GUNDERSON DETTMER

2017 Year-End Executive Compensation Matters: Annual Reporting Reminders And California Employment Law Developments

Insights
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This Alert briefly highlights certain reporting requirements applicable to equity-based compensation, as well as recent California employment law changes, as we begin 2018.

Reminder of Annual Reporting of ISO Exercises and ESPP Purchases

Employers must file information returns with the IRS and provide employees with information statements related to incentive stock option exercises that occurred during calendar year 2017. Similarly, employers (typically relevant only for public companies) must file information returns with the IRS and provide employees with information statements related to initial transfers of stock acquired during 2017 under an employee stock purchase plan that complies with Internal Revenue Code Section 423.

The information returns to be filed with the IRS are Form 3921 (for incentive stock option exercises) and Form 3922 (for transfers of shares acquired under an employee stock purchase plan). Employers may satisfy the requirement to provide employees with an information statement by delivering to the employee “Copy B” of the applicable Form 3921 or 3922 or they may use substitute forms for the employee information statements, provided that the substitute forms meet published IRS guidance as to form and content.

The delivery and filing deadlines are as follows:

- January 31, 2018 – Deadline to furnish an information statement to employees.
- February 28, 2018 – Deadline to file return, if filing a paper copy.
- March 31, 2018 – Deadline to file return, if filing electronically with IRS.

Companies reporting 250 or more transactions (applied separately to transactions under each of Form 3921 and Form 3922) in a year are required to file electronically. Note that each option exercise or stock transfer is a separate transaction, and therefore multiple transactions by a single individual trigger multiple filings.

The penalties for late and incorrect filings range from $50 to $250 per form, with a maximum penalty of $3 million. The increased penalty for intentional disregard of these requirements is $500 per form, with no maximum. The IRS will grant an automatic 30-day extension upon filing a Form 8809, which must be filed electronically or by paper by the applicable deadline. Companies may request an additional 30-day extension due to a claimed hardship, but such extension will not be automatically granted by the IRS and does not extend the due date for delivering "Copy B" of the applicable form to the employee.

Third-party vendors are available to assist companies with preparing and filing Forms 3921 and 3922. For a list of vendors, please contact the attorney with whom you regularly work at Gunderson Dettmer.

Reminder of Reporting Requirements that Apply to Acquisitions of Large Amounts of Stock

We wanted to offer a reminder that federal anti-trust laws impose certain advance filing requirements (as well as stiff penalties for filing failures) in connection with large-value stock acquisitions, including when such acquisitions take place outside of the M&A context. These requirements can be triggered by a company's issuance of stock to employees pursuant to equity compensation awards. They apply to acquisitions of stock in public and in private companies.

The Hart-Scott-Rodino Antitrust Improvements Act (HSR Act) requires companies and individuals (including officers and employees) to give advance notice to the FTC and DOJ when they acquire voting securities that meet certain dollar thresholds. Including as a result of the robust investment environment for non-publicly traded companies and the stock market up-tick, these thresholds are being achieved more frequently.

Acquisitions triggering the HSR filing include exercise of a stock option, settlement of a restricted stock unit (RSU), grant of restricted stock, and purchasing stock in a public or a private transaction, including from the company. The filing is required to be made at least 30 days prior to the proposed acquisition. This means that the acquisition should not close until expiration of that 30-day period (or earlier if “early termination” of the period is granted). For equity compensation awards that trigger the filing requirement, this means that the filing must be made 30 days *prior to* the planned exercise of an option, the scheduled settlement date of a RSU, or the grant date of a restricted stock award.

For 2017, the filing requirement applied if the total aggregate amount of voting stock that the person will hold after making the acquisition is greater than $80.8 million (this amount adjusts early in each calendar year). The 2017 filing fees start at $45,000 for acquisitions valued at more than $80.8 million and increase to $280,000 for transactions valued at more than $807.5 million. Among others who have been the subject of DOJ enforcement actions for failing to make the advance HSR filing, the CEO of Comcast paid a $500,000 fee in 2011 for a filing failure related to certain compensatory awards.

Recent California Employment Law Changes

In addition to recent increases in California (and several California cities’) minimum wage requirements, three notable new employment laws kick in as of January 1, 2018:

- A prohibition on asking job applicants about their salary history,
- A “ban-the-box” law restricting an employer’s ability to seek information about prior criminal history in the interview process, and
- Expanded parental leave for employers with 20 – 49 employees.

