

2019

U.S. FEDERAL REGULATIONS AND NON-CASH AWARDS



IRF Signature Study: 2019 U.S. Federal Regulations and Non-Cash Awards

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While the design of non-cash rewards programs involves exciting elements such as exotic travel destinations, fascinating insights into motivation, and thoughtful personalization, many program owners are also aware of the critical role U.S. regulatory and tax requirements play in incentive program design. The IRF’s research into program owners’ understanding of U.S. regulations affecting programs reveals a high rate of change in incentive program design due to a perceived need to make accommodations in order to comply with regulations.

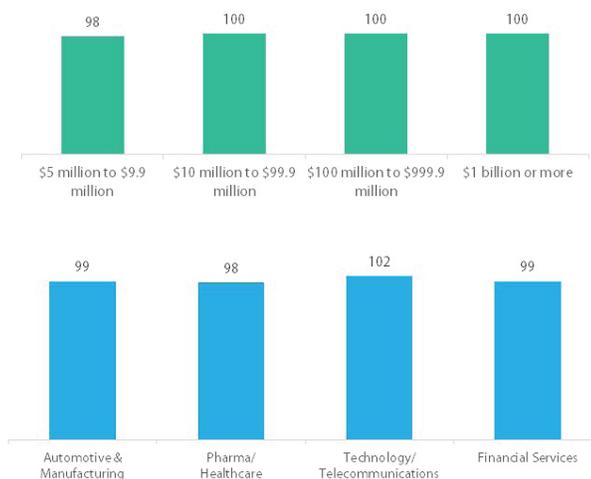
The IRF’s survey generated 398 responses from decision-makers for non-cash rewards programs representing a cross-section of US businesses with \$5 million or more in revenue. The four business sectors reporting were Automotive / Manufacturing, Pharmaceutical / Healthcare, Technology / Telecommunications, and Financial Services.

Over 70% of firms from all sectors reported that they were “extremely” or “very” knowledgeable about regulatory and tax requirements related to non-cash reward programs. They noted that they take a proactive approach to compliance, which correlated closely with high rates of change in program design year over year. More than three-quarters of businesses surveyed agree “strongly” or “somewhat strongly” that regulatory requirements for non-cash programs have led to significant changes in how they design and operate non-cash reward programs. Nearly 70% agreed that regulatory requirements for non-cash programs have diminished the effectiveness of the programs, further adding to the need to change program design.

However, when presented with specific scenarios, respondents frequently identified legal and regulatory issues where none existed, raising the question of whether the high rate of change in program design is always necessary to comply with U.S. regulatory and tax requirements.

- 398 Respondents total
- Cross-section of US businesses with \$5M or more in revenue (balanced)
- Decision-makers for non-cash rewards programs
- Four business sectors

Respondents

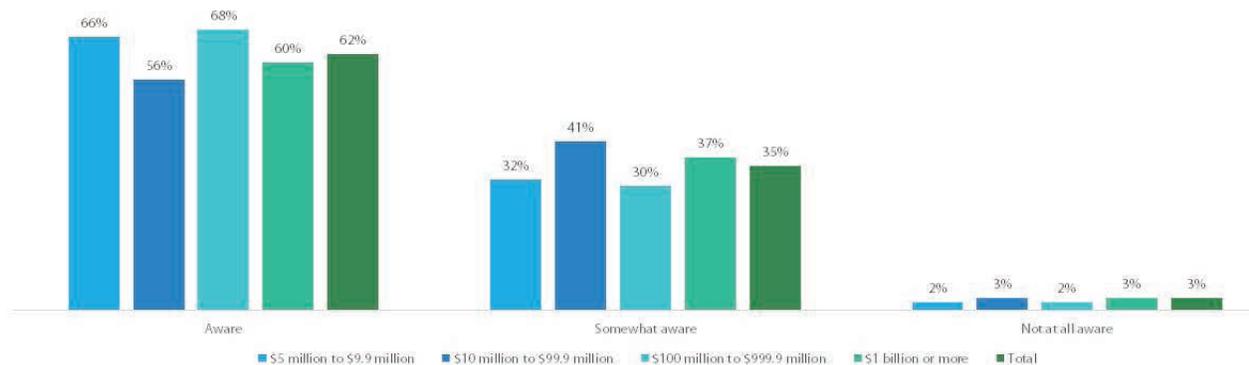


Confidence, Awareness, and Knowledge Not Aligned for Regulatory and Tax Regulations

