Employers/Employees and the 2017 Tax Act

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On December 20, 2017, President Trump signed the Tax Cuts and Jobs Act of 2017 ("Tax Act"), ushering in an extensive array of new tax laws. Among them were changes that affect employers and employees:

Changes to Employee Benefits

Employer Deduction for Qualified Transportation Fringe Benefits. Prior to the Tax Act, an employer could deduct the cost of certain transportation fringe benefits provided to employees (i.e., parking, transit passes, and vanpool benefits). The employee could also exclude these benefits from his/her income. As of January 1, 2018, the employer deduction for qualified transportation fringe benefits has been eliminated. Additionally, except as necessary for ensuring the safety of an employee, any deduction for reimbursement of commuting expenses is disallowed.

Employee Exclusion of Bicycle Commuting Reimbursements. Prior to the Tax Act, an employee could exclude from income qualified bicycle commuting reimbursements of up to $20 per month. These amounts were also excluded from wages for employment tax purposes. As of January 1, 2018, the qualified bicycle commuting reimbursement exclusion has been eliminated.

Employer Deduction for Entertainment, Amusement, and Recreation Provided to Employees. Prior to the Tax Act, an employer could deduct expenses for recreational, social, or similar activities primarily for the benefit of non-highly compensated employees, provided such activities directly related to the active conduct of the employer's business (and such amounts were not includable in an employee's income). As of January 1, 2018, this deduction has been eliminated. The employee exclusion remains unchanged.

Employer Deduction for Meals, Food, and Beverages Provided to Employees. Prior to the Tax Act, an employer could deduct food and beverage expenses provided to employees as a de minimis fringe benefit (and such amounts were not includable in an employee's income). As of January 1, 2018, there is a 50% limitation on the deduction for food and beverages provided as a de minimis fringe benefit, including expenses for the operation of an employee cafeteria located on or near the employer's premises. The employee exclusion remains unchanged.

Employer Deduction for Employee Achievement Awards and Employee's Exclusion. Prior to the Tax Act, an employer could deduct up to $400 (or up to $1,600 for certain plans) of the value of certain employee achievement awards for length of service or safety. The employee receiving such award could exclude the award from income to the extent that the value of the award did not exceed the employer's deduction. As of January 1, 2018, the employee's exclusion and employer's deduction for achievement awards do not apply to cash, gift coupons/certificates, vacations, meals, lodging, tickets to sporting or theater events, securities, and "other similar items." However, an employee can still exclude (and an employer can still deduct) the value of tangible property and gift certificates that allow the recipient to select tangible property from a limited range of items pre-selected by the employer.

Employee Exclusion for Employer-Provided Qualified Moving Expense Reimbursements. Prior to the Tax Act, an employee could exclude qualified moving expense reimbursements paid by his/her employer. These amounts were not included as wages for employment tax purposes. As of January 1, 2018, the exclusion has been eliminated and such reimbursement is fully taxable to the employee. The one exception is for members of the Armed Forces on active duty who move pursuant to a military order.

Employer Deduction for Sexual Harassment or Abuse Settlements Subject to Nondisclosure Agreement. Prior to the Tax Act, employers could deduct ordinary and necessary expenses paid or incurred in carrying on any trade or business, with certain exceptions. As of January 1, 2018, an employer may no longer deduct the cost of any settlement, payout, or attorney fees related to sexual harassment or sexual abuse if the payments are subject to a nondisclosure agreement. This provision is effective for amounts paid or incurred after December 22, 2017.

