Tax Provisions in Administration's FY 2017 Budget Proposals

Compensation, Benefits, & Qualified Plans

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HIGHLIGHTS OF TAX PROPOSALS IN THE ADMINISTRATION'S FISCAL YEAR 2017 BUDGET RELATING TO COMPENSATION, BENEFITS, & QUALIFIED PLANS

KPMG has prepared a 103-page **book** that summarizes and makes observations about the revenue proposals in the administration's FY 2017 budget. For ease of reference, we have compiled our summaries and observations relating to certain specific industries and topics in separate booklets. This booklet highlights revenue proposals that relate to compensation, benefits, and qualified plans. Other booklets address proposals relating to other topics.

Background

President Obama on February 9, 2016, transmitted to Congress his fiscal year (FY) 2017 budget, containing the administration's recommendations to Congress for spending and taxation for the fiscal year that begins on October 1, 2016. Although it is not expected that Congress will enact—or even vote on—the president's budget as a whole, the budget represents the administration's view of the optimum direction of spending and revenue policy.

The budget would, according to the White House, reduce the deficit by $2.9 trillion over 10 years. More than $900 billion of that reduction would be attributable to changes in the taxation of capital gains and the reduction of tax benefits for upper income individuals. Reduction also would be achieved through changes in the taxation of international business income (which would raise almost $800 billion in new revenue over 10 years), and from other business tax changes (which would raise approximately $337 billion).

The president also proposes to impose a new fee on oil that would raise almost $320 billion over 10 years. That new revenue would be committed to investment in transportation information infrastructure as part of a multi-agency initiative to build a "clean" transportation system less reliant on carbon-producing fuels.

The budget also reiterates the president's goal of cutting the corporate tax rate and making structural changes and closing loopholes. In *The President's Framework for Business Tax Reform* (February 2012), he proposed cutting the corporate rate to 28%. The budget does not, however, provide sufficient revenue to offset the cost of such a rate reduction.

Business tax proposals

Many other tax proposals in the FY 2017 budget are familiar, having been included in previous budgets, such as:

- Reforms to the international tax system
- Limiting the ability of domestic entities to expatriate

- Repeal of natural resources production preferences
- Repeal of LIFO and LCM accounting
- Taxation of carried interests in partnerships as ordinary income
- Insurance industry reforms
- Marking financial derivatives to market and treating gain as ordinary income
- Modification of the depreciation rules for corporate aircraft
- Denying a deduction for punitive damages
- Imposing a tax on the liabilities of financial institutions with assets in excess of $50 billion

Some previous proposals have been modified significantly, such as expanding the types of property subject to a proposed change to the like-kind exchange rules.

In place of the current system of deferral of foreign earnings, the president is again proposing a minimum tax on foreign earnings above a risk-free return on equity invested in active assets. The minimum tax, imposed on a country-by-country basis, would be set at 19% less 85% of the per-country foreign effective tax rate. The new minimum tax would be imposed on a current basis, and foreign earnings could then be repatriated without further U.S. tax liability.

As part of the transition to the new system of taxation of foreign earnings, the budget would also impose a one-time 14% tax on earnings accumulated in CFCs that have not previously been subject to U.S. tax.

Individual (personal) tax revisions

As in the case of businesses, many of the individual (personal) tax proposals in the budget are familiar, including measures that generally would:

- Limit the tax value of certain deductions and exclusions to 28%
- Impose a new minimum tax (the so-called "Buffett Rule") of 30% of AGI
- Limit the total accrual of tax-advantaged retirement benefits
- Restore the estate, gift, and GST parameters to those in effect in 2009

Among the set of revisions proposed involves reforms to the taxation of capital gains for upper-income taxpayers, which would offset the cost of extension and expansion of tax preferences for middle- and lower-income taxpayers. The highest tax on capital gains would be increased from 23.8% (including the 3.8% net investment income tax) to 28%. In addition, the Green Book* indicates that a transfer of appreciated property would generally be treated as a sale of the property. Thus, the donor or deceased owner of an appreciated asset would be subject to capital gains tax on the excess of the asset's fair market value on the date of the transfer over the transferor's basis.

