A “20/20” Look at the 2017 Tax Act

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Gil Ghatan, Ropes & Gray LLP
Chelsea Rubin, Morgan, Lewis and Bockius LLP
Robert A. Wexler, Adler & Colvin

These materials were prepared without input or review from any government speaker. They reflect the views of the authors only.
This panel will discuss any newly released guidance impacting tax exempt organizations. Time permitting, the panel may also discuss interesting developments under the Department of Treasury and Internal Revenue Service 2019-2020 Priority Guidance Plan.
Section 512(a)(6): Special rule for organizations with more than 1 unrelated trade or business

Section 512(a)(6), introduced by the Tax Cuts and Jobs Act (P.L. 115-97), requires a tax-exempt organization to compute unrelated business taxable income (“UBTI”) separately for each unrelated trade or business, effective for tax years beginning after December 31, 2017. The rule generally prevents tax-exempt organizations from offsetting UBTI generated by a profitable unrelated trade or business with a loss from an unprofitable one. However, the statute did not define the scope of the activities that could be grouped together as a single unrelated trade or business.

Notice 2018-67, 2018-36 IRB 409, provides the first published guidance on section 512(a)(6). (See Supplement 1)

- Permits tax-exempt organizations to “rely on a reasonable, good-faith interpretation” of sections 511-514 in determining whether they have more than one unrelated trade or business, pending issuance of proposed regulations. A good-faith interpretation must consider all the facts and circumstances.
- IRS will consider an organization’s groupings of activities to be reasonable and in good faith if the organization uses the six-digit North American Industry Classification System (NAICS) – a standard used by federal agencies to classify businesses for statistical purposes, already used by the Form 990-T.
- Interim and Transition Rules for Partnership Interests
  - Interim Rule: Until proposed regulations are issued, a tax-exempt organization may treat a “qualifying partnership interest” as a single trade or business and may further aggregate all of its qualifying partnership interests as a single trade or business. This is true even if the partnership is engaged, directly or indirectly, in multiple trades or businesses. A partnership interest must meet either a \textit{de minimis} or a control test to be a qualifying partnership interest.
    - \textit{De minimis} test: Tax-exempt organization holds directly no more than 2 percent of the profits interest and no more than 2 percent of the capital interest in the partnership. If no specific profits interest is identified on Schedule K-1, the \textit{de minimis} test is not met.
    - Control test: Tax-exempt organization holds no more than 20 percent of the capital interest in and, based on all the facts and circumstances, does not have control or influence over the partnership.
    - Under both tests, interests held by a disqualified person (within the meaning of section 4958), a supporting organization or a controlled entity in the same partnership will be considered in determining the tax-exempt organization’s percentage interest.
  - Transition Rule: A tax-exempt organization may treat a partnership interest acquired before August 21, 2018 (when Notice 2018-67 was released) as constituting a single trade or business, even if the partnership conducts more than one trade or business.
• A tax-exempt organization may aggregate unrelated debt-financed income from a qualifying partnership interest with other UBTI from its qualifying partnership interests, and may aggregate unrelated debt-financed income from a partnership interest that satisfies the transition rule with other UBTI from that partnership interest.

• Comments requested on:
  ° Use of NAICS codes to identify separate trades or businesses
  ° Standard for identifying partnerships in which an organization does not significantly participate
  ° NOL ordering rules
  ° Any other issues discussed in the Notice

• ABA submitted comments on December 4, 2018 (see Supplement 2)
• Ropes & Gray LLP alert on Notice 2018-67 (see Supplement 3)
Section 4960: Tax on excess tax-exempt organization executive compensation

Section 4960, also introduced by the Tax Cuts and Jobs Act (P.L. 115-97), imposes an excise tax equal to the corporate tax rate (currently, 21 percent) on certain tax-exempt organizations (“applicable tax-exempt organizations” or “ATEOs”) and related organizations that pay excess compensation to employees of the ATEO. The excise tax generally applies if, during the taxable year, the ATEO pays remuneration in excess of $1 million or any “excess parachute payment” to any of the ATEO’s employees who are among the five highest paid for the current year and any prior taxable year beginning after December 31, 2016 (“covered employees”). Compensation paid by any related organization to an ATEO employee is taken into account in determining whether such employee is a covered employee and in determining total compensation subject to the excise tax.

Notice 2019-9, 2019-4 IRB 403, provides the first published guidance on section 4960. (See Supplement 4)

- Permits employers to base their positions with respect to the excise tax on a good faith, reasonable interpretation of section 4960. Positions reflected in the Notice constitute a good faith, reasonable interpretation of section 4960.
- The Notice provides clarification for many of the definitional ambiguities created by the statute, including the following:
  - **Taxable year**: The period for measuring remuneration paid and parachute payments is the calendar year that ends with or within the taxable year of the employer.
  - **Government entities**: Government entities that are not recognized as tax exempt under section 501(a) and those that do not exclude income under section 115(1) are not ATEOs, meaning that certain state colleges and universities may not be ATEOs subject to section 4960.
  - **Related organizations – control**: The excise tax is triggered by compensation paid not only by the ATEO but also by any related organization, which is defined as a person or government entity that (1) controls or is controlled by the ATEO, (2) is controlled by one or more persons that control the ATEO, (3) is a supported or supporting organization of the ATEO, or (4) in the case of a voluntary employees’ beneficiary association (VEBA), that establishes, maintains or makes contributions to the VEBA. To establish control, the Notice applies the greater than 50 percent control threshold from the unrelated business income tax rules for payments from controlled entities.
  - **Related organizations – for-profit and government entities**: For-profit and government entities can be considered related organizations for purposes of determining whether an ATEO employee is a covered employee and whether such employee receives excess remuneration or an excess parachute payment, and related organizations are liable for their proportionate share of any resulting excise tax based on the portion of the employee’s total compensation paid by each related organization.
  - **Covered employee**: Only an ATEO has covered employees, and, per the Notice, only common law employees (including officers) can be covered employees. An employee
need not be paid excess remuneration or an excess parachute payment during a taxable year to be treated as a covered employee. Once an ATEO employee is a covered employee, he or she will always be a covered employee of such ATEO, with no expiration date.

- ATEOs need to keep track of their covered employees at all times, even if there is no excess remuneration or excess parachute payments in a given year, as the excise tax could be triggered in a future year. Over time, this may become increasingly likely, as the $1 million threshold for excess remuneration is not indexed for inflation.

- Using a common law employee definition for determining ATEO employees may inadvertently treat as covered employees individuals that provide services to an ATEO on a volunteer basis, such as employees of a company serving as volunteer officers or otherwise providing services to a related company foundation.

  - **Limited services exception:** The Notice excludes from an ATEO’s covered employees certain employees of an ATEO and related organizations, if the ATEO pays a small portion of the employee’s total remuneration. Under this rule, an ATEO employee is not treated as one of the ATEO’s five highest-compensated employees unless the ATEO pays at least 10 percent of the total remuneration paid by the ATEO and all related organizations to the employee during the year. If no ATEO pays at least 10 percent of an employee’s total remuneration during the year, this exception does not apply to the ATEO that paid the most remuneration to the employee during the year.

  - **Medical services exception:** Remuneration paid to a licensed medical professional (including a veterinarian) for the performance of medical or veterinary services by such professional is disregarded for purposes of determining whether excess remuneration or excess parachute payments have been paid. The Notice clarifies that such remuneration is also excluded when determining an ATEO’s covered employees. The Notice indicates that administrative, teaching, and research services generally are not considered medical services for purposes of the exception and provides rules for allocating time spent by medical professionals between medical and non-medical services. The employer must make a reasonable, good faith allocation of such services, and if any remuneration allocation is set forth in an employment agreement or similar written arrangement, such allocation must be used to the extent the amount allocated to medical services is not unreasonable.

  - **Remuneration:** Remuneration for purposes of section 4960 is not limited to amounts reported on IRS Form W-2 in boxes 1 or 5. Remuneration is treated as paid when it is no longer subject to a substantial risk of forfeiture (i.e., when it vests), using the definition in proposed Treasury Regulations under section 457(f), regardless of whether the arrangement is subject to section 457(f) or section 409A. Under this definition, compensation is subject to a substantial risk of forfeiture only if it is conditioned on the performance of substantial future services or if it is conditioned upon the occurrence of a condition related to a purpose of the compensation and the possibility of forfeiture is substantial. The amount of remuneration treated as paid when such remuneration ceases to be subject to a substantial risk of forfeiture is the present value of such remuneration, determined using reasonable actuarial
assumptions. Subsequent earnings on such amounts are treated as paid at the end of the calendar year in which they accrue.

- **Excess parachute payment:** The excise tax is imposed on an excess parachute payment, which is defined as any payment in the nature of compensation made by an ATEO or a related organization to a covered employee if (1) the payment is contingent on the employee’s separation from employment with the employer and (2) the aggregate present value of the parachute payments equals or exceeds an amount equal to three times the “base amount” (generally, an employee’s average annual compensation over the most recent five-year period). The Notice emphasizes that an excess parachute payment equals the excess of the parachute payment over the base amount (i.e., not only on the portion of the payment in excess of three times the base amount).

- ABA submitted comments on July 12, 2019 (see Supplement 5)
- Ropes & Gray LLP alert on Notice 2019-9 (see Supplement 6)
The latest Priority Guidance Plan (“PGP”), released October 8, 2019 (see Supplement 7) sets forth the Department of Treasury’s and the Internal Revenue Service’s guidance priorities for the next fiscal year. In addition to nine items specifically included under the Exempt Organization’s section, four items of special relevance to tax-exempt organizations are listed under the implementation of the Tax Cuts and Jobs Act section.

PART 1. IMPLEMENTATION OF TAX CUTS AND JOBS ACT (TCJA)

24. Regulations under §274 concerning qualified transportation fringes, including the application of § 512(a)(7), and other issues under §274.
   - Presumably this guidance is being adjusted to account for the retroactive revocation of section 512(a)(7) as enacted by the Further Consolidated Appropriations Act, 2020 (P.L. 116-94).

29. Regulations on computation of unrelated business taxable income for separate trades or businesses under §512(a)(6), as added by section 13702 of the TCJA.

49. Regulations under §4960, as added by section 13602 of the TCJA.

50. Final regulations on the excise tax on net investment income of certain private colleges and universities under §4968, as added by section 13701 of the TCJA. Proposed regulations were published on July 3, 2019.

PART 6. GENERAL GUIDANCE: EXEMPT ORGANIZATIONS


2. Guidance on circumstances under which an LLC can qualify for recognition under §501(c)(3).

3. Final regulations on §506, as added by the PATH Act of 2015. Temporary and proposed regulations were published on July 12, 2016.
   - PUBLISHED 07/23/19 in FR as TD 9873.

4. Final regulations on §509(a)(3) supporting organizations. Proposed regulations were published on February 19, 2016.

5. Guidance under §4941 regarding a private foundation's investment in a partnership in which disqualified persons are also partners.

6. Regulations regarding the excise taxes on donor advised funds and fund management.

7. Regulations and other guidance under §6033.
   - PUBLISHED 09/10/2019 in FR as REG-102508-16 (NPRM).

8. Final regulations under §6104(c). Proposed regulations were published on March 15, 2011.

9. Final regulations designating an appropriate high-level Treasury official under §7611. Proposed regulations were published on August 5, 2009.
Part III - Administrative, Procedural, and Miscellaneous

Request for Comments Regarding the Calculation of Unrelated Business Taxable Income under § 512(a)(6) for Exempt Organizations with More than One Unrelated Trade or Business; Interim and Transition Rules for Aggregating Certain Income in the Nature of Investments; and the Treatment of Global Intangible Low-Taxed Income Inclusions for Purposes of the Unrelated Business Income Tax

Notice 2018-67

SECTION 1. PURPOSE

Section 13702 of “An Act to provide for reconciliation pursuant to titles II and IV of the concurrent resolution on the budget for fiscal year 2018,” Public Law 115-97 (131 Stat. 2054 (2017)) (the Act), enacted December 22, 2017, added new § 512(a)(6) to the Internal Revenue Code (Code). Section 512(a)(6) requires an organization subject to the unrelated business income tax under § 511, with more than one unrelated trade or business, to calculate unrelated business taxable income (UBTI) separately with respect to each trade or business. This notice discusses, and solicits comments regarding, various issues arising under § 512(a)(6) and sets forth interim guidance and transition rules relating to that section. This notice also provides guidance on the treatment of
global intangible low-taxed income (GILTI) under § 951A for purposes of the unrelated business income tax under § 511.

The contents of this notice are as follows. Section 2 provides a general background of the law on UBTI and § 512(a)(6). Section 3 outlines general concepts for identifying separate trades or businesses for purposes of § 512(a)(6) and provides interim reliance on a reasonable, good-faith standard for making such a determination. Section 4 discusses the possible treatment of income described in § 512(b)(4), (13), and (17). Section 5 discusses general principles surrounding income from partnerships. Section 6 sets forth interim and transition rules under § 512(a)(6) for aggregating income from partnerships and debt-financed income from partnerships. Section 7 discusses the application of § 512(a)(6) to certain organizations subject to the UBTI rules of § 512(a)(3). Section 8 discusses the effect of § 512(a)(6) on income described in § 512(a)(7) (fringe benefits). Section 9 provides information on how to calculate net operating losses (NOLs) within the framework of § 512(a)(6). Section 10 concludes that, for purposes of calculating UBTI, an inclusion of GILTI is treated as a dividend and follows the treatment of dividends under § 512(b)(1) and 512(b)(4). Section 11 summarizes reliance on rules provided in this notice. Section 12 requests comments and provides information for submitting comments.