Program owners were generally confident in their ability to identify regulatory and tax regulations. Their overall awareness of regulations was moderate, while their knowledge of what these regulations mean was relatively lower. From a vertical perspective, Financial Services and Technology / Telecommunications firms were more likely to consider themselves knowledgeable on these regulations compared to Pharmaceutical / Healthcare and Automotive / Manufacturing.

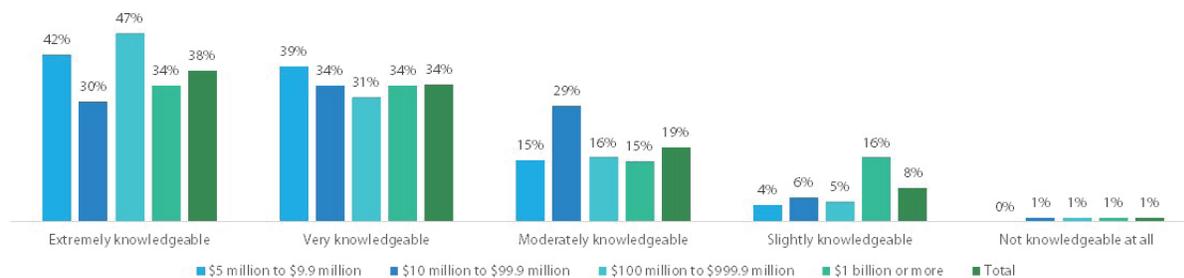
- Program owners' overall **confidence** in the ability to identify regulatory and tax requirements was high, with 77% of respondents being "very confident."
- Program owners' overall **awareness** of regulatory and tax codes was moderate, with 62% of firms stating they are "aware" of regulatory and tax codes.
- Program owners' overall **knowledge** of regulatory and tax codes lagged behind awareness, with 38% of firms reporting that they were "extremely knowledgeable" regarding the regulatory and tax requirements that businesses must comply with for their non-cash rewards programs. (Another 34% rated themselves "very knowledgeable.")
- Knowledge of regulatory and tax requirements was relatively higher for Financial Services firms (46% "extremely knowledgeable") and Technology/ Telecommunications firms (41% "extremely knowledgeable") – and relatively low for Automotive & Manufacturing (29% "extremely knowledgeable").

Awareness of Regulatory & Tax Requirements (Firm Size Data)



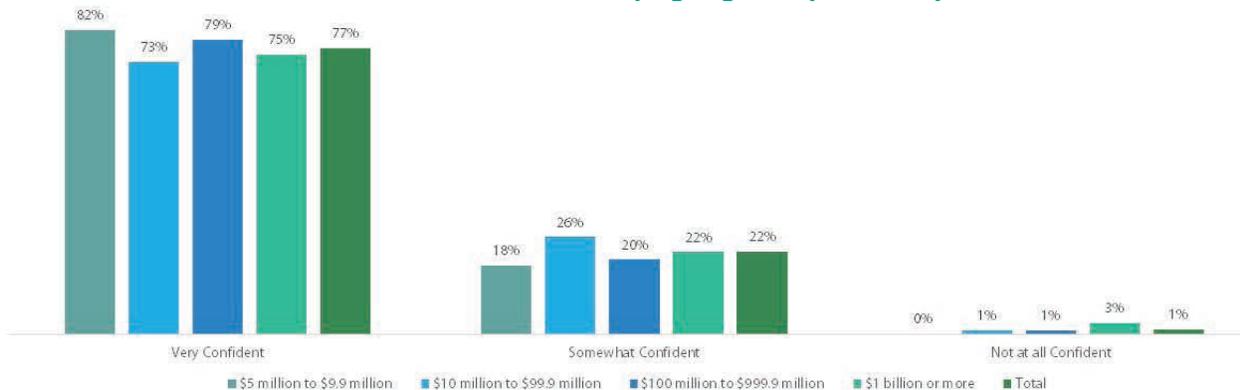
Are you **aware** of the **regulatory and tax codes** that impact the business use of non-cash rewards?

