An eligible employee may bring a civil action against an employer for violations.

FMLA does not affect any Federal or State law prohibiting discrimination, or supersede any State or local law or collective bargaining agreement which provides greater family or medical leave rights.

Job Benefits and Protection:

- For the duration of FMLA leave, the employer must maintain the employee's health coverage under any "group health plan."

For Additional Information:

If you have access to the Internet visit our FMLA website: http://www.dol.gov/esa/whd/fmla. To locate your nearest Wage-Hour Office, telephone our Wage-Hour toll-free information and help line at 1-866-4USWAGE (1-866-487-9243); a customer service representative is available to assist you with referral information from 8am to 5pm in your time zone; or log onto our Home Page at http://www.wagehour.dol.gov.

U.S. Department of Labor
Employment Standards Administration
Wage and Hour Division
Washington, D.C. 20210

*U.S. GOVERNMENT PRINTING OFFICE 2001-476-344/9051

FIGURE 6.2 Family Leave Act of 1993 poster.

As an example of the complexity and the criticality of understanding the language of the FMLA, let's look at one particular term, "serious health condition."
Serious Health Conditions
FMLA defines a serious health condition as

An illness, injury, impairment, or physical or mental condition that involves either:

- Any period of incapacity or treatment connected with inpatient care (that is, an overnight stay) in a hospital, hospice, or residential medical-care facility, and any period of incapacity or subsequent treatment in connection with such inpatient care or

- Continuing treatment by a health care provider, which includes any period of incapacity (that is, inability to work, attend school, or perform other regular daily activities) because of any of the following:

1. A health condition (including treatment therefore, or recovery therefrom) lasting more than three consecutive days, and any subsequent treatment or period of incapacity relating to the same condition, that also includes either of the following:
   - Treatment two or more times by or under the supervision of a health care provider
   - One treatment by a health care provider with a continuing regimen of treatment

2. Pregnancy or prenatal care. A visit to the health care provider is not necessary for each absence.

3. A chronic serious health condition that continues over an extended period of time, requires periodic visits to a health care provider, and may involve occasional episodes of incapacity (for example, asthma, diabetes). A visit to a health care provider is not necessary for each absence.

4. A permanent or long-term condition for which treatment may not be effective (for example, Alzheimer’s, a severe stroke, terminal cancer). Only supervision by a health care provider is required, rather than active treatment.

5. Any absences to receive multiple treatments for restorative surgery or for a condition that would likely result in a period of incapacity of more than three days if not treated (for example, chemotherapy or radiation treatments for cancer).

The paradox of the term “serious health condition” (and so many other FMLA terms) is that, despite the large amount of effort and large number of words dedicated to defining it, in practice its meaning remains somewhat ambiguous. As with all other aspects of the FMLA, HR-related law, and the HR profession in general, a significant amount of analysis (coupled with sound judgment and careful monitoring of relevant court interpretations) is essential.
Uniformed Services Employment and Reemployment Rights Act (USERRA), 1994—Mandatory Benefit Program

The Uniformed Services Employment and Reemployment Rights Act (USERRA) provides reinforcement rights for individuals who miss work because of “service in the uniformed services,” which is defined as voluntary or involuntary uniformed service.

Employers are required to inform their employees of their rights under USERRA. This requirement can be met by displaying the following poster, as shown in Figure 6.3, that clearly outlines employees’ rights and obligations under USERRA.

NOTE

Be aware of special USERRA rules that apply for returning reservists. Specifically, according to a 2002 DOL News Release:

National Guard and reservists returning to civilian occupations after serving in support of President Bush’s post-Sept. 11 national emergency declaration should have their active duty time counted toward their eligibility to take time off from work under the Family and Medical Leave Act (FMLA).

The Department of Labor has issued a memorandum that clarifies its position on the rights of returning uniformed service members to family and medical leave under the Uniformed Services Employment and Reemployment Rights Act. USERRA entitles returning service members to all the benefits of employment that they would have obtained if they had been continuously employed.

Under ordinary circumstances, a worker becomes eligible for leave under the FMLA after working for a covered employer for at least 12 months, during which he or she completed at least 1,250 hours of work. The memorandum says that employers should count the months and hours that reservists or National Guards would have worked if they had not been called up for military service toward FMLA eligibility.

REVIEW BREAK

We’ve looked at laws—those that guide and regulate as well as those that create certain benefits. Now let’s take a look at specific types of optional, or voluntary, benefits (which therefore, by definition, are not government mandated).
Optional Benefits Programs

Let’s now take a look at some of the different types of benefits programs organizations offer that are voluntary.
Retirement Plans

By definition, retirement plans “defer” income—and therefore defer the tax that must be paid on that money until it actually becomes income, which occurs at the time of distribution. Following are some examples of specific retirement plans.

