Tax Cut and Jobs Act

Presented by:

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Introduction

- Changes are effective after December 31, 2017 (unless otherwise noted)
- Most individual provisions sunset on December 31, 2025
- Withholdings guidance:
  - Deadline to adjust employee withholdings rates is February 15, 2018
  - Until the new Form W-4 is issued, continue using the 2017 Form W-4
    - Right now, employees do not need to resubmit Form W-4
    - A revised 2018 Form W-4 and instructions are expected in late February
  - Notice 2018-14:
    - In light of the delayed Form W-4, suspends the requirement that employees must provide a revised Form W-4 within 10 days of any change to their tax status that would reduce the allowances to which they are entitled
    - Describes the procedures by which employees may claim exemption from withholding for 2018 using the 2017 Form W-4 (expires 30 days after the 2018 Form W-4 is released)

Individual Tax Provisions

- Brackets adjusted:

2018 Tax Rate	Single	Married Filing Jointly
10%	$0 to $9,525	$0 to $19,050
12%	$9,526 to $38,700	$19,051 to $77,400
22%	$38,701 to $82,500	$77,401 to $165,000
24%	$82,501 to $157,500	$165,001 to $315,000
32%	$157,501 to $200,000	$315,001 to $400,000
35%	$200,001 to $500,000	$400,001 to $600,000
37%	Over $500,000	Over $600,000

Individual Tax Provisions

- Individual mandate "repealed" (reduced penalty to zero)
  - Effective after December 31, 2018
  - May have employees asking to drop coverage mid-year
    - Unless they experienced "change in status," no mid-year election is permitted under cafeteria plans
  - Employers should be aware that less employees purchasing insurance could mean:
    - If healthy individuals opt out of coverage, premiums may rise (higher, faster)
    - If fewer individuals seek coverage through the exchange, employers may be less likely to incur employer mandate penalties
  - NO CHANGE TO EMPLOYER MANDATE!
    - Large employers must continue to offer coverage to full-time employees
- Expands the medical expense deduction for two years
  - Lowers the threshold for medical expense deduction to expenses that exceed 7.5 percent of adjusted gross income
    - Previous threshold was 10% (Obama administration raised to 10%)
  - Only applies for 2017 and 2018 tax years (then back to 10%)
  - Note that the 10% early withdrawal penalty does not apply to payments up to the amount of deductible medical expenses
    - special tax notice may require amendment if specific enough to list %

Corporate Tax Provisions*

- Corporate tax rate reduced to flat rate of 21% (rather than graduated structure capped at 35%)
- Alternative Minimum Tax repealed
- Temporary 100% expensing for certain business assets (graduated through 2027)
- Limitation on deduction for business interest
- Repeal of deductions for certain fines, penalties and settlements
- Employer credit (up to 25%) for paid family and medical leave
  - Sunset after December 31, 2019
  - May signal wide spread transition to paid leave in future

*Many not applicable to tax-exempt entities

Benefit Provisions: Executive Compensation

- Current rules prohibit publicly held companies from deducting more than $1 million per year in compensation paid to senior executive officers
  - The new changes eliminate the exemption for commission- and performance-based pay
  - The legislation also expands the scope of covered individuals to include CFOs, along with an organization's CEO and three highest-paid employees, beginning in 2018
  - A transition rule applies to remuneration provided under a written binding contract that was in effect on Nov. 2, 2017, and was not modified in any material respect after that date
- Creates excise tax for nonprofits (including 501(c)(3) and 501(c)(6) organizations) on:
  - The compensation of the five highest-paid employees who earn <u>more than $1 million</u>
  - Excess parachute payments - payments in the nature of compensation contingent on change in corporate ownership or control, which equal or exceed three times the employees' "base amount" (generally his average annual compensation over the previous five tax years)

  - Note: 501(c)(6)s are business leagues or associations having some common business interest, the purpose of which is to promote such common interest and not to engage in a regular business of a kind ordinarily carried on for profit
    - Examples include the U.S. Chamber of Commerce and National Football League

Benefit Provisions:
Executive Compensation – Take Away

- Employers should review compensation arrangements for their top officers and consider whether any changes should be made
- Tax-exempt entities should consider including protective language in any new executive compensation arrangements that would allow them to modify or reduce compensation to the extent needed to avoid the new excise taxes