Knowledgeable Regarding Regulatory & Tax Requirements (Firm Size Data)



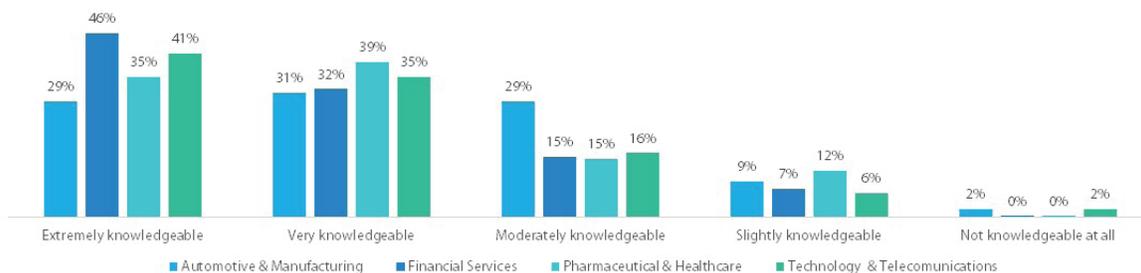
How **knowledgeable** are you regarding the **regulatory and tax requirements** that businesses must comply with for their non-cash reward programs?

Confidence in Identifying Regulatory & Tax Requirements (Firm Size Data)



For each item, please indicate which of the options BEST describes your level of confidence.

Knowledgeable Regarding Regulatory & Tax Requirements (Sector Data)



How knowledgeable are you regarding the regulatory and tax requirements that businesses must comply with for their non-cash reward programs?

Compliance as a Shared Responsibility

Compliance is top of mind for incentive program owners across all sectors, and the majority of firms are taking a proactive approach to compliance. More than half of respondents (54%) “strongly agree” that their company is taking a proactive approach, understanding, and addressing regulatory compliance in their non-cash rewards programs before the rules are put into enforcement by the government (and another 39% “somewhat agree”).

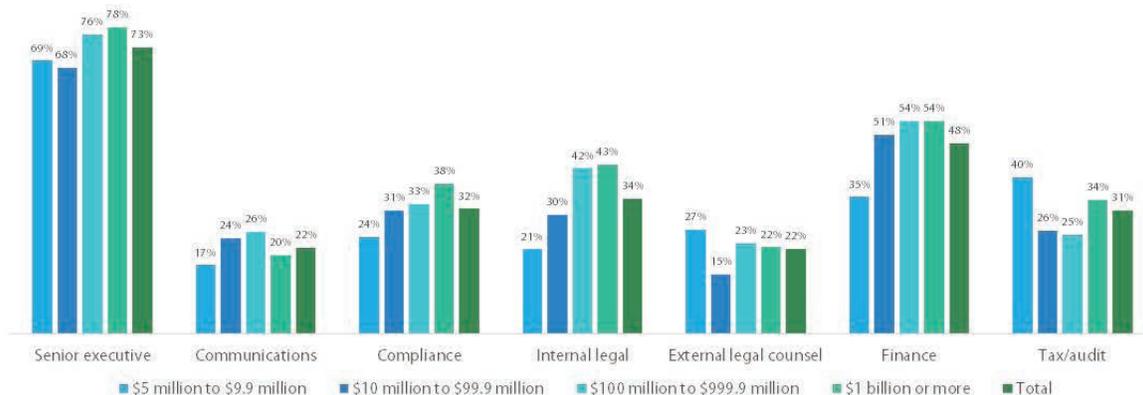
Compliance practices are more fully developed at Financial Services and Technology / Telecommunications firms, consistent with the higher ratings of knowledge reported by program owners in these sectors, discussed in the previous section.

