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Retail & Consumer Sector

Knowledge Brief: Technical and Quality Newsletter

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What's inside:

Introduction

In this edition of the R&C *KnowledgeBrief*, we:

- Highlight SEC comment letter trends in the sector related to restructuring charges and provide disclosure reminders;
- Summarize the key provisions of the revised exposure draft on leases issued in May 2013 by the FASB and IASB;
- Discuss emerging trends with respect to implementation of conflict minerals rules in the R&C sector and share related perspectives;
- Highlight data protection and privacy considerations for retailers, including various marketing technologies and the related collection and use of personal consumer data;
- Provide an update on potential sales tax considerations applicable to remote retailers when there is not a physical presence in the consumer's state (e.g., internet sales) as a result of the proposed Marketplace Fairness Act of 2013; and
- Discuss key provisions of the Patient Protection and Affordable Care Act and related considerations for R&C companies.

We hope you find this *KnowledgeBrief* informative and useful. Please contact your PwC engagement team if you have questions or would like to further discuss any topics in this edition.

Restructuring – comment letter trends and disclosure reminders

Restructuring activity in the R&C industry continues to be high as companies respond to the economic environment, changes in consumer preferences and the impact of these and other factors on their business strategy. As such, the SEC staff continues to focus on accounting and reporting of restructuring activities through the comment letter process, stressing the importance of transparent disclosure and complying with the relevant guidance.

What is the guidance?[1]

ASC 420-10, *Exit* or *Disposal Cost Obligations* (ASC 420-10), addresses the recognition, measurement, and reporting of costs associated with exit and disposal activities, including restructuring activities. Costs associated with exit or disposal activities under ASC 420-10 include (1) employee termination benefits pursuant to one-time termination plans (other than pre-existing arrangements or a new plan that is expected to be an ongoing benefit arrangement), (2) contract termination costs, and (3) other exit costs (including costs to consolidate or close facilities and relocate employees). Certain other costs, such as costs to terminate a capital lease under ASC 840-10 or costs associated with the impairment of a long-lived asset (groups) accounted for under ASC 360-10, may be associated with exit or disposal activities but are not included in the scope of ASC 420-10.

The required disclosures in the financial statements, as outlined in ASC 420-10, include (a) description of the exit or disposal activity, including the expected completion date; (b) information about costs incurred to date and expected to be incurred for each reportable segment and for each major type of cost associated with the activity (e.g., one-time termination benefits, contract termination costs, and other associated costs); (c) a reconciliation of the beginning and ending liability balances; and, (d) the line item(s) in the income statement where the costs are aggregated. Disclosures are required in all periods, including interim periods, until the restructuring plan is completed. The SEC staff also provides presentation and disclosure guidance in Staff Accounting Bulletin Topic 5.P (SAB Topic 5.P), which indicates that restructuring charges should be included in continuing operations and separately disclosed on the income statement, if material. If a classified or "two-step" income statement format is used, the proper classification of the restructuring charge depends on the nature of the charge and the assets and operations to which it relates.

1 Refer to ASC 420-10, Exit or Disposal Cost Obligations, and SAB Topic 5.P, Restructuring Charges, for complete guidance.

The SEC staff frequently reminds registrants that whether or not currently recognized in the financial statements, exit plans which affect a known trend, demand, commitment, event or uncertainty should be separately disclosed in management's discussion and analysis (MD&A). Registrants should identify the periods in which material cash outlays are anticipated, including the expected source of their funding, and discuss material changes in the liability or revisions to restructuring plans in periods subsequent to the initiation date. MD&A should also include a discussion of the anticipated effects on future operating results and liquidity resulting from the restructuring plan (e.g., reduced employee expense, reduced depreciation, etc.). There is no "one size fits all" disclosure – companies should ensure their disclosures are robust, transparent and reflect the current and expected impacts of their restructuring plans.

Companies should also be mindful when discussing results of operations in earnings releases and MD&A when disclosing financial results excluding restructuring charges as these items may be considered non-GAAP measures. To the extent non-GAAP measures are presented, additional disclosures would be necessary to comply with the relevant guidance (e.g., Regulation G, Instruction 2 to Form 8-K 2.02 and/or Regulation S-K Item 10(e)).