Benefit Provisions: Paid Leave Credit for Employers

- Creates a federal tax credit for eligible employers that provide paid family and medical leave for qualified employees under the FMLA
- Tax credit ranges from 12.5% to 25% of the cost of each hour of paid leave
  - 12.5% if workers receive half of their earnings, rising incrementally to 25% if workers receive their entire regular earnings
- In order to be an "eligible employer," the employer must have a written policy which:
  - (1) provides qualified employees with not less than 2 weeks of annual paid FMLA leave (prorated for non-full time employees); and
  - (2) requires that the rate of payment under the program b not less than 50% of the wages normally paid to such employee for services performed for the employer
- A "qualifying employee" is one who:
  - (1) has been employed by the employer for at least one year; and
  - (2) for the preceding year was paid no more than 60% of the "highly compensated employee" dollar threshold (i.e., $72,000 for 2018)
- The credit does not apply to any leave which is paid by a state or local government or required by state or local law
- The program is a "trial run" that will end in 2019 unless extended by Congress

Benefit Provisions:
Paid Leave Credit– Take Away

- This is not a requirement to pay employees – it’s up to you
- Employers seeking to take advantage of the paid leave credit should review their current leave policies and ensure that they meet the required guidelines

Benefit Provisions:
Defined Contribution Retirement Plans

- Under the 2017 rules, participants terminating employment with a plan loan outstanding must repay within 60 days of their departure to avoid default
  - Those who fail to do so must pay income tax on the loan's balance, and borrowers younger than 59½ also must pay a 10% early withdrawal penalty
  - Borrowers can avoid the taxable withdrawal by contributing to an IRA or other qualified employer plan in an amount equal to the defaulted loan
  - The contribution is treated as a rollover, offsetting the outstanding loan amount after separation and must be made in 60 days of the employee's departure
- Under the new rules, the deadline for repayment is extended to the latest date on which the participant can file his/her tax return for the year of termination
  - This change is only available to plan loan offsets arising from a participant's failure to repay the loan due to separation from service or plan termination

Benefit Provisions: Defined Contribution Retirement Plans – Take Away

- Gives former employees additional time to repay the borrowed money while avoiding early distribution penalties and a permanent reduction to their tax-sheltered retirement savings
- Employers may need to revise their loan procedures and/or participant communications to reflect this change

Benefit Provisions:
529 Educational Savings Plans

- 529 plan assets can now be used to pay elementary and high school tuition, in addition to college tuition and related college expenses (e.g., books, room and board)
- Savers may transfer up to $15,000 annually from a 529 plan to a 529 ABLE account that offers tax-advantaged savings for those who become blind or disabled before age 26, without affecting eligibility for benefits such as Medicaid

Benefit Provisions: 529 Educational Savings Plans – Take Away

- Using 529 plan funds for private-school fees will lessen the time that assets can compound tax-free to pay for college costs
- Private elementary and secondary schools may start to factor a family's 529 plan savings into making financial-aid decisions

Benefit Provisions: Achievement Awards

- Under existing rules, employers may deduct the cost of employee achievement awards of "tangible personal property"
- New legislation specifically excludes certain items from being considered tangible personal property:
  - Cash, cash equivalents, gift cards, gift coupons or gift certificates, or vacations, meals, lodging, tickets to theater or sporting events, stocks, bonds, other securities, and other similar items
- Not as much of a change as clarification

Benefit Provisions: Achievement Awards – Take Away

- Participating employers will need to identify awards that will now be taxable fringe benefits and deduct payroll taxes accordingly

Benefit Provisions: Commuting benefits

Mass Transit	Parking	Biking

• 2018 Limit: $260
• Eliminates employer deduction
    • Unless necessary for ensuring employee's safety
• Remains tax exempt for employees
	• 2018 Limit: $260
	• Eliminates employer deduction
	    • Unless necessary for ensuring employee's safety
	• Remains tax exempt for employees
		• 2018 Limit $20
		• Suspends exclusion from gross income and wages
		• Reimbursements are taxable and subject to payroll taxes and income withholdings

Benefit Provisions:
Commuting Benefits – Take Away

- Eliminating the tax deduction for employers may seem like a disadvantage to offering these benefits
- Decrease in corporate tax rate (from 35% to 21%) may help offset any loss of the deduction
- Get creative: employers that rent space from the same entity that owns the applicable parking facility may be able to renegotiate their lease to include free parking
- Some employers may choose to keep the benefits to stay competitive

Benefit Provisions:
Volunteer Length of Service Award Plan

- The bill doubles the benefit accrual permitted for special volunteer length of service award plans from $3,000 to $6,000 and indexes the $6,000 for inflation going forward
- Employers may consider increasing the plan's benefits in light of the increased cap, by plan amendment

- Note:457(e)(11)(A)(ii) permits benefit based solely on length of service to bona fide volunteers (or beneficiaries) on account of qualified service by such volunteers
  - Qualified Service = Firefighting and prevention services, emergency medical services, and ambulance services

