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HIPAA Business Associate Agreement Grace Period to End Shortly

The Health Information Technology for Economic and Clinical Health (HITECH) Act made a number of changes affecting “business associates” under the HIPAA privacy and security rules (the “HIPAA Rules”). Among those changes were updates to the “business associate agreements” that the HIPAA Rules require covered entities, such as most group health plans, to maintain with their business associates, which could include benefits brokers, claims administrators, consultants, and cloud and other data storage providers. Final HIPAA regulations clarified those changes, including the time by which amendments to the “business associate agreements” must be made.

The final HIPAA regulations established a transition rule that permitted covered entities and business associates to continue to operate under certain existing business associate agreements for up to one year beyond the compliance date of the final regulations (September 23, 2013). Under that rule, a qualifying business associate agreement is deemed compliant until the earlier of (1) the date such agreement is renewed or modified on or after September 23, 2013, or (2) September 22, 2014. Accordingly, business associate agreements that have not been updated need to be brought into compliance shortly.

When examining whether a covered entity has complied with the business associate agreement requirement, it is important to remember that the final regulations also clarified what entities are business associates. The final regulations made clear that business associates include subcontractors of business associates. As a result, covered entities and business associates need to re-examine the relationships with their subcontractors to ensure they obtain appropriate satisfactory assurances in writing concerning “protected health information” (PHI).

The final regulations also clarified that business associates include entities that store PHI (digital or hard copy) on behalf of a covered entity, "even if they do not actually view the [PHI]." This clarification creates significant compliance issues for entities such as cloud service providers and hard copy document storage companies that have access to the records of their clients but may rarely access them. While some entities may resist signing business associate agreements, the regulations make clear that entities that meet the definition of a business associate will be treated as having that status regardless of whether a business associate agreement is in place. Of course, that rule does not eliminate the covered entity’s compliance obligation to have the agreement in place.

A starting point for business associate agreement compliance is the set of sample provisions posted by the Office of Civil Rights. However, there are other issues that parties to the business associate agreement will want to address, such as, data breach coordination and response, indemnity, and agency status. Additionally, a number of state laws (e.g., California, Massachusetts, and Maryland) require businesses to have contracts with third-party service providers to safeguard personal information, which likely will include information in addition to protected health information under HIPAA.

With the expiration of the HITECH transition rule for business associate agreements looming, covered entities and business associates should be sure to examine their business associate agreements, as well as whether their agreements with third party vendors meet applicable state law requirements to safeguard personal information.

Significant ACA Questions Persist

The Patient Protection and Affordable Care Act (ACA) survived a very real threat when the Supreme Court found that the federal government could enforce penalties against individuals who have not obtained health coverage. The Obama Administration and other proponents of the ACA were hopeful the resolution of that matter would quell other challenges to the ACA’s viability, but that hope dissipated quickly. Courtrooms across the
country have been busy sorting through a myriad of challenges to the ACA.

**Religious Organizations and the Contraceptive Services Mandate**

The most recent Supreme Court matter was the *Hobby Lobby* case. Although most of the media coverage focused on the ACA contraceptive services mandate, the crux of the Court’s ruling was that a closely-held for-profit corporation could “exercise religion.” Holding that companies like Hobby Lobby can exercise religion and sincerely object to the provision of contraceptive services, the Supreme Court ruled that for-profit businesses must be afforded a religious accommodation if they object to providing contraceptive services based upon religious beliefs. Prior to the ruling, the regulations only made the accommodation available to non-profit religious organizations.

The ACA requires certain group health plans to furnish preventive care and screenings for women without any cost sharing requirements. Congress did not specify the type of preventive care that should be made available and left that decision to the discretion of the Department of Health and Human Services (HHS). HHS, in turn, implemented by regulation the Institute of Medicine’s recommendation to include all Food and Drug Administration (FDA) approved contraceptive methods, sterilization procedures, and patient education and counseling within the preventive services without cost sharing mandate.

Under the regulation, employers with religious affiliations are permitted to abstain from providing contraceptive services if they are “religious employers.” The term “religious employer” is narrowly defined and generally limited to churches and religious activities. Employers with religious affiliations not included in the exemption, e.g. universities and hospitals, objected to this narrow definition and, in response, an “accommodation” was created for non-profit religious organizations opposing contraceptive coverage on religious grounds.