Frequent areas of SEC staff comment

The SEC staff's comments generally focus on compliance with the above guidance, emphasizing the importance of transparent disclosure. The following are recent examples of comments provided to R&C companies related to restructuring activities:

Example 1

Please address each of the following for each restructuring activity by reportable segment: Disclose the specific adverse economic, business, competitive, etc. factors that precipitated the material restructuring charges. Quantify the expected effects on future operating income (i.e., the amount by which you expect expenses to decrease) and cash flows including the period the effects are expected to be realized. For restructuring activities from prior periods, disclose whether you have realized the anticipated savings. If the anticipated savings are not achieved as expected or are achieved in periods other than as expected, please disclose as such. Please also disclose the reasons for the differences and the likely effects on future operating results and liquidity. Disclose the periods in which material cash outlays are anticipated to be made and the expected source of funding the plan.

Please refer to SAB Topic 5:P.4 and Item 303(a)(3) of Regulation S-K for guidance.

Example 2

For each exit or disposal activity that has not been completed as of the most recent balance sheet date (i.e., for each exit or disposal activity with a remaining accrual), please tell us your consideration of providing (i) a description of the exit or disposal activity, including the facts and circumstances leading to the expected activity and the expected completion date and (ii) for each major type of costs and for each reportable segment the total amount expected to be incurred in connection with the activity, the amount incurred in the period and the cumulative amount incurred to date. Please also tell your consideration of disclosing the reason(s) for any adjustments to the liability, such as the $XX million reduction in the reserve related to lease terminations and other reversals in fiscal 2011 recorded in income. Refer to ASC 420-10-50-1.

Overview of the revised exposure draft on leases

In May 2013, the FASB and IASB issued a revised *Leases* exposure draft (ED) that represents an overhaul of lease accounting rules. The proposed changes will impact many key financial metrics and will have a significant impact on the R&C industry as such companies often have a large number of operating leases. The proposed accounting standards will also have far-reaching impacts on a lessee's business processes, systems and controls.

The ED requires lessees to capitalize on the balance sheet all leases that extend for more than one year. For such leases, the lessee will record a lease liability (representing an obligation to pay rent) and a right-of-use asset (representing the right to use the leased asset during the lease term). The lease liability will be equal to the present value of the lease payments to be made during the lease term. The right-of-use asset will be equal to the lease liability plus any initial direct costs, such as commissions or legal fees.

Income statement recognition will depend on the nature of the leased asset. Leases of property will be presumed to apply a straight-line lease expense pattern, similar to current operating leases. In contrast, leases of non-property (e.g., equipment) will be presumed to apply a front-loaded expense profile with the expense allocated between interest and amortization.

Does the contract contain a lease?

The analysis will start with determining if a contract meets the definition of a lease. This generally means that the customer receives the right to "control" an "identified asset" for a period of time. Under the ED, the determination of whether a contract is accounted for as a lease will take on incremental significance because leases, other than short term leases[2], will be recognized on the balance sheet, and certain leases will result in the recognition of a front-loaded, rather than straight-line, expense.

For example, if a department store agrees to provide a specific concession area to an apparel company ("concessionaire") within the store and has the sole right to alter the location by giving one month's prior written notice to the concessionaire without the concessionaire's consent or any economic or other disincentives, there is no identified asset; therefore the arrangement does not contain a lease.

Suppose in the above example the concessionaire is a coffee shop and the concessionaire bears the cost of all fixtures, which includes installing the plumbing. In this situation, the fixed plumbing could make changing the coffee shop location economically unfeasible and therefore, it may be reasonable to conclude that the location specified in the contract is an identified asset. If the concessionaire has the right to control the most significant decisions relating to use during the contract period (e.g., product range served, use of own employees, etc.) and the concessionaire also obtains substantially all of the economic benefits during the contract term because it keeps most of the sales revenue, the concessionaire has the right to control the use of the indentified asset throughout the

2 The ED defines "short term lease" as a lease that, at commencement date, has a maximum possible term under the contract, including any options to extend, of 12 months or less. Any lease that contains a purchase option is not considered a short term lease.

term of the contract. Therefore, the arrangement contains a lease because both the "identified asset" criterion and the "control" criterion are met.

