New Excise Tax For Tax-Exempts Can Ensnare For-Profit Employers: Comment Deadline Fast Approaching

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As discussed here, the IRS's initial interpretation of a new excise tax under Section 4960 of the Internal Revenue Code could catch for-profit employers who set up foundations, trusts, PACs, and other tax-exempt entities off guard. The tax is 21% of certain compensation paid to the top five highest paid employees of the tax-exempt entity. Although the tax was designed to apply for compensation to high-paid executives of tax-exempt entities, an aggregation rule in the IRS's initial guidance (Notice 2019-9) picks up compensation paid by related employers, even if they are for-profit companies.

For example, suppose a for-profit company controls more than 50% of the board of a tax-exempt foundation, and the company's treasurer also serves as an officer of the foundation. If the foundation is treated as a common law employer of the treasurer (even if the for-profit company is also a common law employer), the CIO could be a covered employee of the foundation. If the treasurer makes more than $1 million—whether in the current year or in the future—the excise tax can be triggered, even if all of the treasurer's compensation is paid by the for-profit company. A similar issue could arise if the treasurer receives significant separation pay, even if it does not reach the $1 million threshold. The tax would be owed by the for-profit employer and any others who pay the treasurer's compensation.

The deadline for submitting comments to the IRS is April 2nd. Employers who are affected by the rule's broad net should consider submitting comments (and we can help).

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