SECTION 2. BACKGROUND

Under § 501(a), organizations described in §§ 401(a) and 501(c) generally are exempt from federal income taxation. However, § 511(a)(1) imposes a tax (computed
as provided in § 11) on the UBTI of organizations described in § 511(a)(2), which includes organizations described in §§ 401(a) and 501(c) (other than a trust described in § 511(b) or an instrumentality of the United States described in § 501(c)(1)) as well as state colleges and universities. Additionally, § 511(b)(1) imposes a tax (computed as provided in § 1(e)) on the UBTI of certain trusts described in § 511(b)(2).¹ Organizations described in § 511(a)(2) and trusts described in § 511(b)(2) are collectively called “exempt organizations” throughout this notice, unless otherwise stated.

Section 512(a)(1) defines UBTI as the gross income derived by any exempt organization from an unrelated trade or business regularly carried on by it, less the deductions allowed by Chapter 1 that are directly connected with the carrying on of such trade or business, both computed with the modifications described in § 512(b). An exempt organization determines whether it has income from an unrelated trade or business under the general principles of §§ 511 through 514 and the Treasury regulations thereunder.

Section 513(a) defines “unrelated trade or business” as any trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or

¹ Section 408(e) states that an individual retirement account (IRA) is subject to the taxes imposed by § 511. Accordingly, any reference to an exempt organization in this notice includes an IRA, without regard to whether it is a traditional IRA, Roth IRA, simplified employee pension (SEP-IRA), or savings incentive match plans for employees (SIMPLE IRA).
performance by such exempt organization, other than trusts described in § 513(b)(2), of its charitable, educational, or other purpose or function constituting the basis for its exemption under § 501 (or, in the case of a state college or university, to the exercise or performance of any purpose or function described in § 501(c)(3)). In the case of a trust that is exempt from tax under § 501(a) and described in § 401(a) (qualified retirement plans) or § 501(c)(17) (supplemental unemployment compensation benefits trusts (SUBs)), however, § 513(b) defines “unrelated trade or business,” as any trade or business regularly carried on by such trust or by a partnership of which it is a member.

An exempt organization may conduct an unrelated trade or business directly or indirectly through another entity, such as a partnership (including any entity treated as a partnership for federal tax purposes). Section 512(c) provides that, if a trade or business regularly carried on by a partnership of which an exempt organization is a partner is an unrelated trade or business with respect to such organization, the exempt organization includes in UBTI – subject to the exceptions, additions, and limitations of § 512(b) – its distributive share of partnership gross income (whether or not distributed) and partnership deductions directly connected with such gross income. See § 1.512(c)-1 (describing how UBTI is calculated in a situation in which an exempt organization’s distributive share of partnership income consists of both UBTI and income that is excluded from the calculation of UBTI). In determining whether a partnership conducts one or more trades or businesses that are unrelated trades or businesses with respect to an exempt organization partner, the exempt organization would use the applicable
definition of “unrelated trade or business” in § 513(a) or (b).\(^2\) Section 512(c) applies regardless of whether an exempt organization is a general or limited partner. Rev. Rul. 79-222, 1979-2 C.B. 236.

Except as described in § 512(a)(3) (discussed in section 7 of this notice), exempt organizations exclude from the calculation of UBTI gross income from dividends, interest, annuities, etc.; royalties; rents; and gains and losses from the sale, exchange, or other disposition of property. See § 512(b)(1), (2), (3), & (5). The reason that these and “similar items” are excluded from UBTI is because Congress indicated that such items “are not likely to result in serious competition for taxable businesses having similar income.” S. Rep. No. 81-2375, at 30-31 (1950). Additionally, Congress stated that “investment-producing incomes of these types have long been recognized as a proper source of revenue for [exempt] organizations and trusts.” Id. However, gross income from other sources in the nature of investments are not specifically excluded by § 512(b) and are generally included in the calculation of UBTI. Such gross income could include an exempt organization’s share (whether or not distributed) of the gross income of a partnership when the exempt organization is a partner and the partnership is engaged in one or more trades or businesses that are unrelated trades or businesses

\(^2\) Because IRAs described in § 408 are subject to the tax imposed by § 511, under § 408(e), and IRAs are most similar to § 401(a) trusts, it is reasonable to apply the definition of “unrelated trade or business” described in § 513(b) to IRAs. The Treasury Department and the IRS intend to provide that the § 513(b) definition of unrelated trades or businesses should be used in application of § 511 for accounts subject to the tax in § 511 pursuant to § 408(e).
with respect to the exempt organization partner.³

An exempt organization may engage in more than one unrelated trade or business. Prior to the enactment of § 512(a)(6), § 1.512(a)-1(a) provided that, with respect to an exempt organization that derives gross income from the regular conduct of two or more unrelated trades or businesses, UBTI was the aggregate gross income from all such unrelated trades or businesses less the aggregate deductions allowed with respect to all such unrelated trades or businesses. However, § 512(a)(6) changes this calculation for exempt organizations with more than one unrelated trade or business. Congress intended “that a deduction from one trade or business for a taxable year may not be used to offset income from a different unrelated trade or business for the same taxable year.” H.R. Rep. No. 115-466, at 548 (2017). Specifically, § 512(a)(6) provides that, in the case of any exempt organization with more than one unrelated trade or business:

(A) UBTI, including for purposes of determining any net operating loss (NOL) deduction, shall be computed separately with respect to each trade or business and without regard to § 512(b)(12) (allowing a specific deduction of $1,000),

(B) The UBTI of such organization shall be the sum of the UBTI so computed with respect to each trade or business, less a specific deduction under § 512(b)(12), and

(C) For purposes of § 512(a)(6)(B), UBTI with respect to any such trade or business shall not be less than zero.

³ In the case of a trust that is exempt from tax under § 501(a) that is described in § 401(a) or § 501(c)(17), § 513(b) defines “unrelated trade or business” as any trade or business regularly carried on a partnership of which it is a member.
Thus, § 512(a)(6) no longer allows aggregation of income and deductions from all unrelated trades or businesses. Section 512(a)(6) applies to taxable years beginning after December 31, 2017, but, as discussed in more detail in section 9 of this notice, not to NOLs arising before January 1, 2018, that are carried over to taxable years beginning on or after such date.

Separately, section 14201 of the Act added new § 951A of the Code. Section 951A(a) provides that “each person who is a United States shareholder of any controlled foreign corporation for any taxable year of such United States shareholder shall include in gross income such shareholder’s global intangible low-taxed income for such taxable year.”

SECTION 3. SEPARATE TRADE OR BUSINESS

.01 In General

In the case of any exempt organization with more than one unrelated trade or business, § 512(a)(6)(A) requires the organization to calculate UBTI, including for purposes of determining any NOL deduction (discussed in section 9 of this notice), separately with respect to each such trade or business. In enacting § 512(a)(6), Congress did not provide criteria for determining whether an exempt organization has more than one unrelated trade or business or how to identify separate unrelated trades or businesses for purposes of calculating UBTI. The Treasury Department and the IRS intend to propose regulations for determining whether an exempt organization has more than one unrelated trade or business for purposes of § 512(a)(6) and how to identify
separate trades or businesses for purposes of calculating UBTI under § 512(a)(6)(A).

.02 Reasonable, Good-Faith Interpretation of §§ 511 through 514

Pending issuance of proposed regulations, and pursuant to additional interim guidance provided in section 6 of this notice, exempt organizations may rely on a reasonable, good-faith interpretation of §§ 511 through 514, considering all the facts and circumstances, when determining whether an exempt organization has more than one unrelated trade or business for purposes of § 512(a)(6). A reasonable, good-faith interpretation includes using the North American Industry Classification System 6-digit codes described in section 3.03.

The Treasury Department and the IRS note that the fragmentation principle in § 513(c) and § 1.513-1(b), and related guidance, may also provide helpful guidance. Prior to the passage of § 512(a)(6), the fragmentation principle was primarily used to separate unrelated trades or businesses from exempt activities, but it might also have utility in identifying separate trades or businesses for purposes of § 512(a)(6)(A). The fragmentation principle provides that an activity does not lose its identity as a trade or business merely because it is carried on within a larger aggregate of similar activities or within a larger complex of other endeavors which may, or may not, be related to the exempt purposes of an organization. For example, the regular sale of pharmaceutical supplies to the general public by a hospital pharmacy does not lose its status as a trade or business merely because the pharmacy also furnishes supplies to the hospital and patients of the hospital in accordance with its exempt purposes or in compliance with
the terms of § 513(a)(2) (stating, in part, that the term “trade or business” does not include any trade or business that is carried on by an organization described in § 501(c)(3) or a state college or university primarily for the convenience of its members, students, patients, officers, or employees). See § 1.513-1(b). Similarly, activities of soliciting, selling, and publishing commercial advertising do not lose their statuses as trades or businesses even though the advertising is published in an exempt organization periodical that contains editorial matter related to the exempt purposes of the organization. Id. Additionally, several revenue rulings provide examples of how the fragmentation principle has been applied. See, e.g., Rev. Rul. 78-145, 1978-1 C.B. 169 (regarding the sale of blood products by a blood bank).

.03 Possible Methods for Identifying Separate Trades or Businesses

There is no general statutory or regulatory definition defining what constitutes a “trade or business” for purposes of the Internal Revenue Code. Whether an activity constitutes a trade or business may vary depending on which Code section is involved. See generally Commissioner v. Groetzinger, 480 U.S. 23, 27 (1987). The Treasury Department and the IRS request comments regarding rules to identify separate trades or businesses that achieve the intent of Congress in enacting § 512(a)(6) and are administrable for exempt organizations and the IRS.

Several Code sections describe factors for determining whether an organization is engaged in a trade or business or a line of business, including §§ 132, 162, 183, 414, and 469 (see also section 5.02 of this notice), and the regulations thereunder. The
Treasury Department and the IRS have considered these Code sections and are concerned that they do not provide useful models for identifying separate trades or businesses for purposes of § 512(a)(6). Nonetheless, the Treasury Department and the IRS request comments describing whether and how these and other Code sections (and the regulations thereunder) may aid in determining how to identify an exempt organization’s separate trades or businesses for purposes of § 512(a)(6)(A).

Although some commenters have suggested the creation of a facts and circumstances test to identify separate trades or businesses for purposes of § 512(a)(6), the Treasury Department and the IRS would like to set forth a more administrable method than a facts and circumstances test alone for identifying separate trades or businesses for purposes of § 512(a)(6). A facts and circumstances test would increase the administrative burden on exempt organizations in complying with § 512(a)(6) because such organizations would have to perform a fact-intensive analysis with respect to each of their trades or businesses, document the analysis, and then track and keep records consistent with such analysis. Additionally, such a test would likely result in inconsistency across the exempt organization sector in light of differing approaches in budgeting and staffing and thus create unequal burdens and cause exempt organizations to make business decisions such as budgeting and staffing solely to avoid the requirements of § 512(a)(6). Finally, such a test would also increase the administrative burden on the IRS in implementing and enforcing § 512(a)(6) because verifying whether an exempt organization calculated its UBTI correctly would require a
fact-intensive analysis of the organization’s trades or businesses and the determinations
made with respect to identifying separate trades or businesses for purposes of
calculating UBTI under § 512(a)(6)(A).

To provide additional guidance in proposed regulations for determining whether an
exempt organization has more than one unrelated trade or business for purposes of
§ 512(a)(6) and how to identify separate trades or businesses for purposes of
calculating UBTI under § 512(a)(6)(A), the Treasury Department and the IRS are
considering the use of North American Industry Classification System (NAICS) codes.
Prior to proposed regulations, the Treasury Department and the IRS will consider the
use of NAICS 6-digit codes to be a reasonable, good-faith interpretation under section
3.02 of this notice.

The NAICS is an industry classification system for purposes of collecting,
analyzing, and publishing statistical data related to the United States business
economy. See EXECUTIVE OFFICE OF THE PRESIDENT, OFFICE OF MANAGEMENT AND
BUDGET, NORTH AMERICAN INDUSTRY CLASSIFICATION SYSTEM (2017), available at
example, under a NAICS 6-digit code, all of an exempt organization’s advertising
activities and related services (NAICS code 541800) might be considered one unrelated
trade or business activity, regardless of the source of the advertising income. Use of all
6 digits of the NAICS codes would result in more specific categories of trades or
businesses whereas use of fewer than 6 digits of the NAICS codes would result in
broader categories of trades or businesses. Exempt organizations filing Form 990-T, “Exempt Organization Business Income Tax Return,” already are required to use the 6-digit NAICS codes when describing the organization’s unrelated trades or businesses in Block E. The Treasury Department and the IRS request comments regarding whether using less than 6 digits of the NAICS codes, or combining NAICS codes with other criteria, would appropriately identify separate trades or businesses for purposes of achieving the objective of § 512(a)(6). The Treasury Department and the IRS also request comments on the utility of this method, other methods, or a combination of methods that could be used for making this determination.

.04 Allocation of Directly Connected Deductions

Section 512(a)(1) permits an exempt organization with an unrelated trade or business to reduce the income from that trade or business by the deductions allowed by Chapter 1 of the Code that are directly connected with the carrying on of such trade or business. To be “directly connected” with a trade or business, an item of deduction must have a proximate and primary relationship to the carrying on of the unrelated trade or business generating the gross income. See § 1.512(a)-1(a). Expenses, depreciation, and similar items attributable solely to the conduct of an unrelated trade or business are proximately and primarily related to that trade or business and qualify to reduce income from such trade or business under § 512(a)(1) to the extent such items meet the requirements of §§ 162 (trade or business expenses), 167 (depreciation), and other relevant provisions.
To the extent that an exempt organization may have items of deduction that are shared between an exempt activity and an unrelated trade or business, the Treasury regulations at § 1.512(a)-1(c) and (d) provide special rules for allocating such expenses. For example, if facilities are used both to carry on exempt activities and to conduct unrelated trade or business activities, then expenses, depreciation, and similar items attributable to such facilities must be allocated between the two uses on a reasonable basis. See § 1.512(a)-1(c).

