

HEALTH CARE REFORM NEWS

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Employee Benefit Changes in the Tax Cuts and Jobs Act Of 2017

Last month, we reported on the [Tax Cuts and Jobs Act \(H.R. 1\)](#) (the “Bill”), which was passed by Congress and awaited President Trump’s signature. On December 22, 2017, President Trump signed the Bill, overhauling America’s tax code for both individuals and corporations and providing the most sweeping changes to the U.S. Tax Code since 1986. The House and Senate Conference Committee provided [Policy Highlights](#) of the major provisions of the Bill, and the Joint Committee on Taxation provided a lengthy [explanation](#) of the Bill.

Compared to initial proposals, the final Bill generally does not make significant changes to employee benefits. The chart that follows highlights certain health & welfare and fringe benefit plan provisions of the Bill (comparing them to current law). Notable changes affecting health & welfare and fringe benefits include:

- Repeal of the Individual Mandate penalty beginning in 2019;
- New tax credit for employers that provide qualifying paid family and medical leave, as described by the Family Medical Leave Act; and
- Elimination/changes of employer deductions and/or employee income exclusions for fringe benefits, including qualified transportation fringes, moving expenses, and meals/entertainment.

What’s Not Changing In Health & Welfare and Fringe Benefits

ACA Employer Mandate & Reporting

While the individual mandate penalty has been reduced to zero beginning in 2019, at this time, the employer mandate and employer reporting requirements under the Affordable Care Act (ACA) **remain** in effect.

Other ACA Taxes and Requirements

There were **no** changes to other ACA taxes and requirements. For example, the bill does **not** eliminate (or delay) the 40% excise tax on high-cost plans (“Cadillac Tax”) that is scheduled to be effective beginning in 2020, nor does it eliminate the fees paid annually to fund the Patient-Centered Outcomes Research Institute (PCORI) through 2019. However, the Trump Administration has indicated its intention to renew ACA repeal and replace efforts in 2018, which may result in additional changes at a later date.

It has been recently reported that Republican legislators are targeting a further delay of two ACA-created taxes – a 2.3% excise tax on medical devices, and an annual fee imposed on health insurers known as the HIT tax – for inclusion in a spending bill that must be passed by January 19. Both of these taxes are scheduled to go into effect beginning in 2018 after a delay was incorporated in a 2015 year-end tax extenders deal. Employer groups have been lobbying for an elimination or delay of the Cadillac Tax and relief on the employer mandate. It remains to be seen whether these tax relief items will be included as part of a spending bill later this month.

FSA, HSAs, Adoption Assistance and Education Assistance Programs

Earlier versions of the Bill in both the House and Senate included provisions that would have significantly affected the tax treatment of many employee benefits. However, the final Bill makes **no** changes to the tax treatment of HSAs, dependent care FSAs, health FSAs, adoption assistance programs, or qualified education assistance programs. However, it has been reported that repealing restrictions on using FSAs, HSAs and other account-based plans to purchase over-the-counter medications could also be considered during negotiation of the spending bill.

Qualified Transportation Fringe Benefits

Employees may continue to receive transit expense reimbursements (other than bicycle commuting expenses) on a tax-free basis under qualified transportation fringe programs, but the Bill eliminates the employer deduction for employer-paid transportation benefits. Because contributions made under pre-tax salary deferral arrangements are considered employer contributions, it would appear that employers lose the deduction for any qualified transportation fringe benefits provided to employees, including those funded through pre-tax employee contributions. However, it is not entirely clear whether the law was intended to have this effect or whether the deduction is lost only for expenses the employer pays directly (i.e., without pre-tax employee contributions).

Given this ambiguity, employers may wish to wait for a technical correction to the Bill or IRS guidance before making any changes (such as converting transportation programs to after-tax arrangements which would generally be more tax efficient for employers) or eliminating such programs, whether through a cafeteria plan or otherwise (which could also raise issues under local ordinances in such cities such as Washington, DC, New York, and San Francisco that require employers to maintain such programs).

Note that tax-exempt employers are also impacted by this change. They will be taxed on the value of qualified transportation fringe benefits (such as payments for mass transit) provided to the same extent that a for-profit employer would be denied a deduction for providing tax-free transit benefit, by treating the funds used to pay for the benefits as unrelated business taxable income (UBTI).

