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NAVIGATING US TAX REFORM:

Tax-Exempt Organizations

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THE ACT FORMERLY KNOWN AS THE TAX CUTS AND JOBS ACT

Key TEO Provisions

- New excise tax on certain compensation paid to highly compensated employees
- Changes to the calculation of unrelated business taxable income (UBTI)
 - UBTI is increased by the amount of certain fringe benefits
 - Net operating loss deduction can only be taken with respect to the applicable trade or business generating UBTI
- New tax on certain college and university endowments
- A number of changes that impact charitable giving

Executive Compensation

- Section 4960 imposes a 21% excise tax on an employer with respect to (1) compensation in excess of \$1 million as well as (2) excess parachute payments paid by an applicable tax-exempt organization to a covered employee.
- What is an applicable tax-exempt organization?
 - Organizations exempt from tax under Section 501(a) (e.g., 501(c)(3), (c)(4), (c)(6))
 - Farmer cooperatives described in Section 521(b)(1)
 - Organizations with income excluded from tax under Section 115(1)
 - Political organizations described in Section 527(e)(1)

Executive Compensation (cont'd)

- Who is a covered employee?
 - An employee (including a former employee) who is one of the five highest-paid employees for the taxable year or who was a covered employee of the organization (or a predecessor) for any preceding taxable year beginning after December 31, 2016.
- Special rules apply to compensation paid by related entities.

Executive Compensation (cont'd)

- How is “compensation” defined?
 - All remuneration paid for services performed as determined for income tax withholding purposes, plus amounts required to be included in gross income under Section 457(f) at the time they are no longer subject to a substantial risk of forfeiture
 - Excludes:
 - Any designated Roth contribution as defined under Section 402A(c)
 - Compensation paid to a licensed medical professional (including veterinarians) for the performance of medical or veterinary services
- When deferred compensation is “compensation” under 4960
 - 457(b) plan – when paid or made available
 - 457(f) plan – upon vesting
 - May inadvertently trigger excise tax

Executive Compensation (cont'd)

- What is an excess parachute payment?
 - The excess of (a) any payment (in the nature of compensation) to or for the benefit of a covered employee that is contingent on the employee's separation, and the aggregate present value of all payments is at least three times the base amount, over (b) the portion of the base amount allocated to such payment.
 - The base amount is the average annualized compensation includible in gross income for the five taxable years ending before the date of the employee's separation.
 - Excludes payments under a qualified retirement plan, a simplified employee pension plan, a simple retirement account, a tax-deferred annuity, and an eligible deferred compensation plan of a state or local government employer, as well as payments to licensed medical professionals for the performance of medical or veterinary services and to an individual who is not a highly compensated employee under Section 414(q).

Unrelated Business Income Tax

- Section 512(a)(7) increases unrelated business taxable income (UBTI) by the amount of certain fringe benefits for which a deduction is disallowed under Section 274 (e.g., qualified transportation fringe benefits, any parking facility used in connection with qualified parking, and on-premises athletic facilities to the extent a deduction is disallowed).
 - Doesn't apply to the extent that the amount is directly connected with a regularly carried-on unrelated trade or business.
- Section 512(a)(6) requires an organization with more than one unrelated trade or business to compute UBTI separately with respect to each trade or business and without regard to the specific deduction allowed under Section 512(b)(12).
 - A net-operating-loss deduction is allowed only with respect to a trade or business from which the loss arose.

Endowment Excise Tax

- Section 4968 imposes a 1.4% excise tax on the net investment income of each applicable educational institution.
 - Net investment income corresponds to the private foundation definition and generally includes interest, dividends, rents, royalties (and income from similar sources), and capital gain net income, reduced by expenses incurred to earn this income.
- An applicable educational institution is defined as an eligible educational institution within the meaning of Section 25A(f)(2):
 - That had at least 500 students during the previous taxable year, more than 50% of whom are located in the United States;
 - That is not described in the first sentence of Section 511(a)(2)(B) (relating to state colleges and universities); and
 - The aggregate fair market value of the assets of which at the end of the preceding taxable year (other than those used directly in carrying out the institution's exempt purposes) is at least \$500,000 per student.

Endowment Excise Tax (cont'd)

- The number of students of an institution (including for purposes of determining the number of students at a particular location) shall be based on the daily average number of full-time students attending such institution (with part-time students taken into account on a full-time student equivalent basis).
- The excise tax includes the net investment income and assets of related organizations—such as controlling and controlled organizations and supported and supporting organizations.