When a lease contains a bundle of assets

Some entities may lease a bundle of assets instead of a single asset (e.g., land and building, land, building and equipment, or land and equipment). The ED introduces the concept of components and primary asset in a component. This analysis will determine the pattern of income statement expense recognition (i.e., front-loaded or straight-line expense).

For example, assume a consumer products company leases a building for 10 years to be used as a manufacturing plant. The building has a remaining economic life of 40 years. The contract also includes standard detachable warehouse shelving that exists in the building. In this situation, the contract contains two lease components: (a) land and building (property) and (b) shelving (non-property). This is because the shelving is not highly interrelated to the use of the building, it could be sourced from various vendors, and the company could benefit from the use of the standard shelving in another building. Additionally, under the ED, land and building are not separated for classification purposes and will be classified based on the remaining economic life of the building. Thus, in this example, the land and building lease component would follow a straight-line expense recognition pattern since they would qualify as a property lease, and the shelving, which is equipment, would follow a front-loaded expense recognition pattern.

What if in the above example, the equipment was not standard shelving, but was logistics equipment such as a conveyor belt system which was integrated in the building and without which the building would not be able to serve its intended use? If the conveyor belt system was so highly interrelated with the building such that the company could not benefit from the use of the conveyor belt line in some other building, then the company would conclude that there was one lease component in the arrangement which comprised land, building and a conveyor belt. If the primary purpose of this arrangement was to get access to a specialized conveyor belt, then the company would conclude that the arrangement was a lease of equipment in its entirety because the conveyor belt was the primary asset in the lease component and would follow a front-loaded expense recognition pattern.

Determining lease components and the primary asset within a lease component will depend on individual facts and circumstances and significant judgment could be required.

Ongoing requirements

Periodic reassessment will be required under the ED, since lease renewal periods and index based rents will need to be reassessed and the related estimates trued up as facts and circumstances change. These reassessments may produce significant financial statement volatility so the current "set it and forget it" accounting will no longer be feasible.

Transition and timing

Two methods have been proposed for transitioning to the new guidance - one method is effectively a short cut method based on approximation ("modified retrospective"); the other method involves applying the proposed guidance right from the lease start date

("full retrospective"). Issuance of a final standard is unlikely before 2014 and an effective date is unlikely before 2017. There is no grandfathering and leases existing as of the beginning of the earliest comparative period presented in the financial statements will need to effectively be "re-stated." Capital leases will get carried forward.

Developing a roadmap to implementation

Historically, many lessees have not utilized robust systems and controls for their leases. Under the ED, the initial balance sheet recognition and the subsequent reassessment of the lease term, payment estimates and support for management assumptions may require significant changes to existing processes and internal controls. Before the new guidance is effective, management could begin cataloging existing contracts and gather data about payments, renewal options and the length of the arrangements.

Companies may also want to begin evaluating their systems and controls to ensure they have the appropriate infrastructure in place prior to the effective date of the new model. Assessing the current state of leasing systems and processes now could also benefit the existing accounting and reporting of leases.

Conflict minerals – R&C industry emerging trends and perspectives

Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Section 1502) requires publicly traded companies to reasonably inquire into the origin of tin, tantalum, tungsten and gold (collectively, 3TG) minerals contained in their products, to determine whether these minerals were used to directly or indirectly fund armed conflicts in the Democratic Republic of Congo and adjoining countries (collectively, covered countries).

Companies are required to disclose the results of these inquiry processes and findings in a new "Form SD" to be filed annually with the SEC effective for calendar year 2013 with the first filing due no later than May 31, 2014, as well as disclose similar information on the company's website. The impact of this rule generally extends to all companies for which 3TG minerals are "necessary to the functionality or production of a product," wherever they may be located in the supply chain.

Section 1502 poses unique challenges – and offers equally unique opportunities – for the R&C industry.

Many would agree that the underlying intent of the legislation is a reasonable one – that of eliminating the funding for armed conflict in the covered countries, and the often adverse human impact that results. What engenders significant debate is whether the legislation as currently written is the best way to resolve these issues, with current analysis indicating both positive and negative impacts, such as reduced funding for armed groups balancing against reduced demand at legitimate mines and smelters.