The budget also includes a proposal to expand the definition of net investment income to include gross income and gain from any trades or businesses of an individual that is not otherwise subject to employment taxes. The change would potentially affect limited partners and members of LLCs, as well as S corporation owners.

In response to concern that employees in employer-sponsored health plans might unfairly become subject to the Affordable Care Act's excise tax on high-cost plans because they reside in states where health care costs are higher than the national average, the president also proposes modifying the threshold for application of that tax.

Treasury's explanation

The Treasury Department on February 9 released an accompanying explanation of the tax proposals of the budget—Treasury's **Green Book*** [PDF 1.85 MB]—which describes those proposals in greater detail.

*General Explanation of the Administration's Fiscal Year 2017 Revenue Proposals

User's guide

$ = U.S. dollar
% = percent
PATH Act = Protecting Americans from Tax Hikes Act of 2015 (enacted December 18, 2015)
Green Book = Treasury's *General Explanation of the Administration's Fiscal Year 2017 Revenue Proposals*

Compensation, Benefits, & Qualified Plan Tax Proposals

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Employment Taxes

Rationalize Net Investment Income Tax (NIIT) and Self-Employment Contributions Act (SECA) Taxes

The NIIT and the SECA taxes impose a 3.8% tax on certain income and gain of individuals over a threshold amount. The threshold amounts are $200,000 (for single and head of household returns) and $250,000 (for joint returns). Individuals with incomes over these thresholds may currently be excluded from either of these taxes, however. For example, limited partners and S corporation shareholders who materially participate in their businesses may avoid both the SECA taxes and the NIIT on certain income and gains.

The proposal has two components and would be effective for tax years beginning after December 31, 2016. The first component is to amend the definition of net investment income to include income and gain from any trade or business of an individual that is not otherwise subject to SECA taxes. In other words, if an individual has trade or business income that is not subject to SECA because of certain exclusions from SECA, that income would treated as net investment income. The proposal would also cause gain on the sales of trade or business property to be included in the definition of net investment income. As under current law, the tax on net investment income would apply only to individuals with incomes over the thresholds. In addition, all revenue from the NIIT would be directed to the Medicare Hospital Insurance Trust Fund, just as is the revenue from the current 3.8% tax under FICA and SECA.

The second component is to treat individual owners of professional service businesses taxed as either S corporations or partnerships as subject to SECA taxes in the same way. Professional service businesses would be defined as partnerships and S corporations if substantially all of the activities involve the performance of services in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts, consulting, athletics, investment advice or management, brokerage services and lobbying.

Owners who materially participate in the trade or business would be subject to the SECA taxes on their distributive shares of S corporation or partnership income. The current exemptions from SECA (for rents, dividends, capital gains, and certain retired partner income) would continue to apply. Owners who do not materially participate in the trade or business would be subject to SECA only on the "reasonable compensation" for their services, including guaranteed payments for services. Finally, distributions of compensation to owners of S corporations and partnerships would no longer be treated as wages subject to FICA but would be included in earnings subject to SECA taxes.

Make unemployment insurance surtax permanent

The Federal Unemployment Tax Act (FUTA) currently imposes a federal payroll tax on employers of 6% of the first $7,000 paid annually to each employee. This tax funds a portion of the federal / state unemployment benefits system. States also impose an unemployment tax on employers. Employers in states that meet certain federal requirements are allowed a credit for state unemployment taxes of up to 5.4%, making the minimum net federal tax rate 0.6%.

Before July 1, 2011, the federal payroll tax had included a temporary surtax of 0.2%, which was added to the permanent FUTA tax rate. The surtax had been extended several times since its enactment in 1976, but it expired on July 1, 2011.