Defined Benefit Plan

Defined benefit plans represent a more traditional type of pension plan, in which the employer shoulders the balance of the risk. This risk stems from the non-negotiable fact that defined benefit plans promise to pay the employee a specified monthly benefit at retirement. This “specified monthly benefit” could be expressed as an actual dollar amount, or it could be calculated through some sort of formula (this is the more common method). Either way, the PBGC protects participants in defined benefit plans by ensuring that, within certain limitations, the promised benefits will be paid.

Defined Contribution Plan

Unlike defined benefit plans, defined contribution plans do not “promise” a specific monthly benefit (or total benefit) at retirement. Instead, the employer and/or the employee contribute to the employee’s individual retirement savings account. Those
contributions are then invested—investments that can either make money or lose money. In this way, defined contribution plans shift the risk away from the employer (which is where it rests for defined benefit plans) and back to the employee.

**NOTE**

This “shift” may account for part of the reason why defined contribution plans are increasing in popularity, while defined benefit plans are decreasing in popularity (keep in mind that neither of these is legally mandated).

At the “end of the day” (meaning, at the time of retirement), what’s there is there. No promises have been made, therefore no promises about total payouts can be broken. (This does not, of course, mean that the ERISA guidelines of fiduciary responsibility are waived—they absolutely apply to defined benefit plans as well as to defined contribution plans.)

**NOTE**

Defined contribution plans tend to be more advantageous to shorter-term employees.

Examples of defined contribution plans include 401(k) plans, employee stock ownership plans, and profit-sharing plans.

**Employee Stock Ownership Plan (ESOP)**

An employee stock ownership plan (ESOP) is a type of defined contribution plan in which investments to individual accounts are made primarily in the form of employer stock. ESOPs offer certain tax advantages to employers, as well as to employees.

**Profit Sharing Plan**

A profit sharing plan is a type of defined contribution plan under which the organization makes contributions to its employees’ accounts. These contributions often come from profits, and thus also serve as an incentive to performance.

**Simplified Employee Pension Plan (SEP)**

A simplified employee pension plan (SEP) allows employers to make contributions on a tax-favored basis to individual retirement accounts (IRAs) that employees set up for this purpose.

**Health and Welfare Benefits**

Organizations can choose from a wide array of health and welfare benefits, a few of which are explored here.

**Medical Insurance**

Employers and employees can choose from several types of medical insurance plans.
Indemnity Insurance

The most traditional type of medical insurance plan, indemnity plans provide participants with (virtually) unrestricted choices relative to their doctors, hospitals, and other health care providers. Health care providers are paid a fee for the services they actually provide and perform. Hence, the more services that are provided, the greater the fees that will be paid. This is one reason why indemnity plans are usually one of the most expensive type of medical insurance programs from which employers and employees can choose.

Health Maintenance Organizations (HMOs)

Health maintenance organizations, or HMOs, offer a very different model of health care—one that is referred to as “managed care.” One significant difference between HMOs and indemnity plans centers around “choice.” While participant “choices” are nearly unlimited in indemnity plans, participant choices are more closely managed (and many would argue more limited) with HMOs.

For instance, with indemnity plans, participants make choices relative to which doctors they will go to and how often they will go. In an HMO, each participant chooses a primary care physician, or PCP, who serves as a “gatekeeper.” Participants must see their PCPs first, and the PCP then decides whether to refer the patient to a specialist or for additional tests.

In this sense, HMOs truly do “manage” participants’ health care experiences. There are advantages and disadvantages to this approach. Some would argue that HMOs are beneficial in that they emphasize preventive care and control health care costs. And because participants can change their PCP, there is still a critical element of choice inherent to the plan. In addition, HMOs provide a full range of health care, including doctor’s visits, specialist services, hospitalization, surgical services, and so on.

Others would argue that HMOs are overly restrictive. With an HMO, a referral from a primary care physician is required before a participant can see a specialist or get any tests done. In addition to being administratively burdensome (and, at times, inconvenient), some would argue that this disempowers participants relative to their own personal health care choices.

Another concern relative to HMOs centers around capitation, the basis on which doctors are paid. What this means, essentially, is that each PCP is paid each month for every person who chooses that doctor to be his or her PCP—not for the actual amount of care that is provided. In short, providing more care won’t generate more revenue—in fact, it dilutes the physician’s earnings (not in terms of actual dollars, but in the sense that the physician gets paid the same amount of money for doing “more work”). Some individuals do not feel this is problematic, whereas others believe it incents physicians to provide patients with fewer services, or to spend less time with each patient.

Preferred Provider Organizations (PPOs)

A preferred provider organization (PPO) is a managed care health insurance plan that offers a network of health care providers who band together to offer services at a
discounted rate to plan participants. PPOs resemble indemnity plans, in that network providers are paid when they render services and plan participants can choose which doctors they want to visit and when they want to visit them. Plan participants can also choose to avail themselves of doctors or other health care providers who are outside the network; however, the costs to the member will be higher than they would have been if the member had chosen a doctor within the network.

