



Tax Reform Management Alert Series

Issue 1

Tax Reform: Employee Benefits

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This is the first issue in a planned series of alerts for employers on selected topics on tax reform. The series of Tax Reform Management Alerts is designed to provide an in-depth analysis of executive compensation and employee benefits aspects of the tax reform proposals and how they will impact your business.

On November 2, 2017, Republicans revealed their tax plan in the Tax Cuts and Jobs Act (the “House Bill”). While most of the media attention has been focused narrowly on the cut to corporate tax rates and the changes in the individual tax brackets and deductions, the House Bill, and the soon-to-come companion Senate version, have several significant provisions that make important changes affecting executive compensation and employee benefits generally.

On November 16, 2017, the House Bill, as modified by the House Ways & Means Committee, passed with a vote of 227–205. The House initially took a heavy hand to many favorable executive compensation provisions and made some important changes in the retirement and welfare areas, but the House Ways and Means Committee relented a bit. The Senate Finance Committee proposal, as modified (the “Senate proposal”), released late Thursday followed suit in its approach to executive compensation. Thus, employers seem to have avoided sweeping changes that would have effectively ended nonqualified deferred compensation plans.

Nonetheless, the changes that remain will make a significant imprint for many companies if they remain in the bills as they work through the legislative process.

What Happens Next?

Seyfarth is tracking the legislation as it happens and will issue alerts to cover the evolution of what could shape up to be a changed landscape in the executive compensation, retirement, and welfare arenas. The Senate proposal came out of Committee and is expected to be debated on the floor the week after Thanksgiving.

The following provides the highlights of the House Bill, as passed, as compared to the current version of the Senate proposal.

Executive Compensation

ISSUE	HOUSE BILL, AS PASSED	SENATE PROPOSAL
Right to Defer Stock (Private Companies)	<p>Effective for stock attributable to options exercised or RSUs settled after December 31, 2017</p> <ul style="list-style-type: none"> Right to defer income on stock received in connection with an option exercise or RSU settlement if an employee, who is not an "excluded employee,"¹ makes an election no later than 30 days after the first time the right to the stock is substantially vested or transferable (whichever is earlier);² right is limited and will not apply to public corporations Clarifies that Section 83 does not apply to restricted stock units 	Same
Section 162(m) \$1 million Deductibility Limit	<p>Effective tax years beginning after 2017 with no grandfather or transition period</p> <ul style="list-style-type: none"> Eliminates the performance based compensation and commission exceptions, further limiting compensation that can be deducted Includes principal financial officer as "covered employee," realigning definition with the SEC disclosure rules Once an employee becomes a covered employee after 2016, he or she stays one, including if amounts are paid to a beneficiary 	<p>Effective tax years beginning after 2017 with limited grandfather</p> <ul style="list-style-type: none"> Same Same Same

- Generally, an excluded employee is (1) the CEO, CFO (or individual acting in either capacity), (2) family member of CEO or CFO, (3) an employee who has been one of the four highest compensated officers for the corporation for any of the 10 preceding taxable years, or (4) a 1% owner of the corporation at any time during the 10 preceding taxable years.
- If deferred, the deferred income is taxed upon the earliest of (1) the first date the qualified stock becomes transferable, including to the employer, (2) the date the employee first becomes an excluded employee, (3) the date the stock becomes readily tradeable on an established securities market, (4) the date five years after the first date the employee's right to the stock becomes transferable or is not subject to a substantial risk of forfeiture, whichever is earlier (the Senate version simply provides the date that is five years after the first date the right to the stock becomes substantially vested), or (5) the date the employee revokes the deferral election.