Other Benefits and Compensation

This publication is focused on elements of the Bill which affect health & welfare and fringe benefits, but it is important to note that the Bill also impacts certain other employee compensation and benefits matters. Notable changes related to compensation and retirement savings benefits include:

- Extended rollover periods for deemed distributions of loans provided by tax-qualified retirement plans;
- Tax relief for certain retirement plan and IRA distributions taken by 2016 disaster victims;
- Modification of executive compensation deduction limitation for publicly traded companies;
- New excise tax for highly compensated non-profit employees;
- New “qualified equity grant” allowing limited deferral of stock option and restricted stock taxation for non-publicly traded company employees; and
- Modification of excise tax rate for stock compensation held by insiders of expatriated companies.

Next Steps

Only time will tell the full impact of the Bill on employers and employees. For instance, the repeal of the individual mandate beginning in 2019 may result in fewer individuals enrolling in Marketplace coverage and reduce potential employer mandate penalty exposure, which is triggered when a full-time employee receives a premium subsidy for Marketplace coverage. However, if fewer “healthy” individuals enroll in health coverage, it could result in increased premiums.

Given the changes to the corporate tax rates, it remains to be seen whether employers will alter how they compensate their employees, particularly, highly compensated employees, and how they will handle their pension, 401(k)/profit sharing plans, and other employee benefits.

In addition, it is likely there will be a correction bill (and IRS guidance) in 2018 to address unintended consequences, omissions, ambiguities, and drafting errors in the Bill. We will continue to monitor for further legislative and other developments affecting employee benefits as a result of the passage of the Bill.

In the meantime, we suggest that employers work with their payroll departments and vendors, accountants, finance, counsel and other advisors to assess the impact of the Bill to their benefit programs and implement necessary changes to their systems and practices.

SUMMARY OF SELECT EMPLOYEE BENEFITS CHANGES IN THE TAX CUTS AND JOBS ACT (H.R. 1)¹

Provision	Current Law	New Law
Individual Shared Responsibility (Health Insurance Mandate)	<p>The ACA imposes a tax penalty on individuals for any calendar month in which they are not covered by health insurance providing “minimum essential coverage.” For 2018, the annual individual mandate penalty amount per adult is \$695 or 2.5% of household income in excess of tax filing thresholds, whichever is higher.</p>	<p>The individual mandate penalty is reduced to zero.</p> <p><i>Effective Date: January 1, 2019</i></p>
Employer Credit for Paid Family and Medical Leave	<p>The Family and Medical Leave Act (FMLA) entitles certain employees of covered employers to take twelve weeks of unpaid, job-protected leave annually for specified family and medical reasons (e.g., the birth of a child, to care for an employee’s spouse, child, or parent who has a serious health condition, or for a serious health condition that makes the employee unable to perform the essential functions of his or her job).</p> <p>No current law allows employers to claim a credit for compensation paid to employee on family and medical leave.</p>	<p>New general business tax credit for employers that pay employees on family and medical leave, as described by the FMLA.</p> <p>An employer must allow all “qualifying” full-time employees not less than two weeks of annual paid family and medical leave (and a commensurate amount of leave on a pro rata basis for less-than-full-time employees). The leave program must provide for at least 50% of the wages normally paid to an employee.</p> <p>Vacation leave, personal leave, or other medical or sick leave would not be considered family and medical leave. Leave paid for or mandated by a state or local government is not taken into account.</p> <p>A “qualifying” employee is an employee who has been employed by the employer for one year or more, and who for the preceding year, had compensation not in excess of 60% of the compensation threshold for highly-compensated employees (\$120,000 for 2018).</p> <p>The credit would be equal to 12.5% of the amount of wages paid, increased by 0.25% for each percentage point by which the rate of payment exceeds 50% (but not to exceed 25% of the wages paid). The maximum amount of family and medical leave that may be taken into account with respect to any employee for any taxable year is 12 weeks.</p> <p><i>Effective Date: For wages paid in 2018 and 2019 (provision sunsets as of 2020)</i></p>
Employer Deduction for Qualified	<p>An employer may deduct the cost of certain fringe benefits provided to employees, including transportation</p>	<p>Employer deduction eliminated for providing qualified transportation fringes or for expenses incurred for providing transportation for</p>