The administration's FY 2017 proposal would reinstate the 0.2% surtax and make it permanent.

The provision would be effective for wages paid after December 31, 2016.

Expand Federal Unemployment Tax Act (FUTA) base and reform FUTA credit reduction rules

The administration's FY 2017 proposal would raise the FUTA wage base in 2018 to $40,000 per worker paid annually, index the wage base to wage growth for subsequent years, and reduce the net Federal UI tax from 0.8% (after the proposed permanent reenactment and extension of the FUTA surtax) to 0.167%. States with wage bases below $40,000 would need to conform to the new FUTA base in order to receive the full FUTA credit. The provision would impose a minimum tax rate requirement on states for their state employer tax rates equivalent to roughly $70 per employee beginning in 2018.

The provision would be effective upon the date of enactment.

Increase certainty with respect to worker classification

Under a special non-Code provision (*Section 530 of the Revenue Act of 1978*), the IRS is prohibited from reclassifying an independent contractor to employee status, even when the worker may be an employee under the common law rules, if the service recipient has a reasonable basis for treating the worker as an independent contractor and certain other requirements are met. In addition to providing so-called "Section 530 relief" to service recipients, the 1978 legislation prohibited the IRS from issuing guidance addressing the proper classification of workers.

The administration's FY 2017 proposal would allow the IRS to require service recipients to prospectively reclassify workers who are currently misclassified. It is anticipated that, after enactment, new enforcement activity would focus mainly on obtaining the proper worker classification prospectively, since in many cases, the proper classification of workers may have been unclear. In addition, the proposal would lift the prohibition on worker classification guidance, with Treasury and the IRS being directed to issue guidance that: (1) interprets the common law in a neutral manner; and (2) provides narrow safe harbors and/or rebuttable presumptions. Service recipients would be required to give notice to independent contractors explaining how they will be classified and the implications of such classification. Independent contractors receiving payments totaling $600 or more in a calendar year from a service recipient would be permitted to require the service recipient to withhold federal income tax from their gross payments at a flat rate percentage selected by the contractor. The proposal would also clarify rules with respect to Tax Court jurisdiction in relevant proceedings and make technical and conforming changes to those rules.

The provision (included in previous budget proposals) would be effective upon enactment, but prospective reclassification of those workers covered by Section 530 would not be effective until the first calendar year beginning at least one year after the date of enactment. The transition period could be up to two years for independent contractors with existing written contracts establishing their status.

KPMG observation

This proposal could result in a significant increase in costs and burdens on U.S. businesses that have service providers currently classified as independent contractors. The reclassification to employee status may have wide-spread implications outside of federal employment taxes and affect such matters as workers compensation, unemployment benefits, pension requirements, and state employment taxes.

This provision was included in the administration's FY 2015 and 2016 revenue proposals.

Limit Value of Exclusions and Deductions for Certain Benefits and Contributions

The administration's FY 2017 proposal would limit the tax value of certain specified deductions and exclusions from AGI, and all itemized deductions. This limitation would reduce to 28% the value of these deductions and exclusions that would otherwise reduce taxable income in the 33%, 35%, or 39.6% tax brackets. A similar limitation would apply under the alternative minimum tax.

The income exclusions and deductions limited by this provision include any tax-exempt state and local bond interest, employer-sponsored health insurance paid for by employers or from pre-tax employee income, health insurance costs of self-employed individuals, employee contributions to defined contribution retirement plans and individual retirement arrangements, the deduction for income attributable to domestic production activities, certain trade and business deductions of employees, moving expenses, contributions to health savings accounts (HSAs) and Archer medical savings accounts (MSAs), and interest on education loans.

This proposal would apply to itemized deductions after they have been reduced by the statutory limitation on itemized deductions for higher income taxpayers.