**Point of Service (POS)**

Point of service (POS) plans are a combination of the HMO and PPO managed care models. Like the PPO model, there is a network of physicians and health care providers who have agreed to provide services at a discounted rate. Like the HMO model, there is a gatekeeper—a primary care physician who must provide plan members with referrals to specialists and for other services. Unlike the HMO model, however, referrals can be made to physicians who are either inside or outside the network. Although out-of-network referrals will cost participants more, they are permissible.

**Dental Insurance**

Like medical insurance, dental insurance can be offered through an indemnity program, an HMO network, or a PPO network. There are also some specific categories of coverage within dental plans, each of which is likely to offer a different level of reimbursement.

**Preventive Care**

"An ounce of prevention is worth a pound of cure"—that adage is perhaps no more apparent than in dental care (with, of course, the possible exception of performance management—see Chapter 5). Preventive care includes such things as regular dental checkups, exams, cleanings, and sometimes X-rays. It is often reimbursed at 100% of cost (or at 100% of reasonable and customary (R&C) expenses), so as to encourage plan members to take advantage of measures that encourage good oral health and that potentially decrease long-term costs.

**Restorative Care**

Restorative care, as its name implies, refers to oral “repairs” that are usually of a relatively minor nature, such as cavities or root canals. The reimbursement for restorative care is generally less than the reimbursement rate for preventive care (perhaps 80% instead of 100%).

**Major Restorative Care**

For those readers who are thinking, “You think a root canal is minor?” please understand that “minor” is a relative term that is used to describe the degree of restoration that is required, not necessarily the degree of discomfort that is experienced. By comparison, major restorative care—which would be reimbursed at an even lower rate (perhaps 50%)—refers to things such as bridgework and crowns.
Orthodonture
Orthodonture—braces, headgear, retainers, and the like—is a benefit that is often reimbursed at 50%. Unlike the other types of dental insurance discussed previously, orthodonture is often subject to a lifetime cap—perhaps in the vicinity of $1,000–$1,500. Plan members who have multiple children (dependents under the age of 19) with multiple orthodontic challenges might find that they can burn through this benefit relatively quickly. It still, however, represents a significant savings over full-cost orthodonture and may be highly valued by that segment of your employee population with children to raise, palates to spread, and teeth to straighten.

Vision Coverage
Vision coverage is a little different from the other health and welfare benefits we’ve looked at so far. Unlike those other plans, an employer will typically offer vision coverage as a discount program (generally around 10%). Vision coverage generally includes items such as exams, contact lenses, and glasses.

Prescription Drug Coverage
As the cost of prescription drugs rises, prescription drug coverage is becoming an even more highly valued employee benefit. Some employers provide prescription drug coverage as part of their medical plan, whereas others provide this coverage under a separate plan. Plan members may be required to pay a copay, to purchase their prescriptions at certain pharmacies, to use generic drugs (when available), or to use mail-order services for maintenance drugs (prescriptions that are prescribed for chronic, or longer-term conditions, and that are taken on a regular, recurring basis). Even with these restrictions, prescription drug coverage can be a huge benefit to employees.

Life Insurance
Term life insurance is also considered to be a valuable benefit by many employees, as a way of ensuring that they can provide their beneficiaries and loved ones with income in the event of their deaths. Many employers offer a certain amount of life insurance at no cost to employees and offer optional supplemental life insurance, as well.

Long Term Disability Insurance
Long term disability (LTD) insurance replaces a designated percentage of an employee’s income that is lost through illness or injury.

EXAM ALERT
In addition to being familiar with different types of health and welfare plans, be sure to familiarize yourself with various funding options for those plans, such as fully insured plans, partially insured plans, administrative services only (ASO) plans, third-party administrator (TPA) plans, and self-insured plans. It’s equally important to be familiar with cost-shifting and cost-containment strategies and options.
Pay for Time Not Worked

As its name implies, *pay for time not worked* refers to situations in which employees receive compensation for sick days, vacation days, jury duty, personal time, designated holidays, floating holidays, bereavement leave, and the like.

NOTE

Pay for time not worked is a benefit that is highly valued by many employees, overused by some, and underused by others. “Free time” for employees, however, isn’t free of charge to the organization. From the organization’s perspective, pay for time not worked needs to be costed out just like any other benefit.

Work-Life Programs

The same can be said for work-life (“balance”) programs. Programs such as flexible schedules, job sharing, telecommuting, and compressed work weeks can be a great advantage for employees, and a great way for employers to market themselves in the relevant labor market, as well. Still, don’t institute any program without first conducting careful analysis and assessment (see “ADDIE: An Overview,” in Chapter 5). Initiatives have to make business sense, and—ideally—should be sustainable for the foreseeable future. For although there are never any guarantees, it’s not advisable to implement a program that might need to be revoked in the near time. When this happens, legitimate efforts at enhancing the workplace experience for employees can really backfire.
Chapter Summary

Compensation, benefits, and the synergies created by the combination of those two disciplines are both technically challenging and strategically impactful. Knowledge and insight in both of those areas is critical.

