Tax Reform: What Does It Mean for Your Compensation and Benefit Plans?

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The Tax Cuts and Jobs Act of 2017 (Tax Reform Act) passed through Congress and was signed into law by President Trump on Dec. 22, 2017. The Tax Reform Act contains several employee benefit changes:

- *Repeal of the Individual Mandate, but not the Employer Mandate*. The Affordable Care Act (ACA) requires individuals to maintain minimum essential health coverage or pay a penalty when filing their federal income tax return. This individual mandate will remain in effect through 2018 but is repealed starting in 2019. The ACA also imposes penalties on large employers that fail to offer affordable minimum essential health coverage to full-time employees. **The employer mandate penalties are not affected by the Tax Reform Act.**

- *Retirement Plans*. Upon termination of employment, an outstanding loan under a qualified retirement plan may be treated as a distribution, especially if the participant takes a distribution of the remaining portion of his or her accounts under the plan. The participant may rollover the loan balance to another eligible retirement plan if he or she can come up with the money. For loans that are offset after 2017, the Tax Reform Act extends the period a participant has to rollover the loan amount from only 60 days to the due date for filing a federal income tax return for that year.

  Disaster relief distributions related to natural disasters that occurred from 2016-2018 will not be subject to the 10 percent early withdrawal penalty, and participants who receive these distributions may spread the income out over a three-year period. In addition, repayment to the plan is permitted if made within three years from the date of distribution.

- *Elimination of the Performance-Based Compensation Exception under Code Section 162(m)*. Public companies may only deduct up to $1 million in compensation for each “covered employee.” With respect to compensation paid under agreements entered into on or after Nov. 2, 2017, performance-based compensation and commissions are no longer excludible in determining whether the compensation exceeds $1 million. The Tax Reform Act also closes a few loopholes: (1) the CFO is now a covered employee, (2) once an executive becomes a covered employee, he or she remains a covered employee in future tax years, even following retirement, and (3) private companies with public debt will now be covered by this deduction limitation.

- *Tax-Exempt Organizations Excise Tax on compensation in excess of $1 million.* Beginning in 2018, a 21 percent excise tax will apply to compensation in excess of $1 million paid to the top five highest-paid executives at a tax-exempt organization during a tax year. The excise tax also applies to certain parachute payment arrangements. Once an executive is a covered employee, he or she remains a covered employee in future tax years, even following retirement.

- *Qualified Transportation Fringe Benefits*. Effective Jan. 1, 2018, the employer deduction for qualified transportation fringe benefits is eliminated. Employees may continue to exclude the reimbursements from income, except that qualified bicycle commuting reimbursements are includible in income for tax years 2018-2025.

- *Moving Expenses*. For tax years 2018-2025, qualified moving expense reimbursements will be includible in income for all employees (except for a limited exclusion for Armed Forces members on active duty who are ordered to relocate). Other moving expenses incurred by employees will not be deductible during this period. Employment agreements, offer letters and similar arrangements should be reviewed to determine the impact of this tax change on promised benefits.

- *Other Fringe Benefits*. Beginning in 2018, meals provided to employees at an employer's facility or for the convenience of the employer will no longer be deductible under the de minimis fringe benefit rules. Instead, these costs will be subject to a 50 percent deduction cap. After 2025, the deduction will be eliminated altogether. Also effective in 2018, employee achievement awards in the form of cash, cash equivalent and gift cards are not deductible, except when the choice of gifts is limited to an offering preselected by the employer.

- *Paid Family and Medical Leave*. For tax years 2018-2019, eligible employers may be able to receive a tax credit equal to a percentage of wages paid to certain employees who are on a leave under the Family and Medical Leave Act (FMLA). Each employee on a leave under FMLA must be eligible for at least two weeks of paid leave at a rate of at least 50% of their regular pay. The law states that the pay received during the leave cannot be vacation, personal, or medical or sick leave pay. The credit applies only to amounts paid to employees who have been employed at least a year and received pay of $72,000 or less in the prior year. The credit ranges from 12.5% to 25% of the cost of each hour of paid leave. The statute indicates that the pay must be provided under a written policy. Several unanswered questions remain as to how an employer may take advantage of this new tax credit. The first step is determining what changes may be necessary to the company's current written FMLA policy. Guidance from the Internal Revenue Service on the requirements applicable to claim this tax credit is welcome.

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