Treasury's Green Book does not describe in detail the mechanics of the proposed 28% limitation. In principle, however, taxpayers in the 39.6% tax bracket with a $10,000 itemized deduction or exclusion would be able to reduce their tax liability by only $2,800 on account of the deduction or exclusion, rather than $3,960—a tax increase of $11.60 per $100 of itemized deductions compared with current law.

This provision would be effective for tax years beginning after December 31, 2016.

Qualified Plans

Provide for automatic enrollment in IRAs, including a small employer tax credit, increase the tax credit for small employer plan start-up costs, and provide an additional tax credit for small employer plans newly offering auto-enrollment

The administration's FY 2017 budget proposal would require employers in business for at least two years that have more than 10 employees to offer an automatic IRA option to employees. Contributions would be made to an IRA on a payroll-deduction basis. If the employer sponsors a qualified plan, it would not be required to provide an automatic IRA. However, if the employer excluded from eligibility a portion of the workforce or class of employees, the employer would be required to offer the automatic IRA option to those excluded employees.

Small employers (those with no more than 100 employees) that offer an automatic IRA arrangement could claim a temporary non-refundable credit for expenses associated with the arrangement of up to $1,000 per year for three years. Such employers would be entitled to an additional non-refundable credit of $25 per enrolled employee, up to a maximum of $250, for six years. The credit would be available both to employers required to offer automatic IRAs and employers not required to do so (e.g., because they have 10 or fewer employees).

In addition, the "start-up costs" tax credit for a small employer that adopts a new qualified retirement, SEP, or SIMPLE plan would be tripled from the current maximum of $500 per year for three years to a maximum of $1,500 per year for three years and extended to four years (rather than three) for any employer that adopts a new qualified plan, SEP, or SIMPLE during the three years beginning when it first offers (or first is required to offer) an automatic IRA arrangement. This credit would not apply to the automatic IRAs.

Small employers would be allowed a credit of $500 per year for up to three years for new plans that include auto enrollment (this is in addition to the "start-up costs" credit of $1,500 per year). Small employers would also be allowed a credit of $500 per year for up to three years if they add auto enrollment as a feature to an existing plan.

The provision would be effective after December 31, 2017.

Expand penalty-free withdrawals for long-term unemployed

The administration's FY 2017 proposal would expand the exception from the 10% additional tax for early withdrawal from a qualified retirement plan to include distributions to certain long-term unemployed individuals from an IRA, 401(k), or other tax-qualified defined contribution plan.

The provision would apply to eligible distributions occurring after December 31, 2016.

Require retirement plans to allow long-term part-time workers to participate

The administration's FY 2017 proposal would require section 401(k) plans to expand participation eligibility to employees who worked at least 500 hours per year, for at least three consecutive years, with the employer. Employers would receive nondiscrimination testing relief, including permission to exclude these employees from top-heavy vesting and top-heavy benefit requirements after expanding the eligibility group.

This provision would apply to plan years beginning after December 31, 2016.

Facilitate annuity portability

The administration's FY 2017 budget proposal would permit a plan to allow participants to take a distribution of a lifetime income investment through a direct rollover to an IRA or other retirement plan if the annuity investment is no longer authorized to be held under the plan. The distribution would not be subject to the 10% additional tax.

The provision would be effective for plan years beginning after December 31, 2016.

Simplify minimum required distribution (MRD) rules

The administration's FY 2017 budget proposal would exempt an individual from the MRD requirements if the aggregate value of the individual's IRA and tax-favored retirement plan accumulations does not exceed $100,000 on the measurement date. However, benefits under qualified benefit pension plans that have begun to be paid in life annuity form would be excluded. The MRD requirements would phase-in ratably for individuals with aggregate retirement benefits between $100,000 and $110,000.

The administration's FY 2017 proposal would harmonize the application of the MRD requirements for holders of designated Roth accounts and Roth IRAs by generally treating Roth IRAs in the same manner as all other tax-favored retirement accounts, i.e., requiring distributions to begin shortly after age 70½ years. Individuals would not be permitted to make additional contributions to Roth IRAs after they reach age 70½ years.