Many of the religious organizations eligible for the accommodation, however, continue to object to the accommodation’s requirement that the employer notify the insurer or third-party administrator who must then provide coverage for contraceptive services. These non-profit religious organizations have mostly had success with their challenges to the contraceptive services mandate with approximately thirty injunctions granted that prevent the enforcement of the accommodation procedures.

With the circuit courts split on the issue, the religious accommodation to the contraceptive services mandate as applied to non-profit religious employers appeared primed for a Supreme Court ruling. On July 3, 2014, the Supreme Court took an unusual procedural step and granted an application for injunction in the *Wheaton College* matter, while the matter is pending on the merits in the lower court.

But after the Supreme Court granted an application for injunction in the *Wheaton College* matter, the Department of Justice (DOJ) submitted a Supplemental Brief on July 22, 2014, to the 10th Circuit Court of Appeals in another high-profile case addressing the issue, *Little Sisters of the Poor*. In the Brief the government notifies the Court that “the Departments responsible for implementing the accommodations have informed us that they have determined to augment the regulatory accommodation process in light of the *Wheaton College* injunction and that they plan to issue interim final rules within a month.”

We anticipate the forthcoming accommodations procedure to be similar to the process articulated by the Supreme Court when it granted the injunction in the *Wheaton College* matter. The Court stated that an employer must notify HHS in writing that it is a religious non-profit organization that has religious objections to providing contraceptive services coverage. It is difficult to speculate whether the revised accommodation in its final form will continue to be objectionable to non-profit religious employers or whether the Supreme Court would strike down the contraceptive mandate altogether should a case reach that level.
Are Subsidies Available Through the Federal Exchanges?

July 22, 2014, was also a significant day for litigation involving the ACA for another reason. The D.C. Circuit Court of Appeals and the 4th Circuit issued contrary rulings to the question of whether subsidies for health insurance purchased on the federal exchange may be awarded in states that did not establish their own insurance marketplace. The ACA provides that subsidies are available to those "enrolled through an Exchange established by the State." The Supreme Court’s acceptance of a literal reading of the state exchange requirement (as was accepted by the D.C. Circuit) would mean that individuals in 36 states are no longer eligible for the subsidy to lower the cost of their coverage.

The subsidies are an essential element to the ACA’s overall scheme to increase, and encourage, the purchase of health insurance. The ACA’s supporters remain confident that the intent of the provision in question and the ACA itself will prevail. Exactly how the ACA and federal exchange would operate without the subsidies is unclear, but the effects of a ruling against providing subsidies would undoubtedly jeopardize the viability of the ACA.

Even if an applicable large employer offers insurance coverage to full-time employees, the employer still could be subject to an annualized penalty of $3,000 (indexed) per employee who receives an Exchange subsidy to the extent the coverage does not provide minimum value or is not affordable. This penalty is capped at the amount that would apply if the $2,000 penalty described above were to apply.

What should an employer do now to prepare for these penalties?

A. Determine if they are an “applicable large employer.” To do this, employers should count both full-time employees and part-time employee hours as follows:

1. Count the employer’s full-time employees for each month in the prior year.
2. Count the employer’s full-time equivalents for each month in the prior year.
   a) Add total hours for non-full-time employees but count no more than 120 hours per month for any one non-full-time employee.
   b) Divide the number obtained in (a) by 120. This is the full-time equivalent number.
3. Add the numbers obtained in (1) and (2) above (i.e., the full-time employee and full-time equivalent numbers) for each month.
4. Add the 12 sums obtained in (3) and divide by 12. This is the average number of full-time employees and full-time equivalents.
5. If this number obtained in (4) is under 50 (or under 100 for the 2015 determination for certain employers), the employer is not an applicable large employer for the year being determined.

Health Care Reform: Employers Should Prepare Now For 2015 to Avoid Penalties

Under the Patient Protection and Affordable Care Act, beginning in 2015, certain large employers who do not offer affordable health insurance that provides minimum value to their full-time employees may be subject to significant penalties. These penalties are explained below.

In a nutshell, in 2015, “applicable large employers” (explained below) will be subject to an annualized employer “shared responsibility” penalty of $2,000 (indexed) per full-time employee (less the first 80 full-time employees in 2015) if the employers do not offer health insurance to at least 70% (95% after 2015) of their full-time employees and their dependents.
example, if there are three companies, each of which is wholly owned by the same parent company, the companies are all considered one employer for this calculation. Also note that special transition rules apply in determining applicable large employer status for 2015 and that a special seasonal employee exception may apply even if the threshold in (5) is exceeded.