The specific areas we’ve looked at are

- Total Rewards Footing #1: Employee or independent contractor?
- Total Rewards Footing #2: Exempt or non-exempt?
- Total Rewards Footing #3: Compensation + Benefits = Total Compensation
- Related Legislation: Compensation
- Compensation: Job evaluation
- Compensation: Market pricing
- Compensation: Base pay and variable pay
- Compensation: Building and using pay structures
- Related Legislation—Benefits: Laws that regulate, govern, and guide optional benefits programs
- Related Legislation—Benefits: Laws that created mandatory and optional benefits programs
- Optional benefits programs

HR professionals can increase their value to the organization by enhancing their knowledge and skills in these areas—even if such knowledge and skills do not immediately appear to be relevant to our current “primary functions.” In addition, this constitutes a crucial portion of the PHR exam. For that reason, start by learning what is included in this chapter, and then go beyond. The value that will accrue to you, and to your organization, is unquestionably worthwhile.

Key Terms

- Total rewards
- Total compensation
- Compensation
- Benefits
- Employee
- Independent contractor
- Exempt
- Non-exempt
- Fair Labor Standards Act (FLSA)
- Minimum wage
- Overtime
- FairPay
- Salary
- Primary duty
- Executive exemption
- Administrative exemption
- Learned professional exemption
- Creative professional exemption
Computer employee exemption
Outside sales exemption
Highly compensated employee
Safe harbor provisions
Total compensation
Relevant labor market
Lead the market
Lag the market
Match the market
Direct compensation
Indirect compensation
Davis-Bacon Act, 1931
Walsh-Healey Public Contracts Act, 1936
Fair Labor Standards Act, 1938
Workweek
Hours worked
Regular rate of pay
Child Labor
Portal to Portal Act, 1947
Equal Pay Act, 1963
Skill
Effort
Responsibility
Working conditions
Affirmative defenses
Job evaluation
Nonquantitative job evaluation techniques
Whole job ranking
Job classification
Job slotting
Quantitative job evaluation techniques
Point factor
Factor comparison
Market pricing
Market data
Labor market competitors
Job match
Aging
Base pay
Variable pay
Incentive plans
Short-term incentives—individual
Short-term incentives—team/group
Gainsharing
Profit sharing
Pay structures
Grades
Ranges
Range spread
Broadbanding
Compa-ratio
Employee Retirement Income Security Act (ERISA), 1974
Vesting
Cliff vesting
Graded vesting
Plan administrator
Summary plan description
Fiduciary
Fiduciary responsibility
Pension Benefit Guaranty Corporation (PBGC)
Retirement Equity Act, 1984
Qualified Domestic Relations Order (QDRO)
Consolidated Omnibus Budget Reconciliation Act (COBRA), 1985
- COBRA qualifying event
- Older Worker's Benefit Protection Act (OWBPA), 1990
- Health Insurance Portability and Accountability Act (HIPAA), 1996
- Preexisting condition
- HIPAA privacy rule
- HIPAA covered entity
- Mental Health Parity Act (MHPA), 1996
- Sarbanes-Oxley Act (SOX), 2002
- Worker’s Compensation
- Social Security Act (SSA), 1935
- Old Age, Survivors, and Disability Insurance (OASDI)
- Retirement benefits
- Disability benefits
- Survivor’s benefits
- Medicare
- Medicare—Part A
- Medicare—Part B
- Medicare—Part C
- Medicare—Part D
- Unemployment insurance
- Revenue Act, 1978
- Section 125
- Flexible benefits
- Cafeteria plans
- Premium-only plans (POPs)
- Flexible spending accounts (FSAs)
- Full cafeteria plan
- Section 401(k)
- Family and Medical Leave Act (FMLA), 1993
- Job protected leave
- 12-month period
- Health care provider
- Key employee
- In loco parentis
- Serious health condition
- Uniformed Services Employment and Reemployment Rights Act (USERRA), 1994
- Defined benefit plan
- Cash balance plan
- Defined contribution plan
- Employee stock ownership plans (ESOPs)
- Profit sharing plans
- Simplified employee pension plan (SEP)
- Health and welfare benefits
- Medical insurance
- Indemnity insurance
- Health maintenance organization (HMO)
- Primary care physician (PCP)
- Preferred provider organization (PPO)
- Point of service (POS)
- Dental insurance
- Preventive care
- Restorative care
- Major restorative care
- Orthodonture
- Vision coverage
- Prescription drug coverage
- Life insurance
- Long term disability insurance (LTD)
- Pay for time not worked
- Work life programs

Chapter Summary
Apply Your Knowledge

This chapter focuses on issues relating to total rewards. Complete the following exercises, review questions, and exam questions as a way of reviewing and reinforcing the knowledge and skills you’ll need to perform your responsibilities as an HR professional, and to increase the likelihood that you will pass the PHR examination.