The provisions would be effective for individuals attaining age 70½ after December 31, 2016, and for taxpayers who die on or after December 31, 2016 before attaining age 70½ years.

Allow all inherited plan and IRA balances to be rolled over within 60 days

The administration's FY 2017 proposal would expand the option available to a surviving non-spouse beneficiary under a tax-favored employer retirement plan or IRA for moving inherited-plan or IRA assets by allowing 60-day rollovers of such assets.

The provision would be effective for distributions made after December 31, 2016.

Permit unaffiliated employers to maintain a single multiple-employer defined contribution plan

The administration's FY 2017 budget proposal would amend ERISA to permit unaffiliated employers to adopt a defined contribution multiple-employer plan (MEP) that would be treated as a single plan for ERISA purposes, even though the employer may not have a commonality of interests.

Unaffiliated employers eligible to participant in such a MEP would be employers that had not maintained a qualified plan within the previous three years. The provider would be required to be a regulated financial institution and agree to be a named fiduciary of the plan and the plan administrator. The provider would be required to register with the Secretary of Labor before offering the plan to employers. Each participating employer would retain fiduciary responsibility for selecting and monitoring the provider. Employers would be responsible for transmitting employee contributions to the trustee within a specified time frame.

The provision would be effective for years beginning after December 31, 2016.

KPMG observation

Similar to the auto-enrolled employer IRAs in the administration's FY 2017 proposal, this provision is meant to encourage greater participation in retirement programs by smaller employers.

Require non-spouse beneficiaries of deceased IRA owners and retirement plan participants to take inherited distributions over no more than five years

Under the administration's FY 2017 proposal, non-spouse beneficiaries of retirement plans and IRAs would generally be required to take distributions over no more than five years. Exceptions would be provided for eligible beneficiaries, including any beneficiary who, as of the date of the account holder's death, is: (1) disabled; (2) a chronically ill individual; (3) an individual who is not more than 10 years younger than the participant or IRA owner; or (4) a child who has not reached the age of majority. For these beneficiaries, distributions would be allowed over the life or life expectancy of the beneficiary beginning in the year following the year of the death of the participant or owner, except that in the case of a child, the account would need to be fully distributed no later than five years after the child reaches the age of majority.

According to the Green Book, any balance remaining after the death of a beneficiary (including an eligible beneficiary excepted from the five-year rule or a spouse beneficiary) would be required to be distributed by the end of the calendar year that includes the fifth anniversary of the beneficiary's death.

The proposal generally would apply to distributions with respect to plan participants or IRA owners who die after December 31, 2016. However, the requirement that any balance remaining after the death of a beneficiary be distributed by the end of the calendar year that includes the fifth anniversary of the beneficiary's death would apply to participants or IRA owners who die before January 1, 2016, if the beneficiary dies after December 31, 2016. The proposal would not apply in the case of a participant whose benefits are determined under a binding annuity contract in effect on the date of enactment.

Limit the total accrual of tax-favored retirement benefits

Under the administration's FY 2017 proposal, a taxpayer who has accumulated amounts within the " tax-favored retirement system" (i.e., IRAs, section 401(a) plans, section 403(b) plans, and funded section 457(b) arrangements maintained by governmental entities) in excess of the amount necessary to provide the maximum annuity permitted for a tax-qualified defined benefit plan under current law (currently an annual benefit of $210,000 payable in the form of a 100% joint and survivor benefit commencing at age 62 and continuing each year for the life of the participant and, if later, the life of the participant's spouse) would be prohibited from making additional contributions or receiving additional accruals under any of those arrangements. Currently, the maximum permitted accumulation for an individual age 62 years is approximately $3.4 million.

According to the Green Book, the limitation would be determined as of the end of a calendar year and would apply to contributions or accruals for the following calendar year. Plan sponsors and IRA trustees would report each participant's account balance as of the end of the year as well as the amount of any contribution to that account for the plan year. For a taxpayer who is under age 62, the accumulated account balance would be converted to an annuity payable at age 62, in the form of a 100% joint and survivor benefit using the actuarial assumptions that apply to converting between annuities and lump sums under defined benefit plans. For a taxpayer who is older than age 62, the accumulated account balance would be converted to an annuity payable in the same form, when actuarial equivalence is determined by treating the individual as if he or she was still age 62; the maximum permitted accumulation would continue to be adjusted for cost of living increases. Plan sponsors of defined benefit plans would report the amount of the accrued benefit and the accrual for the year, payable in the same form.

The Green Book also explains that if a taxpayer reached the maximum permitted accumulation, no further contributions or accruals would be permitted, but the taxpayer's account balance could continue to grow with investment earnings and gains. If a taxpayer received a contribution or an accrual that would result in an accumulation in excess of the maximum permitted amount, the excess would be treated in a manner similar to the treatment of an excess deferral under current law.

The provision would be effective with respect to contributions and accruals for tax years beginning after December 31, 2016.

Limit Roth conversions to pre-tax dollars

The administration's FY 2017 proposal would permit amounts held in a traditional IRA to be converted to a Roth IRA (or rolled over from a traditional IRA to a Roth IRA) only to the extent a distribution of those amounts would be includable in income if they were not rolled over. After-tax amounts (those attributable to basis) held in a traditional IRA could not be converted to Roth amounts. A similar rule would apply to amounts held in eligible retirement plans.

The proposal would apply to distributions occurring after December 31, 2016.

Eliminate deduction for dividends on stock of publicly traded corporations held in employee stock ownership plans

The administration's FY 2017 proposal would repeal the deduction for dividends paid with respect to employer stock held by an ESOP that is sponsored by a publicly traded corporation. Rules allowing for immediate payment of an applicable dividend would continue, as would rules permitting the use of an applicable dividend to repay a loan used by the ESOP to purchase the stock of the publicly traded corporation. The Secretary would continue to have authority to disallow an unreasonable dividend or distribution (as described in section 1368(a)) for this purpose.

The proposal would apply to dividends and distributions that are paid after the date of enactment.

Repeal exclusion of net unrealized appreciation in employer securities

The administration's FY 2017 proposal would repeal the exclusion of net unrealized appreciation in employer stock in the year of a distribution for participants in tax- qualified retirement plans who have not yet attained age 50 as of December 31, 2016. Participants who have attained age 50 on or before December 31, 2016 would not be affected by the provision.

The provisions would apply to distributions made after December 31, 2016.

Require Form W-2 reporting for employer contributions to defined contribution plans

Employers file Form W-2 to provide to each employee an annual statement showing the remuneration paid by the employer to the employee during the calendar year. A copy of the Form W-2 must also be filed with the Social Security Administration, which shares information on the form with the IRS. Employers are required to report an employee's elective deferrals under a cash or deferred arrangement, such as contributions to a 401(k) plan, on the employee's Form W-2. Employers are not currently required to report the employer's contributions to an employee's defined contribution retirement plan on the employee's Form W-2.

The administration's FY 2017 proposal would require employers to report the amounts an employer contributed to an employee's accounts under a defined contribution plan on the employee's Form W-2.

The proposal (included in previous budget proposals) would be effective for information returns due for calendar years beginning after December 31, 2016.

Employment-Related Tax Credits

Expand and simplify the tax credit provided to qualified small employers for non-elective contributions to employee health insurance

Substantially similar to last year's proposal, the administration's FY 2017 proposal would expand the group of employers that are eligible for this credit to include employers with up to 50 full-time equivalent employees, and would begin the phase-out at 20 full-time equivalent employees. In addition, the coordination of the phase-outs between the number of employees and the average wage would be amended to provide for a more gradual combined phase-out. The proposal also would eliminate a requirement that the employer make a uniform contribution on behalf of each employee, and eliminate the limit imposed by the rating area average premium.