Against this backdrop, R&C companies are pushing ahead with conflict minerals programs in order to comply with the rule. Looking broadly across the sector, the legislative impact has been significant – greater than many originally anticipated – encompassing companies across all consumer goods manufacturing and retailer niches from sporting goods to beauty products and home improvement to office supplies.

As a whole, based on the activity and interactions we are seeing, the R&C industry has progressed ahead of many other sectors, driven in many instances by companies with high public profiles.

While the focus for most remains on compliance with the regulation, there are a number of companies going beyond the compliance obligation and taking advantage of the insight this process is generating. Typically seen when there is a strong social responsibility aspect to the brand strategy, or where there is a younger consumer demographic and brand strategy is aligned to this demographic, we are seeing programs that go beyond a pure compliance obligation to a conflict minerals approach that integrates more seamlessly with sustainability, marketing and consumer strategies.

In a similar vein, we are also seeing some companies beginning to take advantage of supply chain insights, with conflict minerals programs driving visibility into the benefits of nominated vendor programs, supplier rationalization or supplier cost reductions, product integrity initiatives, and increased focus on product lifecycle management strategies. Benefits are also being seen from integrating with other supply chain risk efforts, such as multi-tier vendor risk management, product and materials risk and network risk, as well as tying disparate supply chain compliance efforts together (for example, CA SB 657, REACH, RoHS, FSMA, FCPA, and many materials compliance obligations).

Many, however, remain focused on their compliance obligations and a desire to ensure they are simply undertaking the endeavor in a manner similar to their peers. They are being aided in their efforts by a relatively robust number of R&C industry bodies, many with well-established conflict minerals working groups who are providing a range of guidance and, in some cases, providing training courses on a subscription basis to members. For example, the American Apparel and Footwear Association (AAFA) has provided significant explanatory guidance and perspectives, the Retail Industry Leaders Association (RILA) has focused significant effort in developing supplier training, and the Food Marketing Institute (FMI) and Grocery Manufacturers Association (GMA) have both been very active in recent conferences, events and webcasts in discussing the topic. Companies should take advantage of these resources.

While there is undoubtedly significant guidance and discussion, we are seeing an overall trend across the industry of slowly starting programs, with particular observations including the following:

1. **47% of R&C companies have not commenced supplier engagement.** The vast majority are aware of the legislation, but remain in the process of evaluating the impact across their product portfolio. A recent survey conducted by PwC during the June 2013 Retail and Consumer Conflict Minerals webcast indicated 47% of R&C companies are currently at this stage, and the 75+ retail and consumer companies we have recently spoken with would substantiate these figures. While the majority have begun discussions, many have yet to take concrete steps in beginning the reasonable country of origin inquiry (RCOI) and ensuring their program aligns with both the SEC and the Organization for Economic Cooperation and Development (OECD) requirements.

Our perspective: With the recent resolution of the initial legal challenge of the conflict minerals rules in the SEC's favor, this ruling reaffirmed that companies will need to comply with the requirements of the rules beginning with calendar year 2013. The time required to administer the RCOI survey, conduct any required due diligence, and commence remediation is often significantly longer than many initially anticipate. A recommended first step is to define a draft conflict minerals policy and quickly analyze product exposure and impacted suppliers; this has the benefit of coalescing minds across the company on the legislative impact, and enables early decisions on how the company wants to address the impact.

2. **While companies are often aware of 3TG exposure from metals in their supply chain, there is more limited awareness of other common 3TG exposure.** Companies need to be diligent in reviewing their product portfolio to identify potential exposure to 3TG. Tin, for example, can be readily found in products such as leathers, solder, coatings/some paints, metal alloys and even strengthened plastics.

   Our perspective: A complete exposure analysis and a thorough evaluation of products is conducted by reviewing bills of materials and purchase orders, and engaging in facilitated workshops with product development and sourcing teams.

3. **Blanket supplier requests and responses are more common than expected.** A number of companies have sought blanket confirmations from their suppliers rather than confirmations that apply to the products they purchase. In some instances, we have also seen companies who are relying on blanket supplier responses, or performing very limited work to assess whether the response they have received meets the SEC's requirement of a reasonably reliable representation.