B. If an employer will be an applicable large employer in 2015, it should determine whether it could be subject to penalties in 2015. For example, it should review its group health plan to determine if the insurance coverage is “offered” to full-time employees within the meaning of applicable regulations, provides minimum value, and is affordable.

C. An employer also will need to address how it will determine the full-time status of employees – will it use the “monthly measurement period” or the “look back measurement period.” This is particularly important for employers who have many variable-hour employees or seasonal employees.

D. If the employer’s group health plan does not meet the threshold tests to avoid the penalties noted above, the employer should evaluate whether it wants to restructure its health care offerings or pay the penalties (which are non-deductible).

E. Finally, employers should review their data collection procedures to ensure that they will be able to report the healthcare information required to be reported for 2015 (the actual reporting will occur in 2016). Insurers, sponsors of self-insured plans, and other entities that provide minimum essential coverage during a calendar year will be required to report certain information to the Internal Revenue Service and to participants. In addition, applicable large employers will be required to report about the coverage they provide to both the IRS and to their employees. Draft IRS forms to be used in reporting this information have recently been published by the IRS (Form 1095-B, Form 1095-C Transmittal). Employers should review these forms to understand the data that will need to be reported.


Open enrollment for the 2015 health plan year is just around the corner. We want to make sure that all employers are ready. We want to ensure, as well, that government contractors specifically understand the intersection of the Service Contract Act (SCA) with other federal laws.

To be spared penalties for 2015 under the Patient Protection and Affordable Care Act (PPACA), employers who have 100 or more full-time employees and equivalents (FTEs) should ensure they have identified all their 30-or-over-hour employees and be prepared to offer essential health benefits.

Employers with 50-99 FTEs must confirm they are under 100 and claim the 2015 exemption by certification to the IRS.

In our experience, government contractors who perform work covered by the SCA might be confusing how they satisfy their health and welfare fringe benefit obligations (the $3.81 per hour, for ease of reference), in coordination with health care requirements under the ACA, no matter how many FTEs that government contractor might have. Here are just two examples; we find that we are confronting more and more problematic situations, as government contractors are examining their existing practices now and tweaking their health plans, in anticipation of open enrollment this coming Fall 2014, for the 2015 plan year.
Example 1

For example, the government contractor GovK has 800 FTEs, 400 of whom are covered by the SCA. As has been the practice in years past, in 2015 GovK wants to carve out SCA employees from its company health plan and thinks that simply paying the $3.81 cash to them to allow them to buy their own health insurance (but not offering the same health plan that GovK offers to its non-SCA employees, many of whom are highly compensated), is enough to satisfy ACA. While guidance is still forthcoming related to the ACA, GovK – under these facts – cannot provide health care only to those who are highly compensated (this is a test that the health plan must pass). Moreover, under ACA and tax rules, GovK must benefit generally 70% or more of all employees (another test).

Example 2

In another example, GovK agrees to pay the employee share of the health care premium for both its SCA (so the $3.81 is accounted for through the provision of a benefit) and non-SCA workers. At its most basic, this practice is non-discriminatory under tax and health care rules, because everyone gets the same benefit of the company paying the employee share. However, when an SCA (non-exempt or exempt) employee goes out on unpaid leave, GovK stops providing the $3.81 benefit (the SCA employee isn’t working, so GovK isn’t offering the bona fide benefit), and GovK stops forwarding the employee share of the health care premium to the insurance carrier. In fact, GovK tries to collect the health premium from the SCA employee.

Yet, when a non-SCA (non-exempt or exempt) employee person goes on leave, GovK continues to pay the employee share of the health care premium; GovK won’t collect from the non-SCA employee. While we would have to examine the facts, it is likely that this practice will favor the more highly compensated employees (and therefore is discriminatory from a tax/health plan sense), who tend to be the non-SCA employees.

Further, GovK’s unwillingness to pay the SCA employee’s health premium while that employee is out under Federal Medical Leave Act (FMLA) creates compliance issues under that federal law.

Department of Labor Has Started Investigations of Health Plans

As we see with the brief examples above, compliance with one federal law does not guarantee compliance with (or insulation from) other federal laws.

To underscore the importance of compliance, we note that just last month a DOL investigator has started to evaluate the interplay of these federal laws. We urge government contractor clients to understand that, when dealing with the $3.81 fringe and designing a health plan, they should be mindful of what affects their operations.