Exercises

1. You’ve recently been promoted to a position as an HR generalist, and you’re anxious to get to work. One day, a manager who you haven’t worked with before comes to you to talk about a problem he’s having with one of his direct reports. This direct report happens to be an executive assistant and is a highly trusted and valued member of the department. He handles sensitive information and is always looking to grow and to learn new things. The employee feels, however, that he has been “held back” because he’s classified as non-exempt, and therefore can’t join in with the team on special projects that require overtime or weekend work (there is no money in the budget for overtime hours). This employee ends up feeling excluded and less important. The manager wants you to help him find a way to reclassify the position as exempt. Which of the following answers would be the least appropriate?

A. Coach the manager on how to help the employee understand that he truly is a valued member of the team.

B. Change the employee’s title to “Assistant Manager” and then upgrade the position to exempt.

C. Evaluate the position to see how it has changed since the last review, and determine whether it should be upgraded.

D. Coach the manager on how to have a conversation with the employee about his career objectives.
2. You work as the sole HR professional in a relatively small organization. Recently, the company conducted its first employee survey, and the results indicated that employees don’t understand how the company sets its pay rates—in other words, they don’t know why they are paid what they are paid. The company president, who happened to recently read an article during a cross-country flight about “total rewards philosophy,” has asked you to draft one. He wants it “fast, good, and cheap.” You know that no one source of information alone will give you everything that you need, but you’ve got to start somewhere. Which of the following do you think would be of greatest initial value to you as you put together this document?

A. A sample “total rewards philosophy” statement from a reputable HR-related website.
B. A “total rewards philosophy” statement from a local company that is well-known for being an employer of choice.
C. Your organization’s mission, vision, and values statement, along with your organization’s employee handbook.
D. A brochure from a consulting firm that specializes in communicating with employees about compensation-related issues.

3. A manager who you know fairly well, and with whom you have a good working relationship, leaves a voice mail message for you, asking you to please call her back about a benefits question. You return her call, and she comes down to your office to speak with you in person. She explains that her former assistant, who left nearly a year and a half ago to go back to college, is about to run out of COBRA. She explains to you that he still is one semester away from earning his degree and can’t get decent health insurance through the college plan. She asks if you could leave him on COBRA, just for a few more months. As part of your overall response to this manager, which of the following would be the most appropriate to share?

A. Under COBRA, former employees who are full-time students at the time that COBRA runs out are entitled to an extension for up to 18 additional months if he or she remains a full-time student.
B. Although COBRA requires an employer to continue benefits coverage for only 18 months, the employer has the option to extend COBRA benefits for an additional 18 months.
C. COBRA can be continued for another 18 months, as long as the employee pays the company 110% of the monthly premium costs.
D. COBRA cannot be continued beyond 18 months in this particular situation, but other situations would warrant an extension, and you would be happy to share that information with her.
4. You’re the HR manager at your organization and report directly to the president. (You happen to know that his sister died of cancer about six months ago.) One afternoon, an employee comes to you with a problem. Her sister (who lives out of state) has been diagnosed with a very aggressive form of cancer and has less than six months to live. The employee wants to spend the last few months of her sister’s life with her. The employee has already requested a leave of absence, but was advised by an HR representative and her manager that this sort of leave isn’t covered under FMLA. Your department is going into its “busy season,” so her manager is unwilling to grant any other type of leave. She is concerned about how she will support herself while she is staying with her sister. She asks you whether it would be possible for the company to call this a layoff and let her get unemployment insurance. Sadly, she knows that her sister won’t live longer than six months, so unemployment insurance benefits would carry her through. After you express your sincere concern for her sister’s condition, which of the following answers would be best?

A. Tell the employee that it’s up to the state, not the company, whether unemployment insurance will be granted, and that, although you do sympathize with her situation on a personal level, it’s not possible for you to code the termination as a layoff.

B. Tell the employee that it’s up to the state, not the company, whether unemployment insurance will be granted. However, as long as the president approves (and you’re pretty sure he will), you’re willing to code the termination as a layoff.

C. As HR, your role is that of employee advocate, and you are willing to advocate on her behalf to the president. You are fairly confident that he will approve this request, and will get back to the employee either way as soon as possible.

D. You remind the employee, as gently as possible, that, as HR, your role is to ensure that all of the company’s policies and procedures are followed, and falsifying the termination code would be a violation of policy. As such, you can’t code the termination as a layoff.

5. As the HR manager, you’ve been looking for creative ways to provide employees with greater benefits without incurring significant additional costs. Your company already has a POP in place. Which of the following would you be most likely to recommend?

