

LEGAL UPDATE

Popular Benefits-Related Tax Provisions May be Targeted to Raise Revenue for Federal Tax Cuts

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The White House and Republican leaders in the House of Representatives and Senate are in active discussions about how to pay for the expected extension of the Tax Cuts and Jobs Act of 2017 (Jobs Act) as well as the possible implementation of other tax cuts that have been championed by President Trump, such as excluding tips and Social Security payments from income taxes. Treasury Department officials have made clear that while no final decisions have been made, one of the key points of discussions underway are the revenue offsets that will be used to minimize the total cost of the tax bill.

Some of the largest tax expenditures found in the Internal Revenue Code provide tax-favored treatment for a variety of popular employee benefit programs. As such, reductions, caps or elimination of these provisions are often mentioned as potential revenue offset candidates to help pay for tax cuts in other areas. For example, when the Jobs Act bill was being negotiated, potential revenue raisers discussed included:

- Reducing the exclusion from gross income for employer-provided health benefits;
- Imposing a lifetime cap on the amount that could be accumulated tax-free by a taxpayer in tax-favored retirement accounts such as a 401(k) plan or IRA; and
- Imposing a cap on nonqualified deferred compensation that could be accumulated tax-free or taxing all nonqualified deferred compensation.

When the initial draft Jobs Act bill was published by the House Ways and Means Committee the only one of the above provisions that was included was the proposed taxation of all vested non-qualified deferred compensation subject to Section 409A of the Code, including treating many types of equity-based compensation arrangements as being nonqualified deferred compensation subject to Code Section 409A. The practical effect of this extraordinary provision would have been to eliminate many forms of executive compensation. Fortunately, the provision was removed from the bill before it was finalized and enacted into law.

The failure to include the above provisions in the Jobs Act does not mean they will not be considered again for the new tax bill. Items that are considered as revenue raisers for one tax bill but are not included are often included in a future tax bill. For example, Code Section 409A was first considered as a revenue raiser for tax legislation in 2000, but did not make it into enacted tax legislation until 2004.

Now that tax cuts are on the horizon again, employers, employees, and other taxpayers that value these and other tax-favored employee benefit program tax expenditures should make their views known to their Congressional representatives and take an active role in trade associations and industry groups that lobby in favor of preserving these valuable provisions.

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