Benefit Provisions: Employee Business Expenses

- Employer payment or reimbursement of an employee's business expenses will continue to be tax-free to the employee and tax deductible by the employer
- However, under the new rules, miscellaneous itemized deductions by employees for <u>unreimbursed</u> business expenses are no longer allowed

Benefits Provisions:
Roth Conversions

- Repeals the rule permitting recharacterization of Roth conversions
- Prior Law:
  - Contributions and conversions to an IRA can be recharacterized to another type of IRA within the individual's tax deadline (plus extensions) for the year of the contribution/ reconversion
- What changed:
  - The bill prohibits Roth conversions from being recharacterized after 2017.
  - However, contributions to a traditional IRA can still be recharacterized to a Roth IRA (and vice versa)

Benefit Provisions:
Other Fringe Benefits

- Moving Expenses:
  - Suspends both the Employer deduction and the exclusion from taxable income for recipients of employer-paid moving expenses
    - Exception for certain active-duty members of the armed forces
- Onsite Gyms:
  - Deduction for onsite gyms is repealed
  - Employees can continue to exclude the benefit from income
- Meals:
  - No deduction for expenses related to employee meals provided at employer's convenience
    - Employees can continue to exclude the benefit from income
  - Expands the 50% limit to *de minimus* fringe benefits to onsite eating facilities until December 31, 2025, after which employer costs are no longer deductible
- Entertainment:
  - No deduction for entertainment expenses

Miscellaneous Changes

- 2016 Disaster Relief
  - Various tax relief for 2016 and 2017 distributions from eligible employer plans and IRAs due to 2016 storms and floods
- Restriction on Casualty Loss Deduction
  - Narrows the casualty loss deduction to losses attributable to a disaster declared by the President under section 401 of the Robert T. Stafford Disaster Relief and Emergency Assistance Act, effecting employee's safe harbor hardship withdrawals
- New Cost of Living Adjustment Indexed for IRA Limits
  - Changes the index used to determine the annual cost of living adjustment on IRA contribution and deduction limits

Unchanged Provisions

- No change to 409A, 457(b), 457(f), 401(k), 415, 414(d), 414(h), or 401(a)
- No Roth mandate
- No change to ACA Employer Mandate or reporting
- No change to cafeteria plans under code § 125
- No change to FSAs, health plans, dental plans, vision plans, AD&D, or life insurance plans (for employers or employees)

Additional Information on the Firm

Kennerly Montgomery is a general practice law firm that has provided legal advice to clients for almost 100 years. KM attorneys practice in a variety of areas, representing municipal clients, including local governments, agencies and public utilities.

Bill Mason, Kathy Aslinger, and Ashley Trotto practice extensively in employee benefits law, which includes design, documentation, administration, audit, litigation, termination and qualification of employee health and welfare and pension plans for public, tax-exempt and private employers. The Firm sponsors various prototype retirement plans and prepares both interim amendments and discretionary amendments for all plan types as well as counsels with fiduciaries on ERISA and Federal & state law obligations. They represent clients before various agencies regulating employee benefits.

A Little About Your Presenters

Bill Mason received his law degree from Harvard Law School in 1974, and has been practicing more than 40 years, most of that time in employment and employee benefits for employers. Bill joined Kennerly Montgomery in 2009. He serves on the Board of Directors for the Legacy Parks Foundation and the Education Subcommittee for the United Way of Greater Knoxville. He is the past Chair of the Hillcrest Healthcare Board of Directors. In 2016, the US Treasury Department appointed him as the IRS Taxpayer Advocacy Panel (TAP) representative for Tennessee.

As a leader of Kennerly Montgomery's employee benefits practice, Kathy Aslinger assists clients in maneuvering through the complex world of employee benefit plan design and implementation, benefit considerations in mergers and acquisitions, audits, fiduciary liability issues, DOL and IRS compliance, HIPAA, COBRA, ERISA and state law obligations, and Affordable Care Act compliance. Kathy has been practicing law for almost 20 years and has been with Kennerly Montgomery since 2010. In addition, Kathy serves on the Board of Directors for Uplands Village, a continuing care retirement community in Pleasant Hill, Tennessee.

Ashley Trotto joined Kennerly Montgomery as an associate attorney in the Firm's employment law and employee benefits practice in 2013. Ashley concentrates on the Affordable Care Act and health and welfare plan compliance. She also regularly assists clients in navigating through the FLSA, HIPAA, COBRA, FMLA, ADA and other employment-related legislation. Ashley serves on the Board of Directors for the Smoky Mountain Animal Care Foundation and is also a member of the East Tennessee Benefits and Compensation Association, serves on the Hunger and Poverty Relief Committee of the Knoxville Bar Association and is a member of the United Way Health and Basic Needs Investment Committee. She's also the energy behind the Firm's on-going kindergarten book project at Christenberry Elementary.

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