DOL Planned Revisions to FLSA White-Collar Exemptions

The U.S. Department of Labor (DOL) recently released its 2014 Regulatory Agenda, a non-binding statement regarding anticipated efforts to create and/or change regulations relating to exemptions under the Fair Labor Standards Act (FLSA). The Agenda provides a timetable for issuance of a proposed rule to revise regulations interpreting the “white collar” overtime exemptions, which were last changed in 2004 under President Bush. “White collar” jobs are among those most commonly exempt from overtime requirements under the FLSA, and include salaried employees employed in executive, professional and administrative positions. Under current federal regulations, employees paid a salary of $455 or more per week are not eligible for overtime pay if they also perform exempt duties under one of these, or other, tests for exempt status under the FLSA.

The new rules will likely reintroduce tests requiring that exempt workers spend a specific percentage of their time engaged in the performance of “exempt”
duties, and eliminate the flexibility and functional analysis of the current “primary duty” test. The DOL also will likely raise the minimum salary level for exempt white-collar workers, which is now $455/week under federal law, although it may be higher in some states’ wage and hour statutes. One study proposes $984/week as an appropriate salary benchmark.

In a Memorandum issued in March 2014, President Obama announced his directive to the DOL to revamp FLSA exemptions. President Obama stated his Administration’s view that the $455 salary threshold means that “millions of Americans aren’t getting the extra pay they deserve” because “an exception that was originally meant for high-paid, white-collar employees now covers workers earning as little as $23,660 a year.” In addition to questioning the current salary-basis level, the President also urged simplification of the proposed rules, perhaps a reaction to a recent study which concluded that the current regulatory scheme under the FLSA is a breeding ground for wasteful litigation. For example, a recent decision from the Eastern District of Virginia rejected a claim brought by a highly-paid information technology worker paid a salary substantially above the FLSA’s $100,000/year benchmark for “highly compensated” employees to be deemed exempt under the FLSA. Mock v. Fed. Home Loan Mortg. Corp., 2014 U.S. Dist. LEXIS 97259 (E.D. Va. July 15, 2014).

In Mock, the employee served as an Engineering Senior and Engineering Tech Lead for the Federal Home Loan Mortgage Corporation (“Freddie Mac”) and was a member of a group responsible for maintenance of the Freddie Mac IT infrastructure. He was considered “the subject-matter expert and engineering lead for Freddie Mac’s virtualization infrastructure and ‘VMware,’ an intricate software with various component products that allows for the installation and testing of software programs virtually without affecting actual computers, and which increases information technology storage capacity in space while decreasing the need for physical hardware.” Freddie Mac argued, and the Court agreed, that Mock’s duties qualified him as exempt under the Administrative and Computer Professional exemptions, even without the relaxation in the standard for exempt status under the “highly compensated” ($100,000/year) test. Concerning the Computer Professional exemption, the Court noted that “although Mock did not create or write the Vmware used by Freddie Mac, he upgrades the software, modifies it to adapt it to Freddy Mac’s complex operating systems, and tests upgrades and modifications . . . this necessarily requires both a high level of skill in systems analysis and in-depth knowledge of both the software and Freddy Mac’s operating systems, and clearly establishes that Mock’s duties are exempt.”

The Mock case may be an example of the kind of litigation President Obama is suggesting could be eliminated with clarification of the FLSA’s regulations. Employers should be alert for anticipated changes in the FLSA landscape. If these yet-to-be-proposed changes become final, employers may need to implement changes to classifications. Note that this new rulemaking only addresses federal law; many states already impose a higher salary requirement and differing duties requirements for exemptions.

Some employers may have employees working on alternative work schedules which do not fit the pattern we think of as a typical “workweek.” With respect to calculating hours worked for computation of overtime pay under the Fair Labor Standards Act (FLSA), Department of Labor (DOL) regulations simply require that an employer designate and utilize a standard workweek. However, because of the vague language of the DOL regulations, employers can face challenges to their calculation of overtime payments for an employee’s “workweek.”

The FLSA provides that “no employer shall employ any of his employees . . . for a workweek longer than forty hours unless such employee receives compensation for his employment in excess of the
hours above specified at a rate not less than one and one-half times the regular rate at which he is employed," but the statute does not define "workweek." Instead, the Department of Labor’s regulation provides that:

An employee’s workweek is a fixed and regularly recurring period of 168 hours—seven consecutive 24-hour periods. It need not coincide with the calendar week but may begin on any day and at any hour of the day. For purposes of computing pay due under the Fair Labor Standards Act, a single workweek may be established for a plant or other establishment as a whole or different workweeks may be established for different employees or groups of employees. Once the beginning time of an employee’s workweek is established, it remains fixed regardless of the schedule of hours worked by him. The beginning of the workweek may be changed if the change is intended to be permanent and is not designed to evade the overtime requirements of the Act.