   Our perspective: While some companies are taking the view that a blanket approach or limited work to assess responses is sufficient, the legislation requires RCOI and due diligence to be conducted and reported for 3TG minerals at a product level, and the SEC indicated that companies should obtain "reasonably reliable" representations for the 3TG in their products. We remain uncertain whether the SEC will view blanket confirmation approaches or limited work to assess responses as meeting the requirements defined in the issued guidance and the underlying intent of the legislation.

4. **Many companies are seeking to 'boil the ocean' and subsequently re-evaluate their approach.** Once companies decide to move ahead with supplier inquiries as part of their RCOI, there is a tendency to survey all suppliers at once. We have seen a number of R&C companies taking this approach, with a number feeling the need to subsequently re-plan the effort involved.

   Our perspective: Based on our experience, effective and efficient results are best achieved when companies take a thoughtful approach to developing the supplier RCOI strategy, pilot the approach with a select product category or group of suppliers, then incorporate amendments and adjust accordingly before rapidly replicating the process across remaining categories and suppliers.

5. **Many companies are rushing to a technology solution.** Technology vendors are playing very aggressively in the conflict minerals software space, with "solutions" emerging every month. Many band-aid solutions do exist; the key challenge is that

they often do not effectively integrate or work with other tools across the company. In addition, companies are often looking for a conflict minerals solution, and more rarely are seeking to integrate with other materials compliance requirements.

Our perspective: Technology is an important part of any conflict minerals solution, when it works hand-in-hand with business processes that operate under a thoughtfully constructed conflict minerals strategy. Additionally, as with any technology purchase, important considerations include appropriate due diligence in evaluating vendor viability, particularly for those vendors who have a limited history or very narrow solution, and consideration as to how the solution integrates with other IT applications across the company, particularly those that manage product and supplier data. Lastly, when developing a solution, companies may want to consider the benefit of a stand-alone conflict minerals solution, given the potential over coming years that materials related regulations (including other conflict minerals regulations) will continue their rise in importance for governments, Non-Governmental Organizations (NGO's) and consumers alike.

6. **Many companies have had difficulty collecting detailed data from their internal IT systems to support the identification of 3TG within the supply chain.** The ability to leverage product master and bill of materials (BOM) data can accelerate the identification of 3TG in products. However, companies often find there is limited availability, accuracy or consistency in product data across the organization, with product BOMs that are not complete or that do not always reflect the current product configuration.

   Our perspective: The effort to identify effective product data to assist in determining 3TG exposure can be significant. We would recommend developing an early understanding of current data quality during conflict minerals planning, in particular to identify the extent of work required to identify 3TG products and suppliers.

7. **Companies become entangled in terminology definitions.** There are varying interpretations of how the legislation applies to R&C companies, with the SEC releasing on May 30th additional guidance relating to a common question we hear around packaging. Key issues some companies are wrestling with include: defining "necessary to the functionality or manufacturing" of the product, determining the level of "influence" in regards to contract manufacturing, inclusion of packaging in conflict minerals program scope, or applicability to licensing relationships and joint ventures.

   Our perspective: These are complex questions for companies across all industries. We have developed a conflict minerals *"Frequently asked questions (FAQ)" document on our website (www.pwc.com/us/conflictminerals)* that addresses some of these issues, but others have not yet been fully addressed publicly by the SEC or the SEC staff. Additional guidance is expected, but companies should consult with their legal counsel on these matters and ensure buy-in from stakeholders on any issue areas. In some cases, there may be no clear answer and limited forthcoming additional guidance; in such instances the company should define what it believes to be a reasonable evaluation, and execute against that evaluation.

8. **Many companies are over-relying on supplier responses.** We have seen a number of companies issue supplier surveys without considering whether the

suppliers understand the purpose of the survey, can effectively complete the survey, or consider how difficult it will be, given the nature of products supplied and supply chain involved, for the supplier to effectively respond. This can create supplier confusion, delays, limited responses, or responses that should cause further work to be performed. We are also seeing some R&C companies with multiple hundreds of suppliers who are reaching 95% or more of suppliers being identified as conflict-free in very short time-frames, despite having complex supply chains and a difficult path to reasonably identify the country of origin or smelters.