A. FSAs
B. PCAs
C. ESOPs
D. PNGs
Review Questions

1. Describe the similarities and differences between defined benefit plans and defined contribution plans.

2. Why is it important to communicate with employees about their compensation and benefits (“total rewards”) programs?

3. Define what is meant by “total rewards” and “total rewards philosophy.”

4. What is meant by the term “internal equity”? 

5. What is meant by the term “relevant labor market”? 

Exam Questions

1. Which of the following statements about workweeks is not true?
   A. A workweek is any fixed and regularly recurring period of 168 hours.
   B. The employer can select any day (and any hour) of the calendar week on which to begin the workweek.
   C. The employer can establish different workweeks for different employees or groups of employees.
   D. The hours that an employee works during different workweeks within the same pay period can be “averaged.”

2. Which of the following would not be considered an affirmative defense under the Equal Pay Act?
   A. Seniority
   B. Diversity
   C. Quality of production
   D. Merit

3. Which of the following statements about the point factor method of job evaluation is true?
   A. Point factor systems do not establish levels of performance within each compensable factor, because that would constitute making the error of evaluating the person instead of the position.
   B. There is a greater likelihood of rater subjectivity with point factor methods of job evaluation than with whole job methods because point factor systems require the evaluator to make more judgments.
   C. The product of a completed job evaluation will generate information that will be helpful to establishing a job worth hierarchy.
   D. Although point factor systems address evaluative information about different compensable factors, they do not address the relative importance of each compensable factor.
4. Which of the following could generate a calculation that represents “range spread”?

A. \[
\frac{\$55,000}{\$61,000} = 90.1\%
\]

B. \[
\frac{\$80,000 - \$50,000}{\$50,000} = \frac{\$30,000}{\$50,000} = 60\%
\]

C. \[
\$100,000 - \$40,000 = \$60,000
\]

D. None of the above

5. Which of the following was established by ERISA?

A. Enhanced protection for plan members with preexisting medical condition.

B. A clearer definition of “hours worked” for purposes of minimum wage and overtime payments.

C. Whistleblower protection for employees who report fraud against shareholders.

D. Minimum participation and vesting standards for retirement programs.

6. Fiduciaries must do all of the follow except

A. Protect plan participants by diversifying plan investments.

B. Act with skill, care, prudence, and diligence.

C. Avoid conflicts of interest.

D. Follow the terms of plan documents without deviation.

7. Which of the following did the REA not accomplish?

A. Lowered the minimum age requirement for pension plan participation and increased the years of service that count for vesting purposes

B. Prohibited plans from counting maternity and paternity leaves as breaks in service for participation and vesting purposes

C. Required qualified pension plans to provide automatic survivor benefits that could be waived only with the written consent of the plan participant

D. Clarified that pension plans may obey certain qualified domestic relations (court) orders (QDROs) without violating ERISA
8. PHI refers to
   A. Health information that relates to a specific individual
   B. A managed care health option offered to federal and state government employees
   C. Information that was used as part of the “long form” test under the old provisions of the FLSA
   D. Information that must be maintained in according with the record-keeping requirements of the FLSA

9. Which of the following is not one of the three main provisions of the Social Security Act?
   A. Retirement income
   B. Pension protection
   C. Survivor’s benefits
   D. Disability benefits

10. Which of the following is not required of covered entities by the HIPAA privacy rule?
    A. Designation of a privacy officer
    B. Creation of a code of ethics that applies to all employees who have access to health-related information
    C. Establishment of a complaint-handling and resolution process for issues related to the HIPAA privacy rule
    D. Agreements signed by business associates stating that they will respect the confidentiality of patient information

Answers to Exercises

1. **Answer B is the best answer.** First, reclassifying a position from “non-exempt” to “exempt” is a decision that must be made after much analysis—analysis that is grounded in actual job responsibilities, rather than because of a particular incumbent (or a particular incumbent’s feelings). Also, FLSA status is determined on the basis of the responsibilities that are performed, not on the basis of job title. Finally, it is best to refer to this process as “reclassifying,” not “upgrading,” in that the word “upgrading” seems to reinforce the fallacy that it is better or more desirable to be exempt than it is to be non-exempt. Answer A is not the best answer; it would be appropriate for the manager to help the employee understand how he contributes to, and is valued by, the team. Answer C is not the best answer; it is possible that the position might have changed enough to warrant a reclassification, and a job evaluation would provide information that is necessary for making that assessment. Answer D is not the best answer; this might be an appropriate opportunity for a manager to have a discussion with the employee about his career objectives.
2. **Answer C is the best answer.** The first, and best, source of information that you can have when communicating with employees about total rewards is any resource (written, or otherwise) that expresses, reflects, and articulates the mission, vision and/or values of your own organization. This is the best way to be sure that your total rewards philosophy truly aligns with, and will therefore help fulfill, your organization’s “reason for being.” Although other items are important, if you don’t capture the true essence of your own organization (and why it exists in the first place), any statement of total rewards philosophy that you draft will likely ring hollow, and have limited effectiveness. Answer A is not the best answer; although it may be useful to review (and perhaps even be inspired by) a sample total rewards statement from a reputable HR-related website, “vanilla” statements aren’t as valuable to you in this process as information about your own organization. Answer B is not the best answer; a total rewards philosophy that works brilliantly for one organization (no matter how successful that organization might be) may be completely inappropriate and/or ineffective for a different organization. Answer D is not the best answer; outside consultants may be able to develop a “good” statement “fast,” but “cheap” might be a bit unrealistic. Give this a try on your own first—your organization will appreciate your efforts as well as your budget-sensitive approach.