The Treasury Department and the IRS currently have an item on the Priority Guidance Plan regarding methods of allocating expenses relating to dual use facilities. The allocation issues under § 512(a)(1) also are relevant under § 512(a)(6) because an exempt organization with more than one unrelated trade or business must not only allocate indirect expenses among exempt and taxable activities as described in § 1.512(a)-1(c) and (d) but also among separate unrelated trades or businesses. The Treasury Department and the IRS therefore are considering modifying the underlying reasonable allocation method in § 1.512(a)-1(c) and providing specific standards for allocating expenses relating to dual use facilities and the rules under § 512(a)(6). The Treasury Department and the IRS are requesting comments regarding possible rules or defined standards for the allocation of indirect expenses between separate unrelated trades or businesses for purposes of calculating UBTI under § 512(a)(6)(A), and, in particular, regarding what allocation methods should be considered “reasonable.”
SECTION 4. INCOME TREATED AS AN ITEM OF GROSS INCOME FROM AN UNRELATED TRADE OR BUSINESS

Sections 512(b)(4), (13), and (17) treat unrelated debt financed income, specified payments received from controlled entities, and certain insurance income (as defined in § 953) as items of gross income derived from an unrelated trade or business and therefore includable in the calculation of UBTI under § 512(a) even though such amounts ordinarily would be excluded from the calculation of UBTI under § 512(b)(1), (2), (3), or (5). At least one commenter has questioned how income that is included in UBTI under § 512(b)(4), (13), and (17) is treated for purposes of § 512(a)(6) because that commenter states that amounts included in UBTI under these provisions do not have a nexus to an unrelated trade or business.

The Treasury Department and the IRS note that, in the absence of § 512(b)(1), (2), (3), and (5), interest, royalties, rents, and gains (or losses) from the sale, exchange, or other disposition of property would be included in the calculation of UBTI to the extent that such amounts are “gross income derived by any organization from any unrelated trade or business . . . regularly carried on by it” under § 512(a)(1). Accordingly, the Treasury Department and the IRS see no distinction between “gross income derived by any organization from any unrelated trade or business . . . regularly carried on by it” within the meaning of § 512(a)(1) and amounts included in UBTI “as an item of gross income derived from an unrelated trade or business” under § 512(b)(4), (13), and (17).

However, the Treasury Department and the IRS recognize that one interpretation of
§ 512(a)(6) might impose a significant burden on organizations required to include amounts in UBTI under § 512(b)(4), (13), or (17). For example, one interpretation of § 512(a)(6) might require treating each debt-financed property owned by an exempt organization as a separate trade or business for purposes of § 512(a)(6)(A), because the debt/basis percentage used to calculate the portion of income that is unrelated debt-financed income included in the calculation of UBTI under § 512(b)(4) is specific to each property. Similarly, an exempt organization might be required to report income from each controlled entity as income from a separate trade or business for purposes of § 512(a)(6)(A). The exempt organization would have to track and report each debt-financed property owned directly by an exempt organization or income from each controlled entity separately, which imposes a burden both on the exempt organization and on the IRS. Accordingly, aggregating income included in UBTI under § 512(b)(4), (13), or (17) may be appropriate in certain circumstances. The Treasury Department and the IRS therefore request comments regarding the treatment under § 512(a)(6) of income that is not from a partnership, but is included in UBTI under § 512(b)(4), (13), and (17).

SECTION 5. ACTIVITIES IN THE NATURE OF INVESTMENTS

.01 Partnership Interests

In general, for exempt organizations, the activities of a partnership are considered
the activities of the partners.\textsuperscript{4} Section 512(c) requires an exempt organization that is a partner in a partnership that conducts a trade or business that is an unrelated trade or business with respect to the exempt organization to include in UBTI its distributive share of gross partnership income (and directly connected partnership deductions) from such unrelated trade or business. Whether a trade or business engaged in by the partnership is an unrelated trade or business with respect to the exempt organization is determined under §§ 511 through 514, and the regulations thereunder. Based on § 512(c) and the fragmentation principle, as discussed in section 3.02 of this notice, one interpretation of § 512(a)(6) might require an exempt organization to calculate UBTI separately with respect to each unrelated trade or business regularly carried on by the partnership in which the exempt organization is a direct or indirect partner. For example, if an exempt organization is a partner in a holding partnership that is a partner in multiple partnerships, many of which engage in one or more unrelated trades or businesses with respect to the exempt organization partner, the exempt organization may be engaged in multiple separate unrelated trades or businesses through its interest in the partnership.

02 Permitting the Aggregation of Gross Income and Directly Connected Deductions from Certain “Investment Activities”

The Treasury Department and the IRS have received comments regarding the

\textsuperscript{4} See IRC §§ 512(c), 513(a); Treas. Reg. § 1.513-1(d)(1) and (2); Plumstead Theatre Society, Inc. v. Commissioner, 74 T.C. 1324 (1980); 675 F.2d 244 (9th Cir. 1985); Service Bolt & Nut Co. Profit Sharing Trust v. Commissioner, 724 F.2d 519 (6th Cir. 1983), affg, 78 T.C. 812 (1982); Rev. Rul. 98-15, 1998-1 C.B. 718.
potential significant reporting and administrative burden imposed by § 512(a)(6) on exempt organizations with various activities in the nature of an investment including ownership interests in multi-tier partnership structures that generate UBTI if the Treasury Department and the IRS adopt the interpretation of § 512(a)(6) discussed in section 5.01 of this notice. The administrative burden related to owning partnership interests would be heightened by the difficulty of obtaining sufficient information regarding the trade or business activities of lower-tier partnerships. Accordingly, as a matter of administrative convenience, the Treasury Department and the IRS intend to propose regulations treating certain activities in the nature of an investment ("investment activities") of an exempt organization as one trade or business for purposes of § 512(a)(6)(A) in order to permit exempt organizations to aggregate gross income and directly connected deductions from such “investment activities.” The Treasury Department and the IRS expect that treating these “investment activities” as one trade or business for this purpose will reduce the reporting and administrative burden on organizations required to comply with § 512(a)(6) and will also reduce the burden the IRS may experience in implementing and enforcing § 512(a)(6).

The Treasury Department and the IRS request comments regarding the scope of the activities, both investment partnership interests or other activities in the nature of an investment that may generate unrelated business income, that should be included in the category of “investment activities” for purposes of § 512(a)(6). The Treasury Department and the IRS have received some comments suggesting the definition of
material participation in § 469 could serve as a basis for separating investment activities from more active involvement in an unrelated trade or business. The Treasury Department and the IRS are concerned that the criteria for finding material participation under § 469 are more extensive than appropriate. With respect to partnership interests that could be included in the category of “investment activities” for purposes of § 512(a)(6), the Treasury Department and the IRS note that “investment activities” as discussed in section 6 of this notice should capture only partnership interests in which the exempt organization does not significantly participate in any partnership trade or business.

SECTION 6. INTERIM AND TRANSITION RULES FOR PARTNERSHIP INVESTMENTS

.01 Aggregation of Income and Directly Connected Deductions

(1) In General. Except as provided in section 6.01(2) through (4) of this notice, exempt organizations with partnership investments should use a reasonable, good-faith interpretation of §§ 511 and 514, considering all the facts and circumstances, when identifying separate trades or businesses for purposes of § 512(a)(6)(A) until the issuance of proposed regulations (see section 3.02 of this notice).

(2) Interim Rule for Aggregation of Qualifying Partnership Interests under the De Minimis and Control Tests. Pending publication of proposed regulations, an exempt organization may aggregate its UBTI from its interest in a single partnership with multiple trades or businesses, including trades or businesses conducted by lower-tier
partnerships, as long as the directly-held interest in the partnership meets the requirements of either the *de minimis* test (described in section 6.02 of this notice) or the control test (described in section 6.03 of this notice) ("qualifying partnership interest"). Additionally, under this interim rule, an exempt organization may aggregate all qualifying partnership interests and treat the aggregate group of qualifying partnership interests as comprising a single trade or business for purposes of § 512(a)(6)(A).

(3) **Transition Rule.** Pending publication of proposed regulations, an exempt organization may follow the transition rule (described in section 6.04 of this notice) for partnership interests with respect to which it is not applying the interim rule described in section 6.01(2) of this notice.

(4) **Limitations.** The interim rule and the transition rule do not apply to exempt organizations described in § 501(c)(7) that are subject to § 512(a)(3). See section 7 of this notice. Furthermore, these rules do not otherwise impact the application of § 512(c) and the fragmentation principle under § 513(c).

.02 *De minimis* test

(1) **In general.** A partnership interest is a qualifying partnership interest that meets the requirements of the *de minimis* test if the exempt organization holds directly no more than 2 percent of the profits interest and no more than 2 percent of the capital interest. But see section 6.02(2)(b) of this notice for rules requiring the combining of related interests in certain circumstances.
(2) **Percentage Interest.**  

(a) **Reliance on Schedule K-1.** In determining the exempt organization’s percentage interest in a partnership, the exempt organization may rely on the Schedule K-1 it receives from the partnership. In Part II, line J, a partnership enters the partner’s share of profit, loss, and capital interests at the beginning and the ending of the partnership’s taxable year. An organization will be considered to have no more than 2 percent of the profits or capital interests in the case of a partnership, if the average of the organization’s percentage interest at the beginning and the end of the partnership’s taxable year, or, in the case of a partnership interest held for less than a year, the percentage interest held at the beginning and end of the period of ownership within the partnership’s taxable year, entered in Part II, line J, of Schedule K-1 is no more than 2 percent (without regard to the number of days each such percentage is held during the taxable year). For example, if an exempt organization acquires an interest in a partnership that files on a calendar year basis in May and the partnership reports in Part II, Line J, of Schedule K-1 that the partner held a 3 percent profits interest at the date of acquisition but held a 1 percent profits interest at the end of the calendar year, the exempt organization will be considered to have held 2 percent of the profits interest in that partnership for that year ((3 percent + 1 percent)/2 = 2 percent). To the extent that a specific profits interest is not identified in Part II, Line J, of Schedule K-1, an organization does not meet the *de minimis* test.

(b) **Combining Related Interests.**  

(i) In General. When determining an exempt organization’s percentage partnership interest, the interest of a disqualified person, a
supporting organization, or a controlled entity in the same partnership will be taken into account. For example, if an exempt organization owns 1.5 percent of the profits interests in a partnership and a disqualified person with respect to the exempt organization owns an additional 1 percent profits interest in that partnership, the exempt organization would not meet the requirements of the *de minimis* test because its aggregate percentage interest exceeds 2 percent. However, the exempt organization may still be able to aggregate the income (and directly connected deductions) from that partnership interest with other qualifying partnership interests if the partnership interest meets the requirements of the control test (described in section 6.03 of this notice).

(ii) **Disqualified Person.** For purposes of section 6.02(2)(b)(i) of this notice, the term “disqualified person” has the same meaning as in § 4958(f).

(iii) **Supporting Organization.** For purposes of section 6.02(2)(b)(i) of this notice, the term “supporting organization” has the same meaning as in § 509(a)(3).

(iv) **Controlled Entity.** For purposes of section 6.02(2)(b)(i) of this notice, the term “controlled entity” has the same meaning as in § 512(b)(13)(D).

.03 Control Test

(1) **In General.** A partnership interest is a qualifying partnership interest that meets the requirements of the control test if the exempt organization (i) directly holds no more than 20 percent of the capital interest; and (ii) does not have control or influence over the partnership. The rules in section 6.02(2)(b) of this notice requiring the combination of related interests also apply for purposes of the control test.
(2) **Reliance on Schedule K-1.** When determining the exempt organization’s percentage interest in a partnership the exempt organization may rely on the Schedule K-1 it receives from the partnership. An organization will be considered to have no more than 20 percent of the capital interest, if the average of the organization’s percentage interest at the beginning and the end of the partnership’s taxable year, or, in the case of a partnership interest held for less than a year, the percentage interest held at the beginning and end of the period of ownership within the partnership’s taxable year, entered in Part II, line J, of Schedule K-1 is no more than 20 percent (without regard to the number of days each such percentage is held during the taxable year).

(3) **Control or Influence.** All facts and circumstances are relevant for determining whether an exempt organization has control or influence over a partnership. An exempt organization has control or influence if the exempt organization may require the partnership to perform, or may prevent the partnership from performing, any act that significantly affects the operations of the partnership. An exempt organization also has control or influence over a partnership if any of the exempt organization’s officers, directors, trustees, or employees have rights to participate in the management of the partnership or conduct the partnership’s business at any time, or if the exempt organization has the power to appoint or remove any of the partnership’s officers, directors, trustees, or employees.

.04 **Transition rule**

A previously acquired partnership interest may be difficult to modify to meet the de
minimis test (as described in section 6.02 of this notice) or control test (as described in section 6.03 of this notice) under the interim rule and the exempt organization may have to incur significant transactions costs to do so. Thus, an organization may choose to apply the following transition rule, if applicable, for a partnership interest acquired prior to August 21, 2018: an exempt organization may treat each such partnership interest as comprising a single trade or business for purposes of § 512(a)(6) whether or not there is more than one trade or business directly or indirectly conducted by the partnership or lower-tier partnerships. For example, if an organization has a thirty-five percent interest in a partnership prior to August 21, 2019, it can treat the partnership as being in a single unrelated trade or business even if the partnership’s investments generated UBTI from various lower-tier partnerships that were engaged in multiple types of trades or businesses.

.05 Unrelated Debt-Financed Income. The income from qualifying partnership interests permitted to be aggregated under the interim rule includes any unrelated debt-financed income (within the meaning of § 514) that arises in connection with the qualifying partnership interest that meets the requirements of either the de minimis test or the control test. See §§ 512(b)(4) and 514. For example, assume an exempt organization has an interest in a hedge fund that is treated as a partnership for federal income tax purposes, the interest is a qualifying partnership interest that meets the requirements of the de minimis test, and the hedge fund regularly trades stock on margin. Ordinarily, the dividends from such stock and any income (or loss) from the
sale, exchange, or other disposition of such stock would be excluded from UBTI under § 512(b)(1) and (5). However, because all or a portion of the stock’s purchase is debt-financed, § 512(b)(4) requires that all of or a portion (depending on the debt-basis percentage applied) of the dividend income (if any) and any income (or loss) from the sale of the stock be included in UBTI. For the purpose of the interim rule, the exempt organization may aggregate unrelated debt-financed income generated by the hedge fund with any other UBTI generated by any of the hedge fund’s trades or businesses that are unrelated trades or businesses with respect to the exempt organization.