Employer Tax Credit for Paid Family and Medical Leave. As of January 1, 2018, an employer that offers at least two weeks of annual paid family and medical leave, as described by the Family and Medical Leave Act (FMLA), to all "qualifying" full-time employees (and a proportionate amount of leave for non-full-time employees) will be entitled to a tax credit. The paid leave must provide for at least 50% of the wages normally paid to the employee. "Family and medical leave" does not include leave provided as vacation, personal leave, or other medical or sick leave. A "qualifying employee" is an employee who has been employed by the employer for at least one year, and whose compensation for the preceding year did not exceed 60% of the compensation threshold for highly compensated employees (i.e., compensation did not exceed $72,000). The credit will be equal to 12.5% of the amount of wages paid to a qualifying employee during such employee's leave, increased by .25% for each percentage point the employee's rate of pay on leave exceeds 50% of the wages normally paid to the employee (but not to exceed 25% of the wages paid). **The employer credit is effective in 2018 and 2019 only.**

Employer Benefits Retained

Although earlier drafts of the tax bill called for repeal or modification, the following benefit provisions remain unchanged by the final tax bill:

- The hardship distribution safe harbor rules incorporated into many retirement plans (proposals would have eased hardship rules); The employer-provided child care credit;
- Dependent Care Assistance Programs (DCAPs);
- Adoption assistance programs;
- Employer-provided housing;
- Educational assistance programs.

Elimination of the ACA Individual Mandate and its Effect

In addition, employers should be aware that the Tax Act eliminates the Affordable Care Act's ("ACA") individual mandate penalty starting in **2019.** The individual mandate requires most individuals to carry a minimum level of health coverage. Prior to the Tax Act, individuals who did not enroll in health coverage can incur a tax penalty. After December 31, 2018, individuals will still be required to carry health coverage, but the penalty for failing to do so has been eliminated. This may have an effect on employers. As fewer employees avail themselves of the Exchange coverage, an employer's penalty risk under the ACA's employer mandate decreases. However, the lack of individual penalty could destabilize the Exchange, resulting in more individuals looking to their employers for coverage.

Changes to the Deduction for Excessive Employee Remuneration

Prior to the Tax Act, an employer could deduct compensation (not including commissions or performance-based remuneration) paid or accrued with respect to a "covered employee" of a publicly traded corporation up to a $1 million cap per year. A "covered employee" is defined by the IRS to include the principal executive officer (PEO) and the 3 highest compensated officers (other than the PEO) as of the close of the tax year. While the IRS's definition did not include the chief financial officer (CFO), the Security Exchange Commission's definition (for securities law purposes) includes the chief executive officer (CEO), CFO, and the 3 highest paid employees who were serving as executive officers other than the CEO and CFO in its definition.

The Tax Act repeals the commission and performance based compensation exceptions to the $1 million yearly limit on the deduction for compensation paid to a covered employee of a publicly traded corporation. Additionally, the definition of "covered employee" has been expanded to include the CEO, CFO, and the 3 highest paid employees. The new Tax Act applies as of January 1, 2018, except any contract that was written, binding, and in effect on Nov. 2, 2017, and that is not modified in any material respect on or after such date, is grandfathered in.

New Excise Tax on Tax Exempt Organization Executive Compensation

Prior to 2018, an exempt organization could deduct all compensation paid to its executive employees. Under the Tax Act, an excise tax is imposed (equal to the corporate tax rate of 21%) on compensation in excess of $1 million paid to a tax-exempt organization's 5 highest paid employees for each tax year. The excise tax also applies to parachute payments in excess of the Base Amount. The Base Amount is defined as the average annual compensation of the employee for the 5 years before the employee's separation from employment. The tax on excess parachute payments applies only to payments made to employees who are highly compensated within the meaning of the Internal Revenue Code §414(q). For purposes of the excise tax, the Tax Act exempts remuneration paid to licensed medical professionals in exchange for medical services performed.

Actions for Employers

In light of changes to employer-provided benefits under the final tax bill, employers should take the following actions:

- Review qualified transportation plan(s) in light of the changes to qualified transportation fringe benefits and bicycle commuting reimbursements.
- Review any company policies that involve recreational, social, or similar activities for employees, employee meals, employee achievement awards, and/or employee moving expenses.
- Adjust payroll reporting as necessary and determine whether any taxable amounts are now eligible compensation for retirement plan deferrals and employer contributions.
- Consider utilizing the new tax credit for paid family and medical leave.

The new Tax Act has a wide ranging effect on individuals and businesses. For more information regarding the new Tax Act, contact any of the attorneys in Helsell Fetterman's Taxation Group.

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