Our perspective: Given the volume of requests suppliers are receiving, the more focused and relevant the request that can be made to a supplier, and ensuring they understand the request, the more complete and accurate a response that the supplier is likely to make. Supplier training should be considered, in particular for overseas suppliers who are highly dependent on the company as a customer. In addition, companies should evaluate supplier responses to determine if they meet the SEC's requirement for a reasonably reliable representation. The nature and complexity of global supply chains, combined with limited numbers of conflict-free smelters, will often result in slow and undeterminable responses across one or multiple products.

The trends that we are seeing across the R&C industry for conflict minerals demonstrate that hurdles remain, with the legislative interpretation continuing to evolve with industry bodies and companies alike. For many, this remains a challenging topic that becomes more opaque the further it is examined and may take a number of years to reach a result.

Yet the key to success in this endeavor, is to focus on what can be achieved next and continually place stakes in the ground as decisions are made that provide a firm foundation for progression. Those R&C companies who can internally come together and make firm decisions around the applicability of the legislation, define a policy and begin their product and supplier evaluation in earnest, will find they can make substantive progress quickly.

As many of the NGO's who originally pushed for the passage of the conflict minerals legislation have consistently indicated, this journey is not wholly about the result; it is highly focused on the processes that companies put in place to determine if they utilize conflict minerals and the continuing progress that is made in the attempt to reach a result.

We hope this article has given R&C companies some key areas to consider as they continue to address their own conflict minerals compliance challenges. For other critical success factors to consider in implementation of a conflict minerals program, for help getting started, or for additional resources on this topic, please contact your PwC engagement team or visit our conflict minerals website (*www.pwc.com/us/conflictminerals*) for access to webcasts, thought leadership, FAQ's and more.

Data protection and privacy

New opportunities equal new responsibilities

In the age of personalization and customized user experiences, the R&C industry is well-positioned to take advantage of new opportunities to drive revenue using intelligent marketing and supply chain technologies. Through the use of various technologies (e.g., real time analytics for demand planning) or marketing programs (e.g., loyalty/rewards programs), organizations are able to collect and use large amounts of personal consumer data. While the analysis of sales and personal consumer data can help promote merchandise and drive sales for both retailers and manufacturers, there are certain risks related to data protection and consumer privacy to be carefully considered and addressed, especially with the continually changing threat landscape.

The collection and use of large amounts of consumer data expose organizations to a greater risk of loss or misuse of this information. A data breach can have a severe financial impact on an organization. Studies show that the average U.S. organizational cost of a breach is $5.4M[4] and the average cost per record in the U.S. is $188[4]. These costs include investigation fees, legal fees, monitoring services, and breach notifications. The financial impact may also be increased by regulatory sanctions and fines. In the past five years, there has been an increase in privacy regulation and enforcement. Trends show that privacy regulation and enforcement are likely to continue to increase.

In addition to the financial, legal and regulatory impact, R&C organizations are especially impacted by the damage to the organization's brand and reputation. Customers are becoming increasingly savvy about the privacy practices of the R&C companies they do business with and are also becoming wary of "too good to be true" marketing schemes that simply feed marketers with personal information. Reports[3] suggest that savvy shoppers will increasingly use effectiveness of data protection as a filter for where to shop and spend.

The opportunity to monetize consumer data translates into an increased responsibility to protect customer privacy and organizational risks. So how can an organization continue to benefit from these opportunities while still managing the risks and responsibilities? In a word, prevention.

Sustaining customer trust - a better way forward

More and more R&C organizations are learning that the cost and hassle of preventative measures is typically much less than the financial and reputational impact of a data breach and therefore have adopted such preventative measures.

Preventive data protection and privacy programs help organizations proactively protect their sensitive information, thereby helping to earn and keep customers' trust in an organization's brand. While compliance with industry regulations or standards, such as Payment Card Industry compliance (PCI), is important for protection of certain data, a keen focus on sustainable controls is important for an organization to truly protect all of its sensitive information.