Similarly, any unrelated debt-financed income that arises in connection with a partnership interest that meets the requirements of the transition rule may be aggregated with the other UBTI that arises in connection with that partnership interest.

SECTION 7. SOCIAL CLUBS, VOLUNTARY EMPLOYEES’ BENEFICIARY ASSOCIATIONS, AND SUPPLEMENTAL UNEMPLOYMENT COMPENSATION BENEFITS TRUSTS

Section 512(a)(3) provides special rules applicable to exempt organizations described in § 501(c)(7) (social clubs), (9) (voluntary employees’ beneficiary associations (VEBAs)), and (17) (supplemental unemployment compensation benefits trusts (SUBs)). For these exempt organizations, § 512(a)(3)(A) provides that UBTI means the gross income (excluding any exempt function income), less the deductions allowed by Chapter 1 of the Code that are directly connected with the production of the gross income (excluding exempt function income), both computed with the modifications
provided in § 512(b)(6) (the NOL deduction), (10) (charitable contribution deduction by exempt organizations), (11) (charitable contribution deduction by certain trusts), and (12) (specific deduction). Thus, social clubs, VEBAs, and SUBs are taxed under § 511 on their non-exempt function income, which generally includes investment income and income derived from an unrelated trade or business.

In particular, § 512(a)(3)(B) defines “exempt function income” as the gross income from dues, fees, charges, or similar amounts paid by members of the organization as consideration for providing such members or their dependents or guests goods, facilities, or services in furtherance of the purposes constituting the basis for the organization’s tax-exempt status. However, § 512(a)(3)(B) specifically excludes from the definition of “exempt function income” gross income derived from any unrelated trade or business regularly carried on by such organization (computed as if the organization were subject to § 512(a)(1)).\(^5\) For example, a social club’s nonmember income is treated as gross income from an unrelated trade or business under § 512(a)(3). See Rev. Rul. 2003-64, 2003-1 C.B. 1036. Accordingly, even though § 512(a)(3) uses terminology different from § 512(a)(1), § 512(a)(6) applies to an organization subject to § 512(a)(3) if such organization has more than one unrelated trade or business. For example, a social club that receives non-member income from multiple sources, such as from a dining facility and from a retail store, would have more

\(^5\) However, VEBAs and SUBs are taxed on income to the extent that the amount of assets in the VEBA or SUB at the close of the taxable year exceed the account limit described in § 512(a)(3)(E) and § 1.512(a)-5T. See also Prop. Reg. § 1.512(a)-5.
than one unrelated trade or business and therefore be subject to the requirements of § 512(a)(6).

The Treasury Department and the IRS anticipate that any rules issued regarding how an exempt organization identifies separate trades or businesses for purposes of § 512(a)(6)(A) will apply equally under § 512(a)(1) and (3). Nonetheless, because social clubs, VEBAs, and SUBs are taxed differently than other exempt organizations under § 511, the Treasury Department and the IRS request comments regarding any additional considerations that should be given to how § 512(a)(6) applies within the context of § 512(a)(3). In particular, the Treasury Department and the IRS request comments regarding how these exempt organizations’ investment income should be treated for purposes of § 512(a)(6).

SECTION 8. TOTAL UBTI

.01 In General

To determine total UBTI under § 512(a)(6)(B), an exempt organization takes the sum of the UBTI computed with respect to each separate trade or business under § 512(a)(6)(A), less a specific deduction under § 512(b)(12). However, in calculating total UBTI under § 512(a)(6)(B), § 512(a)(6)(C) provides that UBTI with respect to any trade or business cannot be less than zero.

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6 However, the rules in section 6 of this notice for aggregating UBTI from partnership interests do not apply to social clubs described in § 501(c)(7).
.02 Fringe Benefits

Section 512(a)(7) increases UBTI by any amount for which a deduction is not allowable under this chapter by reason of § 274 and which is paid or incurred by such exempt organization for any qualified transportation fringe (as defined in § 132(f)), any parking facility used in connection with qualified parking (as defined in § 132(f)(5)(C)), or any on-premises athletic facility (as defined in § 132(j)(4)(B)). However, § 512(a)(7) does not apply to the extent the amount paid or incurred is directly connected with an unrelated trade or business that is regularly carried on by the organization. Unlike other paragraphs of § 512, § 512(a)(7) does not treat amounts included in UBTI as a result of that section as an item of gross income derived from an unrelated trade or business (see section 4 of this notice). Furthermore, the Treasury Department and the IRS do not believe that the provision of the fringe benefits described in § 512(a)(7) is an unrelated trade or business. Accordingly, any amount included in UBTI under § 512(a)(7) is not subject to § 512(a)(6).

SECTION 9. NOLS AND UBTI

Prior to the Act, § 172 allowed an NOL deduction equal to the sum of NOLs permitted to be carried back to the taxable year from succeeding taxable years and the NOLs permitted to be carried forward from preceding taxable years. An NOL generally could be carried back two years and carried forward twenty years. See § 172(b) (prior to the Act). Section 512(b)(6), which was not changed by the Act, generally permits exempt organizations subject to the unrelated business income tax under § 511,
including exempt organizations with more than one unrelated trade or business, to take the NOL deduction provided in § 172. In particular, § 512(b)(6)(A) states that the NOL for any taxable year, the amount of the NOL carryback or carryover to any taxable year, and the NOL deduction for any taxable year shall be determined under § 172 without taking into account any amount of income or deduction that is excluded under § 512(b) in computing UBTI. For example, a loss attributable to an unrelated trade or business is not to be reduced by reason of the receipt of dividend income. See § 1.512(b)-1(e)(1).

An NOL carryover is allowed only from a taxable year for which the taxpayer is subject to the provisions of § 511, or a corresponding provision of prior law. See § 512(b)(6)(B); § 1.512(b)-1(e)(3).

However, § 512(a)(6) changes how an exempt organization with more than one unrelated trade or business calculates and takes NOLs into account with respect to a particular trade or business. In particular, § 512(a)(6)(A) requires such an organization to calculate UBTI, including for purposes of determining any NOL deduction, separately with respect to each trade or business for taxable years beginning after December 31, 2017 (post-2017 NOLs). The Congressional intent behind this change is to allow an NOL deduction “only with respect to a trade or business from which the loss arose.” H.R. Rep. No. 115-466, at 547-48. In the first taxable year beginning after December 31, 2017, no exempt organization with more than one unrelated trade or business will have an NOL deduction to take against the UBTI of a particular trade or business calculated under § 512(a)(6)(A).
Additionally, in order to preserve NOLs from tax years prior to the effective date of the Act, Congress created a special transition rule to permit the carryover of any NOL arising in a taxable year beginning before January 1, 2018 (pre-2018 NOLs). In particular, section 13702(b)(2) of the Act provides that § 512(a)(6)(A) does not apply to pre-2018 NOLs; rather, pre-2018 NOLs are taken against total UBTI calculated under § 512(a)(6)(B). Accordingly, even though an exempt organization with more than one unrelated trade or business will not have any NOL deductions when calculating UBTI with respect to a separate trade or business under § 512(a)(6)(A) for the first taxable year beginning after December 31, 2017, such an organization may be able to take an NOL deduction against total UBTI calculated for such year under § 512(a)(6)(B) if the organization has pre-2018 NOLs.

In the second taxable year beginning after December 31, 2017, an exempt organization with more than one unrelated trade or business may have both pre-2018 NOLs and post-2017 NOLs. Section 512(a)(6) may have changed the order in which an organization would ordinarily take losses because § 512(a)(6)(A) requires an organization with more than one unrelated trade or business to calculate UBTI separately (including for purposes of determining any NOL deduction) with respect to each such trade or business before calculating total UBTI under § 512(a)(6)(B). If § 512(a)(6) is read as an ordering rule for purposes of calculating and taking the NOL deduction, post-2017 NOLs will be calculated and taken before pre-2018 NOLs because the UBTI with respect to each separate trade or business is calculated under
§ 512(a)(6)(A) before calculating total UBTI under § 512(a)(6)(B).

Furthermore, section 13302 of the Act made extensive changes to § 172, including limiting post-2017 NOLs to the lesser of (1) the aggregate NOL carryovers to such year, plus the NOL carrybacks to such year, or (2) 80 percent of taxable income computed without regard to the deduction generally allowable under § 172. The limitation in § 172(a) applies only to post-2017 NOLs, but a question exists regarding how the § 172(a) 80 percent income limitation applies when both pre-2018 and post-2017 NOLs exist. The Treasury Department and the IRS intend to issue guidance regarding how § 172 generally applies. However, because § 512(a)(6) provides a more specific rule than the one found in § 172 regarding how the NOL deduction is calculated and taken in the context of calculating UBTI, the Treasury Department and the IRS are requesting comments regarding how the NOL deduction should be taken under § 512(a)(6) by exempt organizations with more than one unrelated trade or business and, in particular, by such organizations with both pre-2018 and post-2017 NOLs. The Treasury Department and the IRS also request comments on the ordering of pre-2018 and post-2017 NOLs and the potential treatment of pre-2018 NOLs that may expire in a given tax year if not taken before post-2017 NOLs.

SECTION 10. TREATMENT OF GLOBAL INTANGIBLE LOW-TAXED INCOME

Commenters have asked whether an exempt organization must include GILTI (included in gross income under § 951A) in the calculation of UBTI. In particular, these commenters have questioned whether GILTI is treated in the same manner as an
inclusion of subpart F income under § 951(a)(1)(A) for purposes of the unrelated business income tax under § 511.

The IRS treats an inclusion of subpart F income as a dividend for purposes of § 512(b)(1). Accordingly, subpart F income generally is excluded from the calculation of UBTI. Congress approved of the IRS’s long-standing position when it enacted § 512(b)(17) as part of the Small Business Job Protection Act of 1996, Public Law 104-188 (110 Stat. 1755 (1996)). See H.R. Rep. No. 105-586, at 136 (1996) (stating that “income inclusions under subpart F have been characterized as dividends for unrelated business income tax purposes” and citing several private letter rulings issued by the IRS taking this position). Although an inclusion of subpart F income under § 951(a)(1)(A) is generally excluded from the calculation of UBTI as a dividend under § 512(b)(1), § 512(b)(17) requires any amount included in gross income under § 951(a)(1)(A) that is attributable to insurance income (as defined in § 953) which, if derived directly by the organization, would be treated as gross income from an unrelated trade or business to be included in the calculation of UBTI.

GILTI is not an inclusion of subpart F income under § 951(a)(1)(A), but instead is a separate inclusion under § 951A(a). Nonetheless, an inclusion of GILTI is generally treated in a manner similar to an inclusion of subpart F income for other purposes of the Code. See H.R. Rep. No. 115-446, at 641 (stating that, “[u]nder the provision, a U.S. shareholder of any [controlled foreign corporation] must include in gross income for a taxable year its [GILTI] in a manner generally similar to inclusions of subpart F income”).
The Treasury Department and the IRS have determined that an inclusion of GILTI under § 951A(a) should be treated in the same manner as an inclusion of subpart F income under § 951(a)(1)(A) for purposes of § 512(b)(1) and (4). Accordingly, an inclusion of GILTI will be treated as a dividend which is generally excluded from UBTI under § 512(b)(1).

Commenters have also questioned whether § 512(b)(17) will apply to treat as UBTI an inclusion of GILTI to the extent attributable to insurance income (as defined in § 953) that does not constitute subpart F income. The Treasury Department and the IRS note that Congress made no changes to § 512(b) when enacting § 951A, and has not otherwise specifically required the inclusion of such insurance income in UBTI. Accordingly, unless provided otherwise in proposed regulations, the Treasury Department and the IRS will not treat GILTI included in gross income under § 951A(a) that is attributable to insurance income as includible in the UBTI of a tax-exempt organization.

SECTION 11. RELIANCE

For taxable years beginning after December 31, 2017, organizations described in § 511(a)(2) and trusts described in § 511(b)(2), collectively called “exempt organizations” throughout this notice, may rely on methods of aggregating or identifying separate trades or businesses under § 512(a)(6) provided in this notice until proposed regulations are published. All such organizations may rely on a reasonable, good-faith interpretation of §§ 511 through 514 taking into account all the facts and circumstances
when determining whether an exempt organization has more than one unrelated trade or business for purposes of § 512(a)(6). For an exempt organization this also includes using a reasonable, good-faith interpretation when determining:

- Whether to separate debt-financed income described in §§ 512(b)(4) and 514;
- Whether to separate income from a controlled entity described in § 512(b)(13); and
- Whether to separate insurance income earned through a controlled foreign corporation as described in § 512(b)(17).

The use of NAICS 6-digit codes will be considered a reasonable, good-faith interpretation until regulations are proposed.

For taxable years beginning after December 31, 2017, exempt organizations, other than organizations described in § 501(c)(7) (social clubs), may also rely on the rules provided for aggregating income from partnerships in section 6 of this notice until proposed regulations are published. These aggregation rules include any unrelated debt-financed income that is earned through a partnership that meets the requirements of the rules described in section 6 of this notice. The rules described in section 6 of this notice include:

- The interim rule that permits the aggregation of qualifying partnership interests that meet either the de minimis test or control test into a single trade or business; and
• The transition rule, which allows for aggregating income within each direct partnership interest acquired before August 21, 2018.

Finally, exempt organizations may rely on sections 8.02 and 10 of this notice. These sections provide that:

• Income under § 512(a)(7) is not income from a trade or business for purposes of § 512(a)(6); and

• For purposes of calculating UBTI, an inclusion of GILTI under § 951A(a) is treated as a dividend and follows the treatment of dividends under § 512(b)(1) and (b)(4).