3. **Answer D is the best answer.** It is true that, according to the facts you have been given, COBRA can’t be extended; however, it’s also true that there may be other facts of which you’re not aware. Be helpful, and also be factual and accurate. Answer A is not the best answer; there is no provision under COBRA that states that an extension beyond 18 months is available for former employees who are full-time students. Answer B is not the best answer; COBRA does not allow employers to continue benefits coverage beyond legally specified time frames. Answer C is not the best answer; COBRA allows for participation to continue for up to another 18 months only under specific circumstances (and those circumstances cannot be “bought” with a 10% surcharge).

4. **Answer A is the best answer.** First, it is important for the employee to understand how the process works, so it is appropriate to share that information with her. No matter how much empathy you feel for her, however, and regardless of any other personal circumstances that might be “pulling at your heart strings,” there are many reasons (ethical, legal, procedural, financial, and so on) why you would not falsify a termination code. You don’t, however, need to go into all those reasons with the employee (although you might want to consider following up with the manager to see if you can come up with any creative solutions). Answer B is not the best answer; although the factual information at the beginning of this answer is correct, there are many reasons (ethical, legal, procedural, financial, and so on) why you should not falsify the termination code. Answer C is not the best answer; as HR, your role is to be a “truth advocate,” not just an employee advocate (and the truth, in this case, is that the employee wasn’t laid off). Answer D is not the best answer; prattling on about policies and procedures at this moment (and at most moments) isn’t the best approach and might only serve to reinforce the notion of HR as the “personnel police.”
5. **Answer A is the best answer.** Like a POP (Premium Only Plan), an FSA (flexible spending account) falls under Section 125. An FSA goes one step further than a POP by allowing employees to set aside pretax dollars to pay for medical expenses that are not covered by insurance. This lowers the employee's taxable income, which benefits the employer as well as the employee. Answer B is not the best answer; PCA refers to the Walsh-Healey Public Contracts Act (PCA), which was passed in 1936. Answer C is not the best answer; an ESOP (employee stock ownership plan) involves the distribution of stock and is much more complex than establishing FSAs. Creating an ESOP has many implications and would not constitute an appropriate solution for a problem such as this. Answer D is not the best answer; PNG is not a commonly known acronym in HR.

**Answers to Review Questions**

1. Some of the differences and similarities between defined benefit and defined contribution plans are summarized in Table 6.6.

### TABLE 6.6 Defined Benefit Plans and Defined Contribution Plans Comparison

<table>
<thead>
<tr>
<th></th>
<th>DB Plans</th>
<th>DC Plans</th>
</tr>
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<tbody>
<tr>
<td>Nature of the plan</td>
<td>More traditional type of pension plan</td>
<td>Less traditional type of pension plan</td>
</tr>
<tr>
<td>More risk is shouldered</td>
<td>The employer</td>
<td>The employee</td>
</tr>
<tr>
<td>What will the plan pay</td>
<td>Promises to pay a specified monthly benefit at</td>
<td>Makes no guarantees about the value of the</td>
</tr>
<tr>
<td>out to the employee?</td>
<td>retirement</td>
<td>plan as of the time of retirement</td>
</tr>
</tbody>
</table>

2. It is important for organizations to communicate with employees about their total rewards programs with respect to each element of each program and to the program as a whole. First, employees may not truly understand all the benefits that they enjoy as employees of an organization. This leads to a second reason why communicating with employees about total rewards is important—most employees do not know the real costs, let alone the actual value, of the benefits they receive (this holds true for mandatory as well as optional benefits). In a very real sense, employees earn benefits, just like they earn cash compensation, and they should know what they are earning. Without this measure of communication, it is more likely that even those benefits that are not entitlements may ultimately begin to feel like entitlements to employees, rather than something of value that they have earned in return for their services to the organization.

3. The term “total rewards” refers to all the compensation- and benefits-related elements that employees within an organization earn and enjoy in return for the services they have provided to their employer. An organization’s total rewards philosophy, however, represents far more than just the amount of cash it pays to employees or even the “fringe benefits” that it provides. Instead, it speaks volumes
about what the leaders of that organization value, the results they want to attain, the behavior they want to encourage, and their commitment to their employees. It is a clear and direct expression of the organization’s mission, vision, and values—regardless of whether that was the organization’s intention. Even the absence of a clearly defined total rewards or compensation system or philosophy sends a very clear message, so be certain that it is the message that your organization truly intends to convey.

4. “Internal equity” refers to fairness (or “equity”) within a department and/or organization with respect to the ways in which jobs are ranked and individuals are compensated.