Additional insights into how firms are implementing compliance procedures:

- Firms reported high levels of confidence in ensuring compliance with regulatory and tax requirements pertaining to non-cash rewards programs, with 69% indicating they are “very confident” they have adequate compliance measures in place.
- As firms become larger, more groups are involved in approving changes to non-cash reward programs prior to their implementation.
- Senior executive and finance departments are more likely to be involved in the review and approval of changes to non-cash rewards and programs.
- Compliance practices are more fully developed at Technology / Telecommunications and Financial Services firms, while Pharmaceutical / Healthcare firms do not yet have fully

- developed and implemented compliance practices.
- Financial Services firms were most likely (66%), followed by Technology & Telecommunications (61%) to have a fully developed and implemented documented policy to guide design, approval, and execution of non-cash rewards programs.
- As far as oversight, Pharmaceutical / Healthcare firms lagged behind other business sectors by 11-14% in having a fully developed and implemented formal review of material changes in program design by the compliance, legal, or audit team.

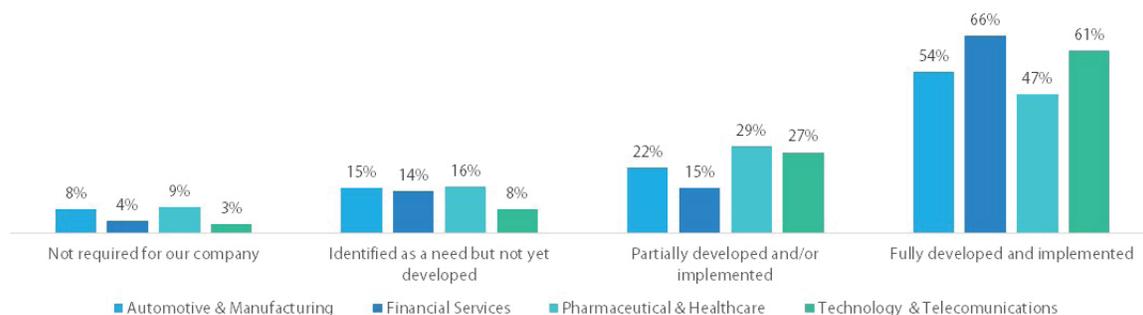
Review & Approval of Program Changes (Firm Size Data)



Which groups must review and approve changes to your non-cash rewards/programs prior to implementation?

Program Oversight Mechanisms Explicit Policy (Sector Data)

An explicit, documented policy to guide design, approval, and execution of non-cash reward programs

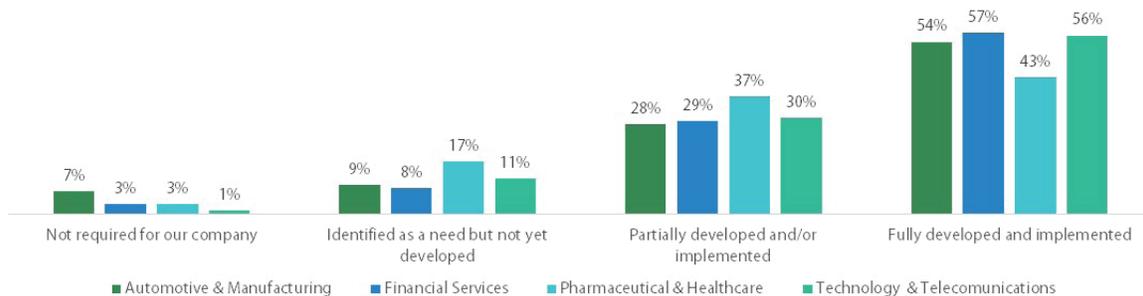


To what extent does your organization have the following oversight mechanisms in place for your non-cash reward programs?