Charitable Giving

- Increases the standard deduction to \$24,000 for joint filers (and surviving spouses), \$18,000 for head-of-household filers, and \$12,000 for individual filers.
 - Amounts adjusted for inflation based on chained consumer price index (C-CPI-U).
- Retains the charitable contribution deduction for taxpayers able to claim itemized deductions.
- Increases the limitation for cash contributions to public charities (and certain private foundations) to 60% of the donor's adjusted gross income (AGI) for taxable years beginning after December 31, 2017 and before January 1, 2026.
- Repeals the special rule enabling a donor to take a charitable deduction of 80% of the amount paid for the right to purchase tickets for athletic events.

Charitable Giving (cont'd)

- Repeals the “Pease” limitation, which sets an overall limit on itemized deductions including charitable contribution deductions for taxable years beginning after December 31, 2017 and before January 1, 2026.
- Doubles the amount eligible for exclusion from estate, gift, and generation-skipping taxes to \$10 million, indexed for inflation occurring after 2011. The change applies to taxable years beginning after December 31, 2017 and before January 1, 2026.

Additional Provisions

- Repeals the IRS's authority to prescribe a "form" for substantiating charitable contributions.
- Requires taxpayers to include the interest on advance refunding bonds in taxable income.



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QUESTIONS ?

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THANK YOU

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Biography



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Alexander L. Reid advises tax-exempt organizations in planning, structuring, and transactional matters. He also represents taxpayers under audit, and helps organizations improve their governance and enhance their tax compliance. Alexander counsels taxpayers seeking administrative guidance from the Internal Revenue Service (IRS) and US Department of the Treasury, as well as on legislative matters with the US Congress. His tax-exempt clients include charities, foundations, colleges and universities, museums, and other nonprofit organizations.

Biography



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Greg L. Needles counsels tax-exempt, governmental, and multinational employers on a range of complex employee benefit and executive compensation matters. He advises on establishing and terminating benefit plans, as well as plan administration issues involving ERISA, the Internal Revenue Code, the Affordable Care Act, COBRA, and HIPAA. He also advises on employment agreements and deferred compensation arrangements for executives.

Biography



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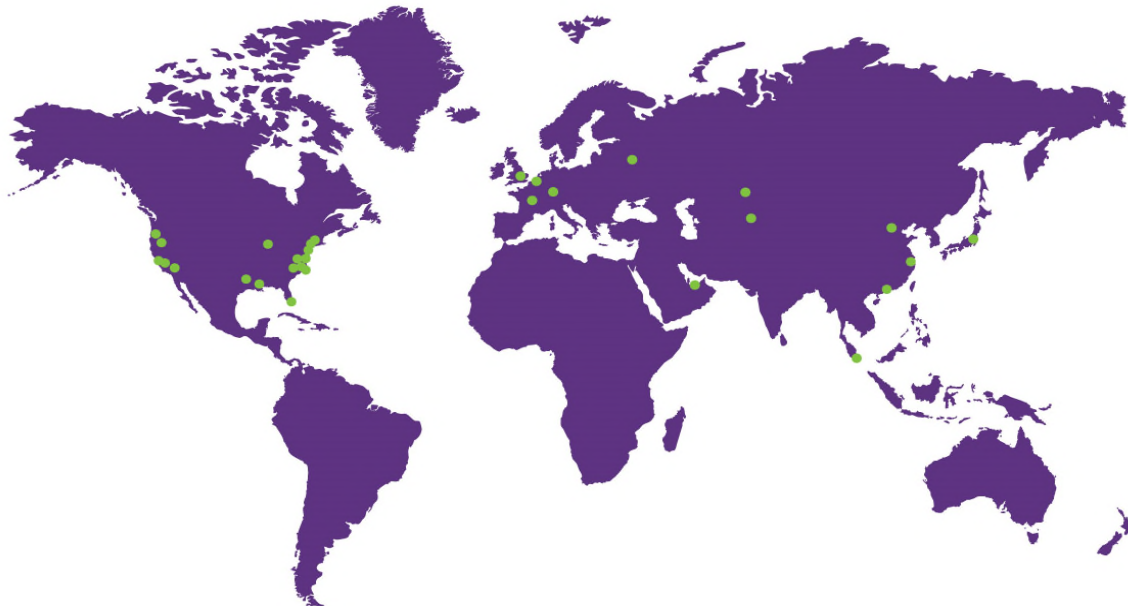
Kimberly Eney advises tax-exempt organizations on the tax and corporate laws integral to advancing their missions. In addition to helping private foundations navigate the Chapter 42 excise tax regime, she advises clients on issues involving unrelated business income tax implications, lobbying and political activity restrictions, intermediate sanctions rules and compensation-related issues, public charity classification and the public support test, applications for tax exemption, relationships with affiliated entities and disqualified persons, Form 990 filing issues, and state nonprofit corporation laws.

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