5. The relevant labor market relates to the size and scope of the geographic area within which an organization would seek to attract qualified candidates. Even within the same organization, the relevant labor market for different positions can vary widely depending on the skills, knowledge, abilities, and behavioral characteristics required to perform each position successfully. Other factors that impact how an organization defines the relevant labor market might be the degree of competition that exists among employers for particular skills and/or knowledge, and/or the degree to which certain skills and/or knowledge requirements are industry specific.

Answers to Exam Questions

1. Answer D is the best answer. The hours that an employee works during different workweeks cannot be averaged, even when those weeks are during the same pay period. Answer A is not the best answer; a workweek is any fixed and regularly recurring period of 168 hours. Answer B is not the best answer; the employer can select any day (and any hour) of the calendar week on which to begin the workweek. Answer C is not the best answer; the employer can establish different workweeks for different employees or groups of employees.

2. Answer B is the best answer. Diversity has not designated as an affirmative defense under the Equal Pay Act. Answer A is not the best answer; seniority would be considered an affirmative defense under the Equal Pay Act. Answer C is not the best answer; quality of production would be considered an affirmative defense under the Equal Pay Act. Answer D is not the best answer; merit would be considered an affirmative defense under the Equal Pay Act.

3. Answer C is the best answer. The information that is generated through the job evaluation process will provide information that is helpful to establishing a job worth hierarchy. Answer A is not the best answer, because point factor systems do establish levels of performance within each compensable factor. (As long as evaluations are conducted relative to the performance expected of the position rather than on the basis of the incumbent’s individual performance, the job evaluation will still be job-based rather than person-based.) Answer B is not the best answer, because the potential for rater subjectivity is lower with the point factor job evaluation method than it is with whole job method of job evaluation. Answer D is not the best answer, because point factor systems do address the relative importance of each compensable factor.
4. **Answer B is the best answer.** The formula to calculate range spread is

\[
\text{Maximum} - \text{Minimum} \over \text{Minimum} = \_\% 
\]

Answer A is not the best answer; it represents a calculation that could generate a compa-ratio, not range spread. Answer C is not the best answer; it represents a calculation that could generate the numerator of the range spread formula. Answer D is not the best answer, because A was correct.

5. **Answer D is the best answer.** ERISA did establish minimum participant and vesting standards for retirement programs. Answer A is not the best answer; enhanced protection for plan members with preexisting medical conditions was established by COBRA. Answer B is not the best answer; a clearer definition of “hours worked” for purposes and minimum wage and overtime payments was established by the Portal-to-Portal Act. Answer C is not the best answer; whistleblower protection for employees who report fraud against shareholders was established by Sarbanes-Oxley.

6. **Answer D is the best answer.** Under ERISA, fiduciaries must follow the terms of plan documents to the extent that those terms are consistent with ERISA, not simply without deviation. Answer A is not the best answer; fiduciaries are required to protect plan participants by diversifying plan investments. Answer B is not the best answer; fiduciaries must act with skill, care, prudence, and diligence. Answer C is not the best answer; fiduciaries must avoid conflicts of interest.

7. **Answer C is the best answer.** The Retirement Equity Act (REA) requires that the participant and his or her spouse must waive the provision that provides for automatic survivor benefits. (This provision cannot be waived independently by the plan participant, as answer C implies.) Answer A is not the best answer; REA did lower the minimum age requirement for pension plan participation and did increase the years of service that count for vesting purposes. Answer B is not the best answer; REA did prohibit plans from counting maternity and paternity leaves as breaks in service for participation and vesting purposes. Answer D is not the best answer; REA did clarify that pension plans may obey certain qualified domestic relations (court) orders (QDRIs) without violating ERISA.

8. **Answer A is the best answer.** PHI stands for “protected health information” that relates back to one individual. Answers B, C, and D are not the best answers, because each offers a fabricated definition that is wholly unrelated to the real meaning of PHI.

9. **Answer B is the best answer.** Pension protection is addressed through ERISA, not through the Social Security Act. Answers A, C, and D are not the best answers, because retirement income (answer A), survivor’s benefits (answer C), and disability benefits (answer D) are the three major provisions of the Social Security Act.
10. **Answer B is the best answer.** The HIPAA privacy rule requires creation of a code of ethics that applies to the company’s key officers (within a “covered entity”). At a minimum, this code must apply to the company’s principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions. It does not, however, have to apply more broadly within the organization. Answer A is not the best answer; the HIPAA privacy rule does require designation of a privacy officer. Answer C is not the best answer; the HIPAA privacy rule does require the establishment of a complaint-handling and resolution process for issues relating to the HIPAA privacy rule. Answer D is not the best answer; the HIPAA privacy rule does require business associates to sign agreements stating that they will respect the confidentiality of patient information.

### Suggested Readings and Resources


eCornell, offering online programs on total rewards. [www.ecornell.com](http://www.ecornell.com), 2007.