3. PwC's Retailing 2020: Winning in a polarized world
4. Ponemon Institute's "2013 Cost of a Data Breach – Global Analysis"

It is important for organizations to understand what data they interact with and where that data is located, including in the hands of their third party vendors. Further, the threat environment has changed dramatically in the past 5 years with attempts to maliciously obtain data becoming more coordinated and sophisticated. Having a broad understanding of threat vectors and actors that are aligned to business risks will prepare key leaders in making strategic decisions around investment priorities. Unless an organization is able to identify what needs to be protected, it is not possible to ensure that the proper protective measures or controls are in place to secure that data. For example, on average, third party errors increased the cost of data breach by as much as $43 per record[4] in the US per the Ponemon Institute's 2013 Cost of Data Breach Global Analysis. Governance, monitoring, and incident response processes are essential elements of a strong data protection and privacy program. Due to the large amounts of turnover typically found within the R&C industry, training and awareness of the importance of this matter throughout the organization may be difficult, but are also essential to a proactive program.

The trust in a brand and a business relationship takes sustained effort to build and to maintain. The emerging trends in the retail and consumer industry centered on use of personal data present opportunities to the businesses for enhancing trust and reputation by providing greater transparency in customer interactions and using data protection and privacy as a competitive differentiator.

Key takeaways

- The retail and consumer sector faces many new opportunities to leverage the data collected to help enhance business/marketing practices, drive revenue growth and maintain customer loyalty through improved brand experiences.
- New opportunities also bring new risks and responsibilities. Key considerations for an organization include the financial, legal, regulatory, and brand risks related to the collection and use of personal consumer data.
- Preventive data protection and privacy programs are typically less costly than the impact of a data breach.
- Market pressures, evolving technology and business practices, and the changing regulatory landscape require proactive measures on data protection/privacy.
- Good privacy practices earn consumer trust, and in turn brand loyalty/ positive reputation.

Sales tax on internet purchases revisited

Once again, the U.S. Congress is considering legislation that would allow states to require out-of-state (i.e., "remote") retailers to collect and remit sales taxes on purchases delivered to in-state customers, such as sales made through internet or catalog channels. Currently, under Constitutional law, states may only require these remote sellers to collect tax if they have a physical presence ("nexus") in the consumer's state. The nexus landscape is continually changing, presenting challenges to multistate retailers. Interest in a Congressional solution continues to receive attention as more and more states have enacted their own nexus laws, seeking to expand the concept of physical presence through "affiliation," "agency," and other concepts.

On May 6, the US Senate passed, by a vote of 69-27 and with significant bipartisan support, the Marketplace Fairness Act of 2013. The legislation provides that, under two different scenarios, states would be allowed to require out-of-state retailers to collect and remit tax. With the Senate passage, the legislation now faces certain challenges in the US House of Representatives, with further amendments expected.

If enacted, under the first scenario, out-of-state retailers would be required to register for sales tax purposes in full member states of the Streamlined Sales and Use Tax Agreement (SSUTA), and as a consequence collect and remit sales tax on all sales made to customers residing in these "streamlined" states. Currently, there are 22 full member states with two associate members. The SSUTA is a decade old effort to create uniformity among state sales taxes. Member states will be required to adopt common tax definitions among other simplifications requirements.

For the second scenario, non-SSUTA member states that meet certain minimum simplification requirements can require remote sales tax collection. The minimum simplification requirements to receive remote seller collection authority include the provision of a single entity within the state for administration, a single audit of a remote seller for all state and local jurisdictions, and a single sales and use tax return for remote sellers to file. Additional simplification requirements include the provision of: a uniform sales and use tax base among the state and the local taxing jurisdictions; taxability, exemption and rates and boundaries information for products and services; and free software to calculate sales taxes due and file returns, among other items.

The legislation contains a small seller exception for remote sellers with gross annual receipts in nationwide total remote sales less than $1 million.

Retailers operating in the e-commerce space should be aware of Congress' efforts in this regard. If enacted, such retailers will need to have compliance systems and procedures in place in order to comply with new collection and filing requirements. Further, retailers should be aware of the states' other nexus expansion efforts occurring simultaneously with this increased federal interest as it is possible that such retailers may already have additional tax collection and/or filing requirements as a result of these efforts in many states.