Provision	Current Law	New Law
Transportation Fringe Benefits	fringe benefits, even though such benefits are excluded from the employee's income. Qualified transportation fringes include parking, transit passes, and vanpools.	<p>commuting between an employee's residence and place of employment, except for ensuring the safety of an employee.</p> <p>Exclusion of qualified transportation fringe benefits is generally preserved for employees.</p> <p><i>Effective Date: Amounts paid or incurred beginning 2018</i></p>
Employee Exclusion for Qualified Bicycle Commuting Reimbursement	Employees may exclude from their income qualified bicycle commuting reimbursements of up to \$20 per month. These amounts are also excluded from wages for employment tax purposes.	<p>Exclusion of qualified bicycle commuting reimbursements is suspended.</p> <p><i>Effective Date: Taxable years 2018 through 2025</i></p>
Employer Deduction and Employee Exclusion for Qualified Moving Expense Reimbursements	Employers may deduct for reimbursements of qualified job-related moving expenses and employees may exclude employer-provided moving expense reimbursements from gross income and wages for employment tax purposes.	<p>Employer deduction and employee exclusion of qualified moving expense reimbursements is eliminated, except for members of the Armed Forces on active duty who move pursuant to a military order.</p> <p><i>Effective Date: Amounts paid or incurred from 2018 through 2025 (provision sunsets as of 2026)</i></p>
Employer Deduction for Entertainment, Amusement, Recreation Expense	Employers may deduct only 50% of otherwise deductible expenses for entertainment, amusement, recreational activities, and membership dues if the expenses directly relate to their business.	<p>Employer deduction eliminated (unless an exception applies).</p> <p><i>Effective Date: Amounts paid or incurred beginning 2018</i></p>
Employer Deduction for Meals, Food and Beverages	<p>Employers may deduct for ordinary and necessary business expenses for meals, food, and beverages.</p> <p>Any deduction for meals, whether entertainment or not, is subject to a 50% limit, unless an exception applies.</p> <p>Food and beverages that can be excluded from an employee's income as a de minimis fringe benefit, including expenses for an employee cafeteria located on or near the employer's business premises, can be fully deducted.</p>	<p>Employer deduction eliminated for meals, food, or beverages, to the extent that such expenses are entertainment, amusement, or recreation (unless an exception applies).</p> <p>For amounts incurred and paid after December 31, 2017 and until December 31, 2025, employer expenses associated with providing food and beverages to employees through an on-premises eating facility that meets requirements are subject to 50% limitation.</p> <p>Beginning in 2026, any deduction for employee cafeterias is eliminated, as is any deduction for meals furnished for the convenience of the employer on the business premises of the employer.</p> <p><i>Effective Date: Generally, amounts incurred and paid beginning 2018</i></p>
Employer Deduction for Achievement Awards	Employee achievement awards for length of service or safety achievements are deductible by employers up to a certain amount if	Employer deduction for employee achievement awards is limited by a new definition of "tangible personal property" that denies the deduction for cash, cash equivalents, and gift cards, coupons,

Provision	Current Law	New Law
	<p>certain conditions are met. Awards that are deductible by an employer are also excluded from employees' income are also excluded from wages for employment tax purposes.</p>	<p>or certificates, vacations, meals, lodging, tickets to sporting or theater events, securities, and "other similar items," except when employees can only choose from a limited array of pre-selected or pre-approved items by the employer.</p> <p><i>Effective Date: Taxable year 2018</i></p>
<p>CPI-U for Tax Code Indexing for Health FSAs, HSAs, transit and parking limits, "Cadillac Tax"</p>	<p>Various Tax Code dollar thresholds/ maximum contribution limits are adjusted for inflation based upon annual changes in the standard DOL-published Consumer Price Index for all Urban Consumers (CPI-U).</p>	<p>Use of the CPI-U as the inflation adjustment is replaced with what is commonly referred to as the "Chained CPI-U." Use of the Chained-CPIU is expected to result in relatively reduced inflation adjustments when compared to the standard CPIU-U. It is expected that statutory maximum contribution limits applicable to HSAs and health FSAs, among others, would increase at a slower rate than if CPI-U continued to apply. Similarly, for purposes of indexing, the dollar thresholds for coverage that triggers the Cadillac Tax under Code Section 4980I would also increase at a slower rate.</p> <p><i>Effective Date: Taxable year 2018</i></p>

¹ This summary is not an exhaustive list of all changes in the Tax Cuts and Jobs Act (H.R. 1). It only covers select employee benefit changes. It is provided for educational and informational purposes only and does not contain legal advice. You should not act on any information provided without consulting legal counsel.

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