ISSUE	HOUSE BILL, AS PASSED	SENATE PROPOSAL
New Tax on Excess Compensation Paid by Not-for-Profits	<p>Beginning 2018, a new tax is imposed on excess compensation paid by a tax exempt employer:</p> <ul style="list-style-type: none"> • Tax equals 20% of compensation paid to a covered employee over \$1,000,000, plus excess parachute payments • The employer is liable for the tax • Covered employees are the 5 highest compensated employees; once an employee becomes a covered employee after 2016, he or she stays one • Excess parachute payments are payments contingent on termination of employment that exceed 3 times the employee's average annualized base compensation (a change in control is not required for this purpose) 	Same
Fringe Benefits		
Repeal of Deduction for Common Executive Perks	Eliminate employer deduction for entertainment expenses, membership dues and other common perquisites, unless the individual pays tax on these benefits, effective for expenses incurred after 2017	More limited changes to current law
Employer-Provided Housing	Beginning in 2018, the exclusion for housing under IRC 119 will be limited to \$50,000 (\$25,000 for a married individual filing a joint return) and will phase out for highly compensated individuals	No change to current law
Moving Expenses	Eliminate employer deduction for moving expenses incurred after 2017 and the exclusion from income for qualifying moving expense reimbursements made after 2017	Same (<i>provision sunsets after 2025</i>)

Welfare

ISSUE	HOUSE BILL, AS PASSED	SENATE PROPOSAL
Individual Mandate	No change to current law	Reduces penalty for individual mandate to \$0, beginning in 2019
Medical expense deduction (individuals may deduct unreimbursed medical expenses that exceed 10% of AGI)	Repeals deduction entirely	No change to current law
Archer Medicals Savings Accounts (MSAs)	Eliminates deduction for contributions to Archer MSAs but permits rollover to Health Savings Accounts (HSAs)	No change to current law
Qualified Transportation Fringe Benefit	Eliminates deductions for transportation fringe benefit	Eliminates deductions for transportation fringe benefit.
Qualified Bicycle Reimbursement	No change to current law	Repeals qualified bicycle exclusion (<i>provision sunsets after 2025</i>)
Dependent Care Assistance Programs	Exclusion repealed beginning in 2023	No change to current law
Adoption Assistance Program	Exclusion repealed beginning in 2018	No change to current law
Educational Assistance	Repeals tax exclusion under Code Section 127 (but not under Code Section 132(d)) for certain employer reimbursements of education-related expenses	No change to current law

Retirement

ISSUE	HOUSE BILL, AS PASSED	SENATE PROPOSAL
Hardship Withdrawals	<ul style="list-style-type: none"> Deletes the six month suspension requirement for elective deferrals following a hardship distribution Increases the plan assets from which a participant can take a hardship distribution to include earnings and employer contributions in addition to employee contributions Provides that a participant can take a hardship before requesting a loan from the plan 	No change to current law
Deferral Limits	No change to current law	Combines governmental 457(b) deferrals of the same employer with 401(k) or 403(b) deferrals for purposes of annual limit

ISSUE	HOUSE BILL, AS PASSED	SENATE PROPOSAL
415 Contribution Limits	No change to current law	Reduces the maximum aggregate contributions for individuals that are eligible for more than one plan (401(k), 403(b) and/or governmental 457(b)) of the same employer
Loans	Following a plan termination or separation from service, allows participants to rollover a qualified plan loan offset amount to an eligible retirement plan by the due date (including extensions) of the participant's federal income tax return for the year in which the offset occurs, thereby avoiding taxation on the offset amount	Same
Post-termination contributions	No change to current law	Eliminates special rule allowing employer contributions to governmental 403(b) plans for up to five years after termination of employment
Catch-Ups Contributions	No change to current law	Eliminates special 403(b) and governmental 457(b) catch-up contributions; retains the general catch-up limit
In-Service Distributions	Age for in-service distributions from governmental plans lowered to earlier of normal retirement date or age 59 ½	No change to current law
Frozen DB Plans	Frozen pension plans allowed to protect grandfathered benefits as long as grandfathered group not modified in a discriminatory manner after plan is closed to new hires	No change to current law

Seyfarth Shaw will continue to monitor Congressional and regulatory efforts and will alert clients as new developments occur.

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