SECTION 12. REQUEST FOR COMMENTS

The Treasury Department and the IRS request comments regarding the application of § 512(a)(6) to exempt organizations with more than one unrelated trade or business. Specifically, the Treasury Department and the IRS seek comments on the general interim rule for distinguishing between trades and businesses under § 512(a)(6) (section 3 of this notice); whether other Code sections (and the regulations thereunder) may provide an administrable model for identifying an exempt organization’s separate trades or businesses (section 3.03 of this notice); whether NAICS 6-digit (or less) codes might be the basis of a method for identifying separate trades or businesses (section 3.03 of this notice); the general rules for allocating deductions between trades or businesses (section 3.04 of this notice); the treatment of income treated as an item of gross income from an unrelated trade or business, including the treatment of debt-financed income
(§ 512(b)(4), (13) and (17)) (section 4 of this notice); the scope of the activities that should be included in the category of “investment activities” (section 5.02 of this notice); the treatment of income derived from activities in the nature of an investment through partnerships (sections 5 and 6 of this notice); any additional considerations that should be given to how § 512(a)(6) applies within the context of § 512(a)(3) (section 7 of this notice); and the calculation and ordering of pre-2018 and post-2017 NOLs and the treatment of pre-2018 NOLs that will expire in a given tax year if not taken before post-2017 NOLs (section 9 of this notice). Comments should be submitted on or before December 3, 2018. Please include Notice 2018-67 on the cover page. Comments should be sent to the following address:

Internal Revenue Service  
CC:PA:LPD:PR (Notice 2018-67), Room 5203  
P.O. Box 7604  
Ben Franklin Station  
Washington, DC 20044

Submissions may be hand delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to:

Internal Revenue Service  
Courier’s Desk  
1111 Constitution Ave., N.W.  
Washington, DC 20224  

Submissions may also be sent electronically to the following e-mail address:

Notice.Comments@irs counsel.treas.gov.

Please include “Notice 2018-67” in the subject line.
All comments will be available for public inspection and copying.

SECTION 13. PAPERWORK REDUCTION ACT

The collection of information in this notice is the requirement under § 512(a)(6) that an exempt organization with more than one unrelated trade or business calculate UBTI separately with respect to each such trade or business. The collection of information contained in this notice is reflected in the collection of information for Form 990-T that has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. 3507(c)) under control number 1545-0687.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid OMB control number.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by § 6103.

SECTION 14. DRAFTING INFORMATION

The principal authors of this notice are Stephanie N. Robbins and Jonathan A. Carter of the Office of Associate Chief Counsel (TEGE). For further information regarding this notice contact Mr. Carter at (202) 317-5800 (not a toll-free call).
Supplement 2

ABA Tax Section Comments on Notice 2018-67
Submitted December 4, 2018
December 4, 2018

Hon. Charles P. Rettig
Commissioner
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC 20024

Re: Comments on the regulatory implementation of new section 512(a)(6) in response to Notice 2018-67

Dear Commissioner Rettig:

Enclosed please find comments on the regulatory implementation of new section 512(a)(6) of the Internal Revenue Code in response to the request for comments in Notice 2018-67. These comments supplement our first set of comments dated June 21, 2018. They are submitted on behalf of the Section of Taxation and have not been approved by the House of Delegates or the Board of Governors of the American Bar Association.

The Section of Taxation would be pleased to discuss these comments with you or your staff.

Sincerely,

Eric Solomon
Chair, Section of Taxation

Enclosure

cc: Hon. David Kautter, Assistant Secretary (Tax Policy), Department of the Treasury
Krishna P. Vallabhaneni, Acting Tax Legislative Counsel, Department of the Treasury
Elinor Ramey, Attorney Advisor, Department of the Treasury
William M. Paul, Acting Chief Counsel and Deputy Chief Counsel (Technical), Internal Revenue Service
David Horton, Acting Commissioner, Tax Exempt & Government Entities Division, Internal Revenue Service
Robert Choi, Acting Deputy Commissioner, Tax Exempt & Government Entities Division, Internal Revenue Service
Victoria A. Judson, Associate Chief Counsel, Tax Exempt & Government Entities Division, Internal Revenue Service
Margaret Von Lienen, Director, Exempt Organizations, Tax Exempt & Government Entities Division, Internal Revenue Service
COMMENTs ON INTERNAL REVENUE CODE SECTION 512(a)(6)
SPECIAL RULE FOR ORGANIZATIONS WITH MORE THAN ONE
UNRELATED TRADE OR BUSINESS

These comments ("Comments") are submitted on behalf of the American Bar Association
Section of Taxation and have not been approved by the House of Delegates or the Board of
Governors of the American Bar Association. Accordingly, they should not be construed as
representing the position of the American Bar Association.

Principal responsibility for preparing these Comments was exercised by Megan E. Bell,
Meghan R. Biss, Eve Borenstein, Nathan M. Doane, Dahlia B. Doumar, Laura Kalick, Norah
Jones, James P. Joseph, Jorge Lopez, Elizabeth M. Mills, Tanvi Mirani, James O’Connell, David
A. Shevlin, Jan Smith, Robert A. Wexler and Maura L. Whelan. These Comments were reviewed
by Lisa L. Johnsen, Chair of the Exempt Organizations Committee. The Comments were further
reviewed by Ellen Aprill of the Section’s Committee on Government Submissions and by

Although the members of the Section of Taxation who participated in preparing these
Comments have clients who might be affected by the federal tax principles addressed by these
Comments, no such member or the firm or organization to which such member belongs has been
engaged by a client to make a government submission with respect to, or otherwise to influence
the development or outcome of, the specific subject matter of these Comments.

Contacts: Lisa L. Johnsen
(206) 709-3212
lisa.johnsen@gatesfoundation.org

Robert A. Wexler
(415) 421-7555
wexler@adlercolvin.com

Date: December 4, 2018
EXECUTIVE SUMMARY

These Comments respond to the request by the Department of the Treasury (“Treasury”) and the Internal Revenue Service (the “Service”) for comments on the regulatory implementation of section 512(a)(6),1 as set forth in Notice 2018-67 (the “Notice”). These Comments supplement our comments dated June 21, 2018 (“June Comments”), which we submitted prior to the issuance of the Notice.

Prior to the enactment of section 512(a)(6), as part of Public Law 115-97 (the “Act”),2 exempt organizations were permitted to aggregate their losses and gains from all unrelated business activities and then report and pay taxes on the net unrelated business taxable income (“UBTI”), if any. New section 512(a)(6), which has colloquially been referred to as the “silo” rule, requires, beginning for tax years starting in 2018, that “[i]n the case of any organization with more than 1 unrelated trade or business—(A) unrelated business taxable income, including for purposes of determining any net operating loss deduction, shall be computed separately with respect to each such trade or business . . . .” As the Notice indicates, the definition of “each such trade or business” is the key issue requiring regulatory guidance in interpreting section 512(a)(6). Our June Comments provided our thoughts and recommendations on that definition.

In these Comments, we respond to the specific questions posed in Sections 3 through 10 of the Notice. We summarize our recommendations as follows:

Notice Section 3 -- Identifying Separate Trades or Businesses.

We appreciate the Service’s providing interim guidance for the period prior to the issuance of proposed regulations (the “Proposed Regulations”).

We recommend that the Proposed Regulations provide a safe harbor that authorizes organizations to rely on the first two digits from codes found in the North American Industry Classification System (“NAICS”). We suggest that an organization be permitted to aggregate income and losses from two or more activities that share the same two-digit NAICS code into one UBTI silo.

Notice Sections 4 and 5 -- Investment Income.

Notice Sections 4 and 5 deal with a different aspect of investment income. As discussed in our June Comments, we believe that investment income does not represent “trade or business” income that was intended to be allocated to silos under section 512(a)(6). We understand that Treasury and the Service may not agree with this view. If Treasury and the Service treat investment income as income subject to the silo rules, we recommend the following overall approach:

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1 References to a “section” or “§” are to a section of the Internal Revenue Code of 1986, as amended, unless otherwise indicated.
Because of the administrative complexity of tracking investment expenses, as identified in the Notice, we suggest that all investment income and loss that is otherwise considered to be UBTI under the general UBTI rules, which take into account modifications and exclusions, be aggregated into one general investment income silo.3

This silo would include:

- All income or loss that is deemed to be UBTI by virtue of sections 512(b)(4), 512(b)(13), and 512(b)(17);
- All income or loss from a partnership4 that is not deemed to be “controlled” directly or indirectly by the exempt organization.5 We discuss control below.
- That portion of the income or loss from a controlled partnership that is UBTI only because of sections 512(b)(4), 512(b)(13), or 512(b)(17).

**Notice Section 6 -- Controlled Partnerships.**

An exempt organization should be deemed not to control a partnership unless it owns more than 50% of the profits or capital interest in the partnership, as discussed in more detail below. If an exempt organization is deemed to control a partnership, then (a) the taxable investment income from the partnership, because of sections 512(b)(4), 512(b)(13), or 512(b)(17), should be allocated to the general investment income silo and (b) other trade or business income should be categorized as provided in Section 3, along with the other unrelated trade or business income of the organization.

**Notice Section 7 -- Social Clubs and VEBAs.**

We suggest that the rules discussed above be applied equally to VEBAs and social clubs. For these exempt entities, of course, more income will be included as UBTI because all investment income and all non-member income is deemed to be UBTI. We recommend applying the same two-digit NAICS code analysis to similar activities of a social club or VEBA, and we recommend using the same investment income silo analysis, as well.

**Notice Section 8 -- 512(a)(7) Income is not Subject to 512(a)(6).**

We agree with the Notice that expenses that are treated as UBI solely because of section 512(a)(7) should not be subject to the silo rules. An organization that has only one trade or business, therefore, would be able to aggregate the income or losses from that one activity with any section 512(a)(7) deemed income, and the silo rules would not apply to that organization.

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3 I.R.C. § 512(a)(1).
4 By partnership we mean any entity or arrangement that is classified as a partnership for Federal income tax purposes.
5 We do not specifically address whether this rule should apply to S corporations, but, generally, if S corporation income is subject to silos, then it would seem to follow that such income would be allocated to the general investment income silo.
We understand that applying these principles to organizations with more than one trade or business is more complicated because such an organization is subject to the silo rules. Arguably, an organization with more than one trade or business would not be able to offset losses from one activity against section 512(a)(7) deemed income. In our view, this result is not equitable, and we recommend that, as a matter of equity, Treasury and the Service allow organizations with more than one trade or business to use losses to offset section 512(a)(7) deemed income.

**Notice Section 9 -- Net Operating Losses.**

Our June Comments include suggestions on the treatment of net operating losses (“NOLs”). To reiterate, we suggest that NOLs continue to be treated in a “first in first out” manner, consistent with the customary treatment of NOLs. Ordering NOL is important because post-2017 NOLs are subject to the 80% deduction limitation.

**Section 10 -- Global Intangible Low-Taxed Income.**

We agree with the Notice that exempt organizations are not required to include as UBTI any global intangible low-taxed income (or “GILTI”) that is included in gross income under section 951A because such income is not treated as UBTI under general principles.
DISCUSSION

I. Overview

Prior to the Act, an organization carrying on two or more unrelated business activities calculated its UBTI as the aggregate of its gross income from the activities minus the aggregate allowable deductions. In computing deductions, organizations could account for expenses, depreciation, and similar items that would be deductible by a commercial enterprise so long as the deduction was directly connected with the unrelated trade or business. An item is directly connected if it has a primary and proximate relationship to the carrying on of the trade or business.

Under new section 512(a)(6), this calculation has changed. Now organizations with more than one unrelated trade or business are required separately to compute their UBTI for “each such trade or business.” This change results in an organization calculating its gross income minus allowable deductions, including any net operating losses, in separate “silos” for each trade or business it conducts. The net income from each silo cannot equal less than zero. To determine its UBTI, the organization adds the amounts from these separate silos together. Other than historic net operating losses, the gains or losses from one trade or business may not be used to calculate income outside of its specific silo.

The language of section 13720 of the Act adding section 512(a)(6), section (A) reads as follows:

(6) SPECIAL RULE FOR ORGANIZATION WITH MORE THAN 1 UNRELATED TRADE OR BUSINESS. - In the case of any organization with more than 1 unrelated trade or business -

(A) unrelated business taxable income, including for purposes of determining any net operating loss deduction, shall be computed separately with respect to each such trade or business and without regard to subsection (b)(12),

(B) the unrelated business taxable income of such organization shall be the sum of the unrelated business taxable income so computed with respect to each such trade or business, less a specific deduction under subsection (b)(12), and

(C) for purposes of subparagraph (B), unrelated business taxable income with respect to any such trade or business shall not be less than zero.

After providing an overview of section 512(a)(6) and the UBTI rules, the Notice asks for

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6 Reg. § 1.512(a)–1(a).
7 Reg. § 1.512(a)–1(a).
8 Reg. § 1.512(a)–1(a).
9 I.R.C. § 512(a)(6).
comments on a series of issues. The Notice also recognizes the need for, and importance of, exempt organizations being able to administer section 512(a)(6) efficiently in light of information that is regularly available to exempt organizations. Our discussion and recommendations below follow the sections in the Notice.

II. Specific Guidance

Notice Section 3 -- Identifying Separate Trades or Businesses.

In our comments to Notice Section 3, we first consider whether the interim rule proposed in Section 3.02 might work as a permanent rule. We next consider whether guidance from other Code sections is useful in developing a long-term rule. Finally, we recommend a safe-harbor rule that uses two-digit NAICS codes.

A. The interim rule is useful, but is not a permanent approach.

Notice Section 3.02 provides an interim rule upon which organizations may rely until Proposed Regulations are issued. In Notice Section 3.02, Treasury and the Service provide that until additional guidance is issued organizations may “rely on a reasonable, good-faith interpretation of sections 511 through 514, considering all the facts and circumstances, when determining whether an exempt organization has more than one unrelated trade or business for purposes of section 512(a)(6).” The Notice further provides that use of the six-digit codes contained in the NAICS would constitute a reasonable, good-faith interpretation.