The provision would be effective for tax years beginning after December 31, 2015.

Extend and modify certain employment tax credits, including incentives for hiring veterans

The Work Opportunity Credit (WOTC), which allows a credit to employers for the first-year wages paid to employees in targeted groups, would be made permanent, past its current reach of applying to employees who begin work before January 1, 2020. The targeted group of qualified veterans would be expanded for individuals who begin work after 2016 to include disabled veterans who use G.I. Bill benefits for training within one year after discharge, who are hired within six months after ending their training. The first $12,000 of wages paid these veterans would be eligible for the WOTC.

A credit allowed for wages paid to individuals who are members of Indian tribes (and their spouses) and who, generally, live and work on a reservation, would be made permanent, past its current termination at the end of 2016. In tax years after 2016, the credit would be 20% of the amount of qualified wages and health insurance costs for an employee in excess of the average amount for the two preceding tax years.

Repeal Federal Insurance Contributions Act (FICA) tip credit

The administration's FY 2017 proposal would repeal the income tax credit for FICA taxes an employer pays on tips. Currently, tip income is treated as employer-provided wages subject to employment taxes under FICA. Employers are responsible for withholding and reporting the employee's portion of FICA and paying the employer's portion of FICA. An eligible employer may claim a credit against the business's income taxes for FICA taxes paid on certain tip wages.

The provision would apply for tax years beginning after December 31, 2016.

Other

Improve the excise tax on high cost employer-sponsored health coverage

The administration's FY 2017 budget proposal would modify section 4980I—the excise tax on high cost employer-sponsored health coverage enacted in 2010 as part of the Patient Protection and Affordable Care Act. The administration's FY 2017 budget proposal would raise the threshold at which health plans are subject to the tax in states with higher health-care costs. Specifically, the proposal would modify the threshold above which the tax applies to be equal to the greater of the current law threshold ($10,200 for individual coverage and $27,500 for family coverage, in 2018 dollars) or the average premium for a gold-level health plan in the employees' state of residency.

In addition, the proposal would provide that the cost of coverage under a health flexible spending arrangement (FSA) for similarly situated participating employees is equal to the sum of: (1) the average salary reduction amount elected by those employees for the year; and (2) the average employer contribution for such employees for the year. Furthermore, the proposal would authorize the Secretary of the Treasury to issue guidance identifying similarly situated employees.

Finally, the proposal would require the Government Accountability Office to conduct a study of the potential effects of the excise tax on firms with unusually sick employees, in consultation with Treasury and others. The provision would be effective for tax years beginning after December 31, 2016. However, as under current law, no employer-sponsored health plans would be subject to the tax until 2020.

KPMG observation

This is a new budget proposal designed to lessen the effects of the excise tax on high cost employer-sponsored health coverage (often referred to as the "Cadillac tax") in geographic areas where health care costs are higher than the national average. Furthermore, the proposal appears to be intended to make it easier for employers offering FSAs to calculate the excise tax owed by providing a formula for measuring the cost of coverage under an FSA.

The effective date of the tax was postponed until 2020 through legislation enacted in December 2015, and legislative proposals have been introduced by members of Congress to repeal the excise tax entirely.

Contact us

Karen Field
Washington National Tax
Principal in Charge
Compensation and Benefits
T: 202-533-4234
E: kfield@kpmg.com

Terri Stecher
Washington National Tax
Director
Compensation and Benefits
T: 202-533-4830
E: tstecher@kpmg.com

John Gimigliano
Washington National Tax
Principal in Charge
Federal Legislative and Regulatory Services
T: 202-533-4022
E: jgimigliano@kpmg.com

kpmg.com/socialmedia

kpmg.com/app

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