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Program Oversight Mechanisms Change Review (Sector Data)

Formal review of any material changes in program design by compliance, legal, or audit team



To what extent does your organization have the following oversight mechanisms in place for your non-cash reward programs?

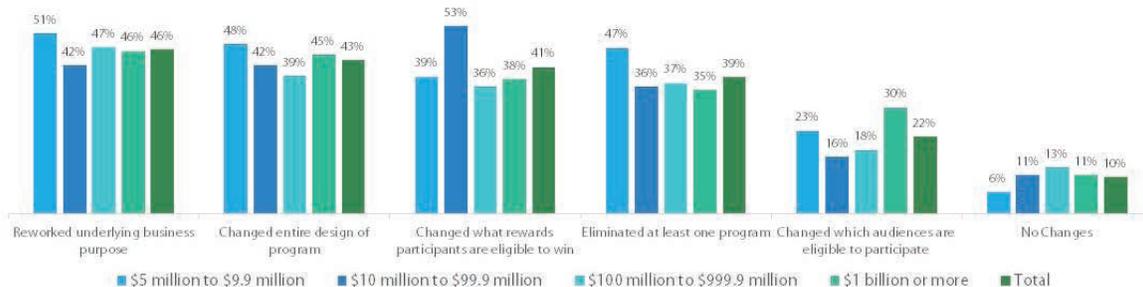
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Program Changes to Address Regulatory & Tax Requirements

High awareness and knowledge of regulatory and tax requirements correlated highly with greater rates of change in program design across all sectors among firms of all sizes. In order to comply with regulatory or tax requirements:

- 46% of firms reworked the underlying business purpose
- 43% of firms changed the entire design of a program
- 41% of firms changed what rewards participants were eligible to win
- 39% of firms **eliminated at least one program**

Regulatory Accommodations Program Design (Sector Data)



Which of the options best describes how your non-cash reward programs have been designed or changed to comply with regulatory and tax requirements?

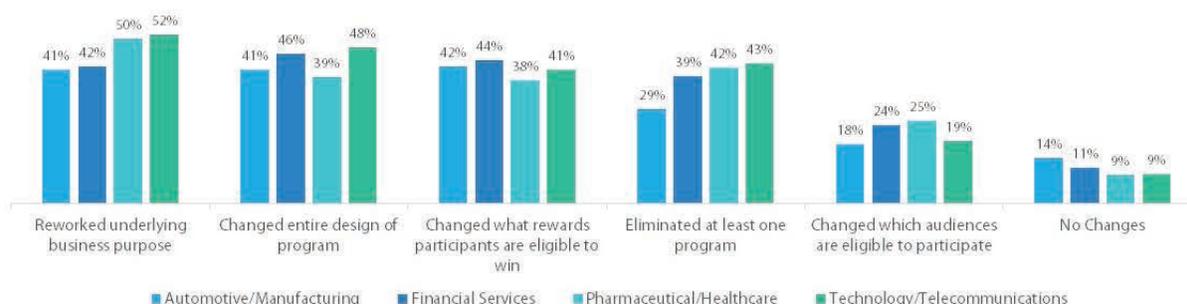
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Additional findings on changes to program design in order to be compliant with regulatory and tax requirements included:

- Almost half of firms (47%) shifted spend from cash incentives to non-cash rewards to comply with regulatory and tax requirements.
- One third of firms (66%) changed the products included in sales or distributor/channel incentive programs to comply with regulatory and tax requirements.
- Changes to reporting and analysis for compliance reasons were high for program statistics (57%) and accounting (54%), but less so for program results and outcomes (32%).
- Firms in a growth phase allocate more resources to ensure non-cash reward programs are in compliance. For firms with revenues of \$5 - \$10 million, 62% increased dollars to pay for changes to rules and rewards and 64% increased staff support for the programs.