Prohibition on Inquiries about Salary History

Beginning January 1, 2018, California employers will not be able to consider salary history in making a hiring decision or in determining the salary level to offer an applicant.This ban is limited to applicants for employment and does not extend to current employees or contractors.Salary history information includes information about compensation and benefits, including commission pay.

Employers cannot directly or through third parties seek salary history information

about applicants, and therefore it's important that any recruiters used by an employer are aware of this law and do not pass along any such information.

If an applicant voluntarily and without prompting discloses salary history information to a prospective employer, the employer can consider and rely on that salary history in setting the applicant's salary; however, the salary history alone cannot justify any disparity in compensation and cannot be used in deciding whether to hire the applicant. (Note that the California Equal Pay Act provides that an employer may not rely on prior salary alone to justify any disparity in compensation between employees of different sexes, races, or ethnicities who perform substantially similar work.) Additionally, employers must now provide the pay scale for a position upon an applicant's reasonable request.

Ban-the-Box Law

Beginning January 1, 2018, California employers with five or more employees are prohibited from asking applicants about their criminal conviction history, either orally or in writing, until a conditional offer of employment has been made.

The new law exempts from its coverage only a handful of positions, including those for which the employer is required by federal, state or local law to check criminal history or to restrict employment based on criminal history.

If an employer decides to offer an applicant employment conditioned on the results of a background check, then it can proceed with a background check. Employers should be mindful to follow all applicable laws when performing a background check, including all notice and procedural steps required under federal and California fair credit reporting laws.

When conducting the criminal history background check, employers should not seek and cannot consider information related to arrests that did not lead to conviction, referral or participation in pretrial or post trial diversion programs, or convictions that have been sealed, dismissed, expunged or statutorily eradicated.

If an employer intends to deny employment based at least in part on the disclosed criminal background history, then the employer must engage in an individualized assessment of the applicant's conviction history to determine whether that history has a *direct and adverse relationship* with the specific duties of the job. When making the individualized assessment, the employer must consider the nature and gravity of the offense and conduct, the passage of time since the date of the offense/conduct and

completion of any sentence, and the nature of the position held or sought.

If the individualized assessment leads to a preliminary decision that the conviction history disqualifies the applicant, then the employer must follow a specific procedure, including notifying the applicant in writing and providing the applicant five business days to respond to the preliminary decision. If the employer decides ultimately not to hire the applicant, then the employer must notify the applicant of the right to file a claim with the California Department of Fair Employment and Housing.

New Parent Leave Act

Under the New Parent Leave Act (NPLA), California employers with 20 to 49 employees must begin providing eligible employees with 12 weeks of unpaid, job-protected parental bonding leave. The leave must be used within 12 months of the birth, adoption or foster care placement of the child.

To be eligible, employees must be employed with the employer for at least 12 months and have completed at least 1,250 hours of service during the 12-month period prior to commencing the leave.

The NPLA does not apply to larger employers who already must comply with the federal Family and Medical Leave Act (FMLA) and the California Family Rights Act (CFRA), both of which provide 12 weeks of unpaid, protected leave for baby bonding purposes to eligible employees of employers with at least 50 employees. However, CFRA regulations apply to the NPLA to the extent they are within the scope of and not inconsistent with the NPLA.

Employers must maintain and pay for the employee’s continued coverage under a group health plan at the level and under the same conditions that coverage would have been provided had the employee continued to work. Under certain circumstances, employers have the ability to recover health benefit premiums paid for employees who do not return to work following a leave under the NPLA.

Employees may use – but employers cannot require employees to use – their accrued vacation, PTO or sick time during the leave. Employers must guarantee reinstatement to the employee’s position or comparable position upon return from the leave and cannot retaliate against an employee who exercises the right to parental leave. Where both parents are employed by the same employer, they are entitled to a combined total of 12 weeks of leave. The Department of Fair Employment and Housing will offer a parental leave mediation pilot program until January 1, 2020.

Ensuring Compliance

To ensure compliance with these new employment laws, employers should review hiring forms and interview guidelines, revise/update applicable policies, train company personnel involved in the interview/hiring and human resources processes, and ensure that any third parties, such as recruiters and HR consultants, involved in these processes are informed about these changes. Additionally, employers should be mindful that other states and, in some cases, cities have enacted similar laws. For example, several other states, as well as Los Angeles and San Francisco, already have “ban-the-box” laws. And New York City adopted a prohibition on inquiries about salary history that went into effect in October 2017. Accordingly, it may make sense for employers that operate in multiple jurisdictions to have uniform policies on these matters.

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