In a recent lawsuit, two employees were classified as non-exempt under the FLSA and were paid an hourly wage. They both worked 12-hour shifts for seven consecutive days beginning every other Thursday. One employee’s shift began at 6:00 a.m. and the other at 6:00 p.m. The employer paid on a two-week pay cycle, with overtime calculated on a Monday-through-Sunday basis. Employee Smith was typically paid for 8 hours of overtime, and Employee Johnson 4. The employees sued the employer for allegedly-unpaid overtime, claiming the employer should have calculated overtime based on their actual schedule, Thursdays through Wednesdays, which would have entitled them to 44 hours of overtime each pay period. Johnson v. Heckmann Water Res. (CVR), Inc., No. 13-40824. 2-14 U.S.App. LEXIS 13501 (5th Cir. July 14, 2014),

The federal court of appeals held that the employer may define the workweek as Monday-Sunday for the purpose of calculating employees’ pay, even though employees’ work schedules were set on a Thursday-Wednesday workweek. The Court concluded that the employer’s definition of the workweek (for payroll purposes) was "a fixed, regularly recurring period of 168 hours—seven consecutive 24-hour periods," which satisfied the FLSA and the relevant Department of Labor regulations, even though the actual work schedule covered two weeks and reduced the employees’ potential overtime pay. In other words, the Court concluded that employers have the ability and discretion to define the workweek for pay purposes, as any 7 x 24 hour period as long as they do so consistently.

The employer’s definition of the workweek and maintenance of that workweek consistently is a fundamental and critical component of payroll and budget planning. Employers should regularly review their work week, payroll, and wage and hour classification policies and practices to ensure they address specific organizational needs effectively, comply with applicable laws and are well-documented in the event of a DOL audit.

IRS Commences Section 409A Compliance Initiative Project

The IRS announced that it has commenced a compliance initiative project (CIP) to review and gauge whether selected employers are complying with the requirements of Section 409A of the Internal Revenue Code (“Section 409A”) with respect to their nonqualified deferred compensation arrangements. Section 409A imposes strict requirements on the design and operation of nonqualified deferred compensation arrangements. Failure to comply with these requirements can cause all vested amounts that are deferred under the arrangement to be immediately taxable and subject to taxes in addition to regular income tax, including a 20% tax plus a tax based on the underpayment of interest.

Overview of CIP

The CIP will involve limited-scope audits of nonqualified deferred compensation arrangements.
sponsored by approximately 50 employers. These employers have already been selected for the CIP from an existing population of employers that are undergoing employment tax audits based, in part, on the likelihood that they maintain nonqualified deferred compensation arrangements. The IRS will limit its review to nonqualified deferred compensation arrangements maintained for the employer’s top ten highly compensated individuals.

The employers will receive Information Document Requests (IDRs) from the IRS focusing on three general aspects of Section 409A compliance: initial deferral elections, subsequent deferral elections, and distribution provisions. The IDRs are expected to request information regarding compliance with both the plan document and operational requirements of Section 409A, and ask the employers to report whether any of the top ten highly compensated employees made deferral elections under, or received distributions from, a Section 409A arrangement during the years under examination in the employment tax audit.

IRS representatives have indicated that the IRS will use the project to test compliance with Section 409A, determine whether the IDRs are effective in gathering information and refine its audit techniques, presumably in preparation for conducting Section 409A audits with respect to other employers on a broader scale in the future. The CIP is expected to be completed within 12 months.

**Takeaway for Employers**

The limited scope of the CIP means that most employers will not be audited within the next 12 months; however, it is clear that the IRS is ramping up Section 409A enforcement and preparing for general Section 409A audits of employers in the future. The IRS has issued guidance permitting self-correction of certain types of Section 409A document and operational failures. These correction programs have eligibility restrictions and time limits for correction, and correction of plan document failures generally isn’t available after the IRS commences an audit of the employer’s nonqualified deferred compensation arrangements. Employers should take this opportunity to review their nonqualified deferred compensation arrangements for documentary and operational compliance with Section 409A and promptly self-correct any violations to take full advantage of the relief offered under the IRS correction programs.

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