Technology / Telecommunications firms made the most changes to both program design and company resources, while Automotive / Manufacturing made the fewest changes to both. Recall that knowledge of regulatory and tax requirements was relatively higher for Technology / Telecommunications firms and relatively lower for Automotive / Manufacturing.

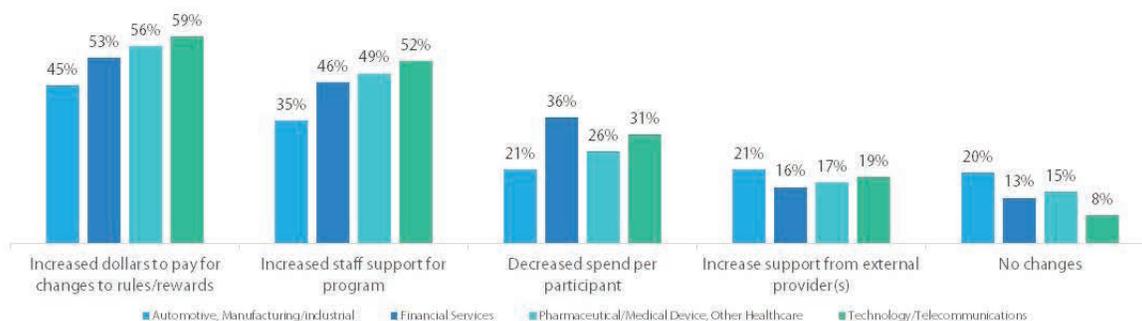
Regulatory Accommodations Program Design (Sector Data)



49

Which of the options **best describes** how your **non-cash reward programs** have been designed or changed to comply with regulatory and tax requirements?

Regulatory Accommodations Company Resources (Sector Data)



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Which of the options best describes how **company resource allocation** for your non-cash reward programs has been designed or changed to comply with regulatory and tax requirements?

Testing Industry Knowledge – False Positives Prevail

With over 70% of program owners reporting their firms had high levels of knowledge about regulatory and tax requirements, our researchers used scenario-specific assessments to test this knowledge. They provided scenarios to the respondents, then asked them to identify if these scenarios had tax, compliance, or compensation implications. These results were reviewed in tandem with legal representative George Delta, Esq. In sum, while responses varied somewhat, overall, respondents too frequently identified legal and regulatory issues where none exist. This begs the question if programs are being changed needlessly where regulatory or tax requirements do not exist. Two illustrative examples are below.

Safety Program Scenario: A company wants to increase the number of eligible employees that receive awards in a safety incentive program from 10% to 20% in a year.

- **Tax:** Most respondents (about six out of ten) **correctly** identified that such a program **would** have tax implications that need to be addressed.
- **Compliance:** About half of respondents believed **incorrectly** that this **would** raise regulatory/compliance issues.
- **Compensation:** This type of safety program could also raise compensation (overtime) issues that would need to be addressed. Very few respondents (less than one in six) identified the compensation issue as a potential problem.

Employee Incentive Scenario: A company operates a call center reward program in which customer service representatives earn rewards based on customer service and operational targets. An executive wants to generate extra excitement by adding a quarterly incentive for the top 5% of its service reps, a \$1,000 gift card to Target.

- **Tax:** Nearly half of the respondents across industries and company size believed **incorrectly** that this **would** raise regulatory/compliance issues.
- **Compliance:** About six in ten of the respondents also **incorrectly** believed that such an incentive **would** have tax implications that need to be addressed.
- **Compensation:** Only a very small number (about ten percent) believed that there **were** compensation (overtime) issues, which was a **correct** assessment.

To read the full summary of the assessments, download *Scenario Specific Assessment: Some Legal Comments* on www.theIRF.org.