Patient Protection and Affordable Care Act

Shared responsibility or "pay or play" – effective January 1, 2015

Employers are required to comply with a number of changes under the Patient Protection and Affordable Care Act (PPACA). Beginning in 2015, all employers will be required to provide medical coverage that is adequate (covering more than 60% of medical expenses) and affordable (the employee's required contribution for the lowest cost, single-only coverage option is less than 9.5% of the employee's income) to employees who work 30 hours or more per week. If employers do not offer affordable benefits to eligible employees, they may be susceptible to the following shared responsibilities penalties:

- Employers not offering coverage to at least 95% of full-time employees (and their dependents) will be subject to an annual penalty of up to $2,000 for each full-time employee if at least one full-time employee received subsidized insurance coverage.
- Employers offering coverage to full-time employees (and their dependents) that is unaffordable or doesn't meet minimum value requirements will be subject to an annual penalty of the lesser of (1) up to $3,000 for each full-time employee receiving subsidized coverage, or (2) up to $2,000 for every full-time employee.

Impact to retail & consumer companies

The PPACA affects all employers, but there are additional considerations which affect R&C companies. According to PwC's Touchstone Survey conducted in 2012, approximately one-third of R&C companies employ 40% or more part-time employees as part of their workforce, compared to only 5% of all other companies.

The survey also pointed out a number of health care related trends including:

- Average R&C company healthcare cost rates increased 6.8% in 2011 and approximately 6% in 2012.
- Most retailers still use traditional managed care programs (PPOs and POS) and lag in pushing High Deductible Health Plans.
- Retailers make higher investments in wellness programs compared to all other companies.

Because retailers employ more part-time staff, it is important for them to manage workforce effectiveness while minimizing costs. As a result of PPACA, retailers have new decisions to make on continuing to provide coverage for part-time and seasonal employees. Important considerations include evaluation of the potential cost impact of coverage expansion on the Company's bottom line, determination of who will be joining health plans if coverage is offered, and determination as to how best to manage tradeoffs between providing coverage and potential penalties.

Workforce management strategy

The requirement to offer benefits to any employee working 30 hours per week or more requires employers to re-evaluate their workforce management strategy. An employer can determine an employee's status as a full-time employee by looking back at a defined

period of not less than three but not more than 12 consecutive calendar months (the "measurement period"), to determine whether during that measurement period the employee was employed on average at least 30 hours of service per week. If the employee was determined to be employed on average at least 30 hours of service per week during the measurement period, then the employee would be treated as a full-time employee during a subsequent period (the "stability period"), regardless of the employee's hours of service during the stability period, so long as he or she remained an employee. As such, full-time or part-time classification in 2014 will drive employee eligibility for 2015.

In order to effectively manage benefit plan costs and avoid penalties, retailers may want to consider how to best manage the service hours of part-time employees to control eligibility and reduce the vulnerability to fines and penalties.

Preparing for the operational impact of PPACA

Retailers should assess the current organizational readiness to comply with the Employer Shared Responsibility requirements of the PPACA. Assessment of the existing process and system capabilities related to workforce management and benefit eligibility may help prevent unnecessary penalties and fines, control medical benefit costs, and generate the required data for regulatory reporting and audit requirements.

- **Affordability and Minimum Value:** Determine if the current medical benefit plan options offered to employees meet both the affordability and minimum value requirements.
- **Look-back Analysis:** Perform a modeling exercise to determine the optimal look-back period to use for each employee group.
- **Workforce Management and Scheduling Process**: Assess the process and controls in place for headcount determinations, part-time scheduling strategies, and employee classification (full-time vs. part-time).
- **System Capabilities:** Assess controls and system configuration settings within the workforce management scheduling system to understand system capabilities to track and monitor employee eligibility to avoid unnecessary fines and penalties.
- **Data Integrity Controls:** Assess the controls over time and attendance data utilized to determine employee eligibility.
- **Monitoring:** Assess existing capabilities at the store, regional and corporate level to monitor employee hours and eligibility on an ongoing basis.

Timing

It is critical that R&C companies begin to assess the operational impact and organizational readiness for PPACA as soon as possible, with specific attention on the impact to workforce management. Part-time employees exceeding an average of 30 hours per week in 2014 will become eligible beginning on January 1, 2015, thus increasing potential medical benefit costs and susceptibility to penalties. As such, it is imperative that R&C companies begin analysis over current operating procedures and protocols and implement solutions to help them achieve their optimum operating efficiency while minimizing their costs, risks and exposures.

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