Notice Section 3.03 requests recommendations on a permanent rule. We recommend a bright line rule rather than reliance solely on facts and circumstance. Both exempt organizations and the government may find a standard that relies exclusively on facts and circumstances difficult to administer. An organization that reports on the basis of facts and circumstances will need to analyze separately each trade or business as well as retain records to demonstrate that it has made a reasonable, good-faith interpretation. Such an effort will require many organizations, including small organizations, to rely upon tax professionals to navigate the rules and to adequately document their decisions. Additionally, a reasonable, good faith standard, rather than bright line rules, will produce inconsistent results across the sector. Some organizations will take cautious approaches while others aggressively test what is “reasonable.” These issues will be resolved only during audits, and results will not be broadly known because audit results are not generally public. Finally, if this test is difficult for the Service to enforce, it will require time consuming and in-depth audits into an organization’s records to determine reasonability.

Accordingly, we recommend that when issuing Proposed Regulations, Treasury and the Service offer not only a basic reasonable, good-faith approach, but also a precise safe-harbor, discussed below. We also recommend that the Service provide itself flexibility to update these safe-harbor, rules through Revenue Rulings, Revenue Procedures, and notices as necessary.

Finally, for organizations that choose a facts and circumstances approach, rather than the safe-harbor, we urge that the Form 990-T be modified to allow organizations to disclose and describe their allocation methodologies. Specifically, we recommend that the Service include a
schedule similar to Schedule O of the Form 990. Alternatively, space could be provided on Form 990-T, Schedule M for the organization to explain its methodology.

B. Other Code sections do not provide helpful guidance.

The Notice asks whether and how sections 132, 162, 183, 414, 469 or other Code sections and the Treasury Regulations (the “Regulations”) thereunder may aid in determining how to identify an exempt organization’s separate trades or businesses for purposes of section 512(a)(6)(A).

We have considered whether existing guidance under other Code sections and Regulations could provide a useable framework. Although we believe that section 132 may provide some useful guidance, we do not recommend that the approaches in those sections be adopted wholesale.

1. Section 132

Some of the framework of section 132 could be useful for identifying separate trades or businesses, particularly the Regulation’s use of NAICS codes at the two-digit level. However, we do not recommend that the section 132 approach be adopted in its entirety. Section 132 and its Regulations discuss, for some of its provisions, lines of businesses and contain limitations with respect to property and services that are offered “for sale to customers in the ordinary course of the same line of business in which the employee receiving the property or service performs substantial services.” In defining a line of business, the Regulations rely upon the Enterprise Standard Industrial Classification Manual (the “ESIC Manual”) formerly prepared by the Statistical Policy Division of the United States Office of Management and Budget (the “OMB”).

The Regulations provide that “[a]n employer is considered to have more than one line of business if the employer offers for sale to customers property or services in more than one two-digit code classification referred to in the ESIC Manual.” The ESIC Manual was developed by OMB to supplement the Standard Industrial Classification manual (“SIC”). However, the ESIC Manual is no longer in use. Similarly, SIC is no longer in use and was replaced in 1997 by NAICS.

The Regulations under section 132 permit the use of industry codes at a two-digit level, rather than requiring a more extensive match. The Regulations also do not require any additional facts and circumstances -- a two-digit match is sufficient. Additionally, the Regulations permit organizations to aggregate their lines of business if certain criteria are met. We recommend that Treasury and the Service consider whether similar rules would be appropriate for the silo rule – that is, a two-digit match without explanation of any additional facts and circumstances.

13 Reg. § 1.132-4(a)(2).
14 Id.
17 Reg. § 1.132-4(a)(3).
2. **Section 162**

   In the UBTI context, the term “trade or business” has long been defined as having “the same meaning it has in section 162 and generally includes any activity carried on for the production of income from the sale of goods or performance of services.” However, neither the Code nor the Regulations define the term “trade or business.” Cases defining a trade or business in the section 162 context are very fact specific. Using section 162 to differentiate between trades and businesses would again require exempt organizations to apply a facts and circumstances test. As a result, we do not believe that section 162 provides a helpful framework for identifying separate trades or businesses for purposes of section 512(a)(6)(A).

3. **Section 183**

   During the Colleges and Universities Compliance Project, the Service relied on the rules contained in section 183 and Regulations section 1.183-2(b)(1)-(9) to determine whether an activity was a trade or business under section 513. In some instances, when an activity had a history of producing losses, the Service determined that the activity was not a trade or business because it was an “activity not engaged in for profit” under section 183. Section 183 defines an “activity not engaged in for profit” as an activity other than one for which deductions are available under section 162. Thus, like section 162, the determination of whether an activity is a trade or business for purposes of section 183 is based on facts and circumstances. Section 183 does not provide further guidance on distinguishing between activities that are trades or businesses. As a result, we do not recommend that Treasury and the Service rely on section 183.

4. **Section 414**

   Section 414 provides rules for controlled groups of businesses. If a controlled group exists under the applicable Code sections and associated Regulations, the employees of those businesses are combined together for certain qualified plan requirements. Section 414(b) refers to controlled groups consisting of corporations, and section 414(c) refers to all other controlled groups. Affiliated service groups are also defined by applicable Code and Regulation sections, in this case section 414(m) and Proposed Regulations sections 1.414(m)-1. These rules aim to prevent employers from setting up multiple entities to avoid compliance with rules applicable to what is essentially a single employer group. However, the purpose of section 414 is different from the purpose of section 512(a)(6) because the silo rules look to a single exempt organization rather than separately incorporated, affiliated businesses. Therefore, looking for common or effective control is not a useful mechanism for separating UBTI activities. Accordingly, we do not believe that this section provides an appropriate framework for identifying separate trades and businesses.

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19 Id.


21 Reg. § 1.183-1(a).
5. Section 469

Generally, a passive activity is any rental activity or any business in which the taxpayer does not materially participate. Businesses in which the taxpayer works on a regular, continuous, and substantial basis are not passive activities. Importantly, passive income does not include salaries, portfolio, or investment income. The passive activity loss rules usually apply at the individual level. Although section 469 was enacted to discourage abusive tax shelters, its impact extends far beyond shelters to virtually every business or rental activity, whether reported on Schedule C, F, or E, as well as to passthrough income and losses from partnerships, S corporations, and trusts. Generally, section 469 does not apply to regular C corporations, although it does have limited application to closely held C corporations. Because most exempt organizations are corporations, the section 469 rubric is not applicable.

C. We recommend a safe harbor using two-digit NAICS codes.

Although we agree with Treasury and the Service that NAICS codes allow organizations to comply more easily with section 512(a)(6), we believe that requiring organizations to have a six-digit match between activities before permitting aggregation is too stringent. Activities that naturally co-exist may not always have six-digit similarity under the NAICS codes. Accordingly, we recommend that Treasury and the Service implement a more permissive system that allows organizations to group activities based upon a less than a six-digit match of the NAICS codes. We recommend a two-digit NAICS code.

NAICS codes are organized from the two to six-digit level. The 2017 NAICS codes have 20 broad sector codes (characterized by two-digit matches), 99 subsector codes (characterized by three-digit matches), 311 industry group codes (characterized by four-digit matches), 709 NAICS industries (characterized by five-digit matches), and 1,057 national industries (characterized by six-digit matches). Out of the 1,057 six-digit codes, over half—530—are the same as their five-digit industry code match.

Although the Service currently requires organizations to use six-digit codes on the Form 990-T and Form 990, the 2017 instructions to both forms (and those of the preceding years back to 2008 in the case of the Form 990), and the draft Form 990-T instructions for 2018 contain fewer than 14% of the 1,057 six-digit codes. Therefore, when we review returns, we see that many organizations have been incorrectly categorizing their unrelated trades or businesses. The

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22 NAICS codes are also useful for organizations with substantial foreign operations, or for foreign organizations that are exempt in the United States (either through an application for tax-exempt status or by operation of treaty). Both Canada and Mexico participate in NAICS. Additionally, the NAICS codes have been correlated to the International Standard Industrial Classification (ISIC) from the United Nations and the General Industrial Classification of Economic Activities with the European Communities (NACE). See https://www.census.gov/esa/www/naics/faqs/faqs.html.


Service’s Statistics of Income office relies upon two-digit broad sector codes when it publishes its data table on “Primary Unrelated Business Activity or Industrial Grouping.” Accordingly, we believe that requiring a match of fewer than six-digits for purposes of classifying trades or businesses would be administrable for the Service. This approach would also provide the Service with all the information necessary to complete more effective audits. We further recommend that, as is the case under section 132, the Service implement the two-digit safe-harbor without requiring the organization to describe additional facts and circumstances. We believe using codes alone will be more efficient and less complex for organizations and the Service.

We believe that a less than six-digit match also permits an aggregation of activities that would naturally be conducted together and potentially share employees and resources. Treating these activities as separate, on the other hand, would require additional tracking and documentation by organizations as well as complicate Service audit activity by requiring detailed investigation into allocation methodologies. Below are some examples of unrelated trade or business activities deemed “common” in the Colleges and Universities Compliance Project. In each example, an organization would not be able to aggregate these “common” activities if it were required to use a six-digit NAICS code:

- **Retail and gift shops**— Physical retail stores, e-commerce stores, catalog, and mail order retail stores all share two-digit NAICS code 45. However, an organization that uses a three- to six-digit NAICS code would not be able to aggregate the income and expenses of a physical gift shop with a virtual gift shop.

- **Food Services**— A cafeteria, snack bar, and limited service restaurant all share the two-digit NAICS code 72. These activities could only be combined using a five or lower-digit NAICS Code (i.e., NAICS sector code 72, subsector code 722, industry group code 7225, or NAICS industry code 72251).

- **Advertising activities**— NAICS code 51 applies to advertising activity in a periodical and to advertising via a website. An organization would only be able to combine income and expenses from these similar advertising activities by using a two-digit NAICS code.

- **Rental Activities**— NAICS code 53 applies to non-residential property rentals, property management for these rentals, and personal property rentals, such as computer equipment. An organization would not be able to aggregate these activities using more than a two-digit NAICS code.

As part of the use of two-digit NAICS codes, we recommend that the Service permit aggregation of activities such as the ones described above. This approach is logical because similar activities may have overlapping expenses, depreciation, staff, etc. By grouping the activities together, an organization can accurately account for both its gains and losses from the overall activity.

We also believe that this approach is consistent with the legislative history of section

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512(a)(6). The House Ways and Means Committee in 2014 stated that the rationale behind the 512(a)(6) silo rule developed as a result of the Service’s Colleges and Universities report, which “detail[ed] how colleges and universities were abusing the unrelated business income tax (UBIT) rules by using loss-generating business activities to shelter gain from profitable businesses.”26 The Ways and Means Committee also observed that the unrelated business income tax rules were being modified to “address these and similar loopholes.”27 In the Colleges and Universities report, the Service categorized activities into broad codes, some of which aligned with NAICS and some of which (e.g., advertising) did not. In particular, the Colleges and Universities report focused on broad categories of activities such as advertising, facility rentals, conference centers, arenas, advertising, food service, and golf courses.28 Allowing organizations to group together their like activities, even using the two-digit industry NAICS Codes, would not frustrate Congressional intent. Losses from these aggregated activities still could not be used to offset gains in other silos, and the law provides that no individual silo may have income less than zero. Accordingly, even if an organization had significant losses in one silo, that amount would not act to reduce the gains in any other silo or the sum of the overall UBTI.

Finally, we recommend that regardless of the methodology Treasury and the Service implement, that the Service consider updates to the instructions to provide a more complete list of the applicable NAICS codes or state clearly in the instructions to the Form 990-T in large, bold font where additional codes can be obtained.

**Notice Sections 4 and 5 -- Investment Income.**

A. **Overview.**

The Notice indicates that Treasury and the Service consider investment income to be trade or business income, but that, as a matter of administrative convenience, Regulations would treat certain investment activities, including certain activities conducted indirectly through partnerships, as a single trade or business for the purposes of section 512(a)(6). The Notice requests guidance in defining investment activities of an exempt organization for the purposes of this UBTI silo.

As we stated in our June Comments, it is our view that investment income should not be classified as income from a trade or business for the purposes of section 512(a)(6) and therefore should not be subject to fragmentation at all. Our view is rooted in case law holding that an organization investing its own assets does not constitute a trade or business. In *Higgins v. Commissioner*, the US Supreme Court, discussing a predecessor to section 162, held that an individual taxpayer’s activities in managing his investments did not constitute a trade or business, “no matter how large the estate or how continuous or extended the work required may be . . . .”29 Further, section 513(c) defines “trade or business” by stating that, “for purposes of

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27 Id.
28 Supra Note 12, at Appendix C.
29 312 U.S. 212 (1941).
this section, the term ‘trade or business’ includes any activity which is carried on for the production of income from the sale of goods or the performance of services.” Investment income is not earned directly from the sale of goods or the performance of services, but rather by investing in somebody else’s trade or business. In the Notice, Treasury and the Service indicated disagreement with our suggestion, but they also recognized the administrative difficulty of separating out different sources of investment income.

We suggest, therefore, that if investment income is to be treated as subject to section 512(a)(6), then all investment income that is otherwise subject to the unrelated business income tax, including income and loss that is characterized as UBTI because of sections 512(b)(4), (13) and (17), be aggregated together in one silo -- taxable investment income.

As to income from partnerships:

1. Income from a partnership that is not controlled by the exempt organization should be allocated to the single investment income silo.

2. Income from controlled (as defined below) partnerships should be treated as follows:

   • Income or loss from a controlled partnership that is UBTI only because of section 512(b)(3), 512(b)(13) or 512(b)(17) should be allocated to the general investment income silo, rather than treated as a separate silo, assuming the exempt organization is clearly able to identify such income from the K-1 received from the partnership or based on its knowledge of the partnership because of its level of control.

   • Other trade or business income from a controlled partnership is effectively treated as being directly attributed to the exempt organization (not simply passed through) and therefore should be categorized by the exempt organization with its other activities using the two-digit NAICS code approach (assuming the exempt organization is reasonably able to assign a NAICS code to such income).

B. Definition of Investment Income.

It is difficult to define investment income for purposes of UBTI, because in general exempt organizations are not subject to unrelated business income tax with respect to investments. Under section 512(b), exempt organizations generally exclude from UBTI all of the types of income that arise from investment activities—dividends, interest, annuities, royalties, rents, and gains or losses from the sale, exchange or disposition of other property. In recognition of the uniqueness of investment-related UBTI, in its description of the revenue sources of exempt organizations, the legislative history of section 512(a)(6) discusses “investment income” as distinct from trade or business income.30 Therefore, as discussed below, we suggest a

definition of “investment income” that focuses not on the features that traditionally define investment -- such as passive involvement -- and instead on the unique circumstances in which the types of income that arise from investment activities -- like interest or rents -- create UBTI.

Another complication arises from partnerships. Under section 512(c), an exempt organization that is a partner in a partnership conducting an unrelated business must include in UBTI its distributive share of income associated with such business (reduced by its distributive share of related deductions). In light of this rule, the Notice recognizes the significant reporting and administrative burden that would result if the fragmentation principle under section 512(a)(6) were to require an exempt organization to distinguish between separate businesses conducted by partnerships in which it invests. Accordingly, the Notice contemplates that the “investment income” category of UBTI would include all income attributable to certain partnerships in which the exempt organization does not materially participate, without requiring the exempt organization to look through the partnership and distinguish between different underlying businesses. We read the Notice to permit aggregating the income and losses from all such partnerships.

Other commentators have suggested that the investment income category should be any passive investments that generate UBTI. We believe, however, that affirmatively defining this category by reference to its passive nature is administratively unfeasible and inappropriate given the unique circumstances subjecting exempt organizations to UBTI on investment income. The Notice specifically rejects the section 469 “material participation” standard as a means to determine whether a given activity is sufficiently passive to be viewed as an investment. We agree that applying section 469 principles to section 512(a)(6) is inappropriate, because the passive nature of an activity is not the hallmark that makes investment activity taxable as UBTI to exempt organizations.

Specifically, income streams that arise from investment activity are subject to UBTI in three key circumstances. Those income streams arise under section 512(b)(4) (relating to unrelated debt-financed income), section 512(b)(13) (relating to income from controlled entities), and section 512(b)(17) (relating to certain insurance income). Because these features—the presence of debt financing or control over the investment entity—are what turn investment income into UBTI for an exempt organization, we recommend that they also serve as the basis for a definition of investment activity under section 512(a)(6). Accordingly, any income that is subject to taxation under these three sections should fall within the general investment income silo, without further inquiry. Importantly, this treatment would include any income within these three categories that an exempt organization earns through controlled partnerships.

We also recommend that the general investment income silo should include any activity from a partnership that is not a controlled partnership. We think that this choice makes sense conceptually and administratively. Absent the unique circumstances outlined in the next section on controlled partnerships, exempt organizations generally view investments in partnerships as an investment. Furthermore, unless the exempt organization is actually involved in preparing partnership returns, it will generally be difficult or impossible for the exempt organization to attempt to peer through the partnership and segregate different business activities. Schedule K-1 does not provide an adequately granular breakdown of UBTI to permit exempt organizations to
segregate in this way. It would be administratively impractical (if not impossible) for exempt organizations and the Service if exempt partners attempted to obtain the necessary information outside of the bounds of the partnership reporting required by the tax law. Different exempt organization partners might take different approaches in how much information to seek and from whom and it might be difficult to obtain all necessary information from a partnership. This approach distinguishes and justifies the different treatment of income from partnerships and income from corporations, because partnerships can only be siloed at the partner level. Therefore, we think that the most administrable approach to non-controlled partnership investments -- an approach consistent with the substance of partnership investment and the principles of administrative ease articulated in the Notice -- is to include in the general investment income silo any investment in a partnership that is not subject to the rules described in the next section.

C. Recommendation and Reasoning

We believe that investment activity is different from trade or business activities and should not be subject to the section 512(a)(6) silo rules. If Treasury and the Service disagree, as the Notice suggests, then for purposes of administrative convenience, we recommend that all investment income, whether in a partnership or not, be placed in one general investment income silo.

The primary reason for this recommendation is that consolidating all investments in one silo would achieve one of the central goals stated by the Notice—easing the administrative burden for both the taxpayer and the Service. It may be difficult for exempt organizations to distinguish between different types of investments or to identify each underlying activity beneath a single investment. The investments may be structured through passthrough entities, for which information necessary to determine a specific silo may be unavailable.

Secondarily, this recommended framework aligns with and mirrors the economic realities of investments. An investment portfolio comprises all individual investments combined. Under modern portfolio theory that informs management of exempt organization investments, organizations focus on the entire portfolio of investments, with consideration of gain and loss in the portfolio as a whole. We believe that the tax treatment of the investments should follow these principles.

In addition, debt-financed property, or property subject to acquisition indebtedness under section 512(b)(4) and section 514, should be included in the general investment income silo because the acquisition of property can be considered an investment asset.

D. Example

Two examples illustrate our proposal:

Example (1): X is exempt under section 501(c)(3) and is not a private foundation. It directly operates a restaurant, the income from which is considered UBTI because it does not satisfy the convenience exception of section 513(a)(2). It also operates a gift shop where it sells
some items that generate UBTI under the fragmentation rule. X also owns a building that was financed with debt. X uses 50% of the building to operate a museum (its exempt purpose) and rents out the balance of the space for retail, thus generating UBTI under sections 512(b)(4) and 514. X has an endowment that it invests in stocks and bonds, but also in 30 partnerships, two of which it is deemed to control and which operate nearby restaurants. In 2018, one restaurant operated by partnership Y has a net loss and one operated by partnership Z has a net gain.

Under our proposal, X would treat the net income from the unrelated items in the gift shop as one silo and pay tax (two-digit NAICS code 45). If X generated a loss from the gift shop, it would report net income of zero on its Form 990-T. X would then aggregate the net income from the restaurant it owns directly with the net income/loss from the two partnerships that it controls because all fit within two-digit NAICS code 72. X would treat the debt-financed investment income from its building, along with its investment income from the 28 partnerships that it does not control, in one general investment income silo.

Example (2): The same facts as above except that X also has a controlled partnership that owns small interests in other partnerships that X does not control that make investments and that owns an 80% profits interest in LLC Q which operates a building construction company. X would allocate all income and loss from the partnerships to the general investment income silo, without the need for further analysis because they are not controlled partnerships. The income from Q is reported in a separate UBTI silo.

Notice Section 6 -- Controlled Partnerships.

An important part of applying the rule that we recommend in our response to Notice Sections 4 and 5, above, is a clear and concise test for determining when a partnership is controlled directly or indirectly by an exempt organization.

Notice Section 6.01(1) states that, except as specifically provided elsewhere, an exempt organization should use a “reasonable, good-faith interpretation of sections 511 and 514, considering all the facts and circumstances, when identifying separate trades or businesses” until Proposed Regulations are issued. Subject to the comments that follow, we agree with these general rules and support their inclusion in Proposed Regulations.

Notice Section 6.01(2) provides that, pending publication of Proposed Regulations, an organization may aggregate its UBTI from qualifying partnership interests (i.e., partnership interests that meet either the “De Minimis Test” or the “Control Test,” as discussed below) and treat the aggregate group as comprising a single trade or business. In our view, as discussed above, any income or loss from a partnership that is not controlled by the exempt organization should be allocated to the general investment income silo. For the reasons discussed above, we do not believe that investment income earned directly by an exempt organization should be aggregated in one silo with a separate silo for income that is aggregated from non-controlled partnerships. Our framework make sense because exempt organizations think about all of their investments as a whole and incur investment advisor and other expenses on their investments as a whole.
Also, as we discuss above, we believe that income or loss from a controlled partnership that is treated as UBTI only because of section 512(b)(4), 512(b)(13), or 512(b)(17) should be allocated to the general investment income silo and that the income of controlled partnerships should be considered as directly attributable to the exempt organization to the extent of its profits interest. Organizations should consolidate this income or loss with its other income and loss, using the two-digit NAICS code safe-harbor analysis. Exempt organizations that control a partnership should be in a good position to evaluate the character of its activities, income, and loss.

We believe that the best test for whether an organization controls a partnership comes from section 512(b)(13), a Code section that addresses precisely the issue of when an exempt organization controls another entity for purposes of the UBIT rules, specifically, whether the exempt organization owns more than 50% of the profits or capital interests in a partnership.

There is less of a logical connection between section 4943, which deals with excess business holdings and which also deals only with private foundations. Section 512(a)(6), of course, covers all exempt organizations, as does section 512(b)(13). Sections 512(a)(6) and 512(b)(13) both address UBTI directly.

We now analyze the two tests set forth in the Notice and provide comments.

A. *De Minimis* Test

Notice Section 6.02 provides that an exempt organization’s partnership interest meets the *De Minimis* Test if the interest is no more than 2% of the profits interest and no more than 2% of the capital interest. We believe a control test without a *De Minimis* Test would be more straightforward. However, if the Regulations adopt a *De Minimis* test, we suggest the following:

First, we recommend that the interest deemed to be *De Minimis* be increased to at least 5% to more accurately reflect the realities of partnership investments. This threshold would be consistent with other areas of the law where 5% operates effectively as a *De Minimis* threshold, including, for example, the FIRPTA rule that stock in a publicly traded corporation is not a U.S. real property interest unless the holder holds more than 5%.  

Second, the Notice provides that, for purposes of the *De Minimis* Test (section 6.02(2)) and the Control Test (section 6.03(2)), an exempt organization may rely on the Schedule K-1 it receives from the partnership. An exempt organization will be considered to have no more than 2% of the interest in the partnership if the average of the exempt organization’s percentage interest at the beginning and end of the year, or (in the case of an interest held for less than a year) at the beginning and end of the period of ownership during the partnership’s year, is no more than 2%. If no specific profits interest is identified in Part II, Line J of the Schedule K-1, the exempt organization does not meet the *De Minimis* Test.

If a *De Minimis* Test is to be implemented, we recommend that Treasury and the Service provide phase-in and grace periods to address certain delays and fluctuations that are beyond the

31 I.R.C. § 897(c).
control of an exempt organization. Specifically, we recommend that holdings for a new partnership be calculated as of the date of the final closing of the partnership, so long as such final closing is no more than 18 months following the partnership’s initial closing. In addition, we recommend that Proposed Regulations provide that an exempt organization is permitted up to 90 days to reduce its interest in a partnership below the relevant limits in any case where its percentage interest increased because of another partner’s withdrawal or percentage reduction. This type of provision would be similar to the 90-day grace period under section 4943 for excess business holdings acquired other than by purchase.

Finally, the section 4943 de minimis rule provides that a private foundation must combine its interests in a partnership that is a business entity with the interests of its disqualified persons only if the foundation (together with certain other foundations) owns more than the stated interest in the partnership. In other words, no combination is required if the foundation (together with certain other foundations) itself owns not more than a de minimis interest in the partnership. For that reason, we recommend that if the Proposed Regulations include a De Minimis Test, it align with section 4943 to provide that an exempt organization’s interests need not be combined with those of any disqualified person, controlled entity, or supporting organization in applying the De Minimis Test. If combination is required, we recommend that it be limited to Type I and Type II supporting organizations for public charities and be treated as it is now under Section 4943 for private foundations.

B. Control Test

Notice Section 6.03(1) provides that an exempt organization’s partnership interest meets the Control Test if the exempt organization (i) directly holds no more than 20% of the capital interest of the Partnership (“Prong 1”); and (ii) does not have control or influence over the partnership (“Prong 2”).

Prong 1 as proposed focuses on an exempt organization’s capital interest in a partnership and sets the threshold at 20%. A partner that holds 20% of the capital interests in a partnership usually is not able to control the partnership, absent other factors. In many areas of tax law, control is determined by more than 50% ownership, and importantly this is the standard in Section 512(b)(13), a related UBTI provision. We continue to recommend that “control” be based on at least majority ownership (e.g., more than 50%), as noted in our June Comments. If the standard is more than 50%, based on section 512(b)(13), then it also makes sense to base the test on capital or profits interests. If, however, the test is 20%, based on Section 4943, then the test should probably be based on profits interests only, and not on capital interests, for consistency with section 4943.

Notice Section 6.03(3) provides that “all facts and circumstances” are relevant in determining whether an exempt organization has control or influence over a partnership for purposes of Prong 2 of the Control Test. We agree that a subjective component is appropriate here and support its inclusion in Proposed Regulations. We recommend that the examples of what may satisfy the subjective test be revised to more accurately reflect partnership structures and control in investment contexts. For example, many exempt organization investors have the right to appoint representatives to an investor committee or advisory body. Such a right does not
evidence “control,” but arguably constitutes the right to participate in or influence management. Similarly, many exempt organization investors have the right to vote for, approve, or reject the appointment or removal of a general partner of a limited partnership or a managing member of a limited liability company. Such a right, while arguably a right to influence the management of the partnership, does not, in our view, evidence control. We therefore recommend that Treasury and the Service clarify in Proposed Regulations that the following do not constitute “control or influence over the partnership” in this context: (a) the right to vote for the appointment or removal of a general partner or managing member, (b) the ability to appoint representatives to investor committees or advisory committees, or (c) the right to approve the selection or removal of a general partner or managing member.

Under Prong 2, Notice Section 6.03(3) also provides that an exempt organization has control or influence over a partnership if the exempt organization has the power to appoint or remove any of the partnership’s officers, directors, trustees, or employees. We recommend that Proposed Regulations remove the specific references to officers, directors, or trustees. We recommend instead saying “has the power to appoint or remove at least a majority of the partnership’s governing body, however that body is configured.” While many organizations classified as partnerships may have officers, directors or trustees, many do not.

Each of the De Minimis Test (section 6.02(2)(b)) and the Control Test (section 6.03(1)) requires that, in measuring the exempt organization’s applicable percentage partnership interest, the exempt organization combine its direct interest with that of any disqualified person, supporting organization, or controlled entity. Further, the definition of “disqualified person” for these purposes is the definition set forth in section 4958(f). We have already described above why, for purposes of the De Minimis Test, we do not believe it is necessary to look at the interests of disqualified persons. If the Proposed Regulations are to use a de minimis test based on section 4943, then that test should parallel Section 4943 and not include the interests of disqualified persons.

For purposes of the Control Test, private foundations are required to track holdings of “disqualified persons” as defined in section 4946 for purposes of the section 4943 excess business holdings rules (as well as for several other purposes). Many private foundations have entered into agreements with fund managers that require the managers to monitor and track interests of disqualified persons so that the foundations can take appropriate corrective action if a concern about an excess business holding arises. We do not object to private foundations having to use the same tracking under section 4946 for purposes of section 512(a)(6) as they already use for purposes of section 4943. However, requiring them to employ one tracking system for section 4943 and another based on section 4958 for section 512(a)(6) would be time consuming and complex. If private foundations are going to have to attribute the interests of disqualified persons for purposes of this test, we strongly recommend that they be allowed to use the same definition of disqualified person that they are already using in other contexts.

For public charities, we believe that any system that requires tracking of disqualified persons, even using section 4958, would be extraordinarily burdensome. It would be exceptionally complex for many public charities – such as a university with 25 trustees, many officers and thousands of major donors –to apply those rules to every single partnership
investment in their portfolio, especially those involving fund of funds and tiered partnerships. We recommend eliminating attribution rules with respect to the control rule for non-private foundations.

If Treasury and the Service do not accept our recommendation, and the Proposed Regulations require use of section 4958, consideration of supporting organizations becomes important. Public charities often form supporting organizations to achieve a variety of goals, including management of significant fundraising gifts, management of investment assets, and segregation of certain activities. Requiring a public charity to combine its partnership interests with those of its supporting organizations for purposes of the UBTI siloing rules is inconsistent with the separate existence and governance of those supporting organizations. Further, a public charity may not have access to detailed information about the investment interests of their supporting organizations and supporting organizations may be on different tax years from some of their supported organizations. Accordingly, we recommend that an exempt organization’s interests not be combined with those of its supporting organizations for these purposes. However, if combination is required, we recommend that it be limited to Type I and Type II supporting organizations.

In summary, we recommend that Proposed Regulations:

1. Use the 50% rules for control from section 512(b)(13), thereby bringing in all the Regulations, rulings, and cases thereunder;
2. If the Proposed Regulations are based on section 4943, instead of section 512(b)(13), then:
   - Do not use a *De Minimis* rule, but if a *De Minimis* rule is adopted, use 5% rather than 2%;
   - Do not require attribution under the *De Minimis* test.
   - Any attribution under the Control Test be based on section 4946 for private foundations and not be required for non-private foundations.

Section 7 -- Social Clubs and VEBAs.

The Notice requests comments on any additional considerations to how section 512(a)(6) applies within the context of section 512(a)(3). In particular, Treasury and the Service request comments regarding how these exempt organizations’ investment income should be treated for purposes of section 512(a)(6).

Section 512(a)(3) provides as follows:

In the case of an organization described in paragraph (7), (9), (17), or (20) of section 501(c), the term “unrelated business taxable income” means the gross income (excluding any exempt function income), less the deductions allowed by this chapter which are directly connected with the production of the gross income (excluding exempt function income), both computed with the modifications
provided in paragraphs (6), (10), (11), and (12) of subsection (b). For purposes of the preceding sentence, the deductions provided by sections 243 and 245 (relating to dividends received by corporations) shall be treated as not directly connected with the production of gross income.

Under section 512(a)(3), for organizations such as social clubs and VEBAs, most income generated from sales or services to non-members is considered as UBTI, most investment income is treated as UBTI, and the exceptions under Section 512(b) exclude investment income. Because of this important distinction, it may be necessary to develop special rules for organizations such as VEBAs and social clubs.

We suggest that social clubs treat any income from non-members (that is otherwise subject to UBTI) in the same manner that other exempt organizations categorize their income, using the two-digit NAICS code, as discussed above. As an example, if a social club derives income from renting out its facility to non-members for private events and also serves non-members, from time to time, in its restaurant or bar, all such income and related expenses would be aggregated together as they are derived from the same type of trade or business.

We also recommend that investment income of social clubs and VEBAs be treated as one trade or business, as we have recommended for other types of exempt organizations. We also would apply whatever rules for income from partnerships are developed for other exempt organizations to also apply to VEBAs and social clubs.

Section 8 – Section 512(a)(7) income.

The Notice indicates that any deemed UBTI resulting from the application of section 512(a)(7) is not derived from an unrelated trade or business, but is nonetheless subject to the UBIT. This rule /decision raises two issues:

First, we request that the Service develop a practical solution so that exempt organizations that do not otherwise file a Form 990-T have a simple way to pay tax on this deemed income without the need to file a full Form 990-T. Perhaps a simple short-form voucher could be filed with quarterly or annual payments.

Second, we recommend that the Proposed Regulations address what, if any, UBTI losses can be used to offset deemed income under section 512(a)(7). We have identified three possible scenarios:

a. If an exempt organization has a single trade or business and that trade or business has losses, then the losses from that activity should be available to offset section 512(a)(7) deemed income. This conclusion seems reasonably clear.

b. The more complicated question is the situation in which an exempt organization has losses from more than one trade or business. We understand that an exempt organization that has more than one trade or business is subject to the silo rules of Section 512(a)(6) and is not

32 see I.R.C. §§ 512(b)(1) et. seq.
allowed to report income of less than zero from any activity or to use losses from one activity to
offset gains from another. The draft instructions to the 2018 draft Form 990-T suggest that
deeded income from section 512(a)(7) is to be reported in addition to, and separately from, the
net income from any siloed activity. In this way, organizations that are subject to the silo rule
may be disadvantaged compared to organizations that have losses from only one trade or
business because they will not be able to use losses from any activity to offset section 512(b)(7)
deemed income.

If Treasury and the Service do not permit organizations with more than one trade or
business to offset losses against section 512(a)(7) deemed income, we believe that larger, more
sophisticated organizations with several unrelated trades or businesses will structure their affairs
to maximize their use of losses, while smaller organizations will be unable to do so and will pay
a higher percentage of tax. As an example, Hospital A has taxable income under section
512(a)(7). It also has losses from a pharmacy and losses from a café that it operates across the
street from the hospital. Hospital A would be well advised to move the café into a wholly owned
taxable corporation that will pay no tax because it has little or no net income. In that way, it has
only one unrelated trade or business, the pharmacy, the losses from which can offset the
512(a)(7) deemed income.

We believe that the more consistent and equitable approach would be to permit
organizations that are subject to the silo rules to use losses from any activity to offset the deemed
income from section 512(a)(7).

Section 9 – Net Operating Losses.

In addition to changing the rules surrounding UBTI, the Act also modified how
organizations calculate their net operating losses (“NOLs”). Section 172 now provides that an
organization is limited in its NOL deduction to 80% of taxable income for losses arising in
years beginning after December 17, 2017. Additionally, organizations may now carry
forward their post-December 2017 NOLs for an indefinite period. Finally, organizations can
no longer carry back their NOLs.

We recommend that the Proposed Regulations address how these modifications to the
rules for NOLs operate in conjunction with the rules under section 512(a)(6) and with the
language from section 13702(b)(2) of the Act. Under that provision, organizations with NOLs
incurred prior to 2018 do not have to calculate those historic NOLs within a silo. The section
provides:

(2) CARRYOVERS OF NET OPERATING LOSSES.—If any net operating
loss arising in a taxable year beginning before January 1, 2018, is carried
over to a taxable year beginning on or after such date—

(A) subparagraph (A) of section 512(a)(6) of the Internal Revenue Code of

33 I.R.C. § 172(a).
34 I.R.C. § 172(b)(2).
35 I.R.C. § 172(b)(1).
1986, as added by this Act, shall not apply to such net operating loss, and

(B) the unrelated business taxable income of the organization, after the application of subparagraph (B) of such section, shall be reduced by the amount of such net operating loss.

Read together, all these sections—section 512(a)(6), section 172, and section 13702(b)(2) of the Act appear to mean that NOLs incurred within a silo, after 2017, can be carried forward indefinitely to offset up to 80% of the income in the same silo.

However, a post-2017 NOL from silo A cannot be used to offset income in silo B. Additionally, it appears that all pre-2018 NOLs can be carried forward (for up to 20 years) to offset total UBTI outside of any specific silo.

Assuming this interpretation is accurate, a number of unanswered questions remain, including the following:

- Do the traditional NOL rules requiring a first in, first out approach apply? If so, then the NOLs incurred prior to 2018 would be used first to offset any net income, whether it is in a silo or not. The language contained in section 13702(b) of the Act makes the order of operations unclear. Taking into account the language in section 172, however, we believe that this order is the appropriate result.

- What happens to post-2017 NOLs in a silo if the exempt organization is no longer operating that silo? Presumably the NOLs would be lost, absent other authority. However, if the organization later resumed the activity that created the post-2017 NOL, could it recapture the NOL given the indefinite carryforward period of section 172? We believe that it should be able to do so.

- Will repeated NOLs in a specific silo continue to be an indicator for examination because the activity may not be a trade or business? Section 512(a)(6) was intended to prevent organizations from using loss-generating activities to decrease overall UBTI, and the silo requirement largely alleviates the concern that an organization would operate an activity at a loss to offset other income. Accordingly, even if the activity in a silo continues to generate losses, the activity will continue to be treated as a trade or business.

- When does an organization take into account its charitable deduction under section 512(b)(10) and how does that work with two new classes of NOLs – pre-2018 NOLs that are not in silos and post-2017 NOLs that are in silos? Under section 170(d)(2), an organization may take into account current year contributions and then carryover contributions in the order that they arose (with a limited carryover period of 5 taxable years). Additionally, section 170(d)(2)(B) provides a special rule when there are NOL carryovers to prevent organizations from having a double tax benefit. The Service has considered in other contexts the appropriate methods of calculating charitable contributions where there is not statutory guidance. For example, in Chief Counsel Advice, the Service considered how to simultaneously calculate a charitable
contribution deduction limit and the alternative minimum tax net operating loss
deduction. In addition to providing guidance on net operating losses, organizations
also need guidance on the charitable deduction calculation.

Section 10 -- Global Intangible Low-Taxed Income.

Notice Section 10 concludes that exempt organizations are not required to include as
UBTI any global intangible low-taxed income (or “GILTI”) which is included in gross income
under section 951A. We agree; such income is not UBTI under general tax principles.

36 CCA 201226021 (Jun. 29, 2012).
Supplement 3

Ropes & Gray LLP Alert on Notice 2018-67
August 23, 2018

IRS Issues Guidance on UBTI Silos and Other UBTI-Related Tax Reform Provisions

In Notice 2018-67, issued August 21, 2018 (the “Notice”), the IRS has provided interim guidance – including rules on which tax-exempt organizations may rely pending proposed regulations – on aggregation of activities under the new unrelated business taxable income (UBTI) “silos” rule. The Notice also addresses other issues related to the silo rule, including debt-financed UBTI, net operating loss (NOL) ordering rules, the new fringe benefit UBTI rule, and the new global intangible low-taxed income (GILTI) inclusions.

The UBTI Silo Rule. Section 512(a)(6) of the Code, enacted by the Tax Cuts and Jobs Act in December 2017, requires a tax-exempt organization to compute UBTI separately with respect to each unrelated trade or business of the organization, effective for tax years beginning after December 31, 2017. The new rule in general prevents tax-exempt organizations from offsetting UBTI generated by a profitable unrelated trade or business with a loss from an unprofitable one. However, the statute left unclear the scope of the activities that could be grouped together as a single unrelated trade or business.

“Reasonable, Good-Faith Interpretation” Standard. The Notice permits tax-exempt organizations to “rely on a reasonable, good-faith interpretation” of Sections 511-514 of the Code in determining whether they have more than one unrelated trade or business, pending issuance of proposed regulations. A good-faith interpretation must consider all the facts and circumstances. The IRS has requested comments on possible methods to identify separate trades or businesses; however, the Notice also states the IRS will consider an organization’s groupings of activities to be reasonable and in good faith if the organization uses the 6-digit codes of the North American Industry Classification System (NAICS). The NAICS is a standard used by Federal agencies to classify businesses for statistical purposes, and IRS Form 990-T requires organizations to list one or more codes based on the NAICS list to describe their unrelated trade or business activities.

Interim and Transition Rules for Partnership Investments. In addition to the general reasonable, good-faith standard, the Notice provides two reliance rules specifically for aggregating partnership interests and activities for purposes of the UBTI silo rule, acknowledging the administrative burden associated with investments in multi-tier partnership structures.

“Interim Rule”: Aggregate all “Qualifying Partnership Interests.” Until proposed regulations are issued, a tax-exempt organization may treat a “qualifying partnership interest” as a single trade or business (even if the partnership is engaged, directly or indirectly through underlying partnerships, in multiple trades or businesses), and may further aggregate all of its qualifying partnership interests together as a single trade or business. In order to be a qualifying partnership interest, a partnership interest must meet the requirements of either the “de minimis” test or the “control” test.

- De minimis test: The de minimis test is met if a tax-exempt organization holds directly no more than two percent of the profits interest and no more than two percent of the capital interest in the partnership. If no specific profits interest is identified in Schedule K-1, the de minimis test is not met.
- Control test: The control test is met if a tax-exempt organization holds no more than 20 percent of the capital interest in, and, based on all the facts and circumstances, does not have control or influence over,
the partnership. The application of this control or influence standard is unclear; for example, it is unclear
whether membership on a limited partner advisory committee (LPAC) may constitute control or
influence. The Notice does not specify whether the organization is eligible under the control test if
Schedule K-1 does not specify the organization’s percentage interest.

For both tests, the interest of a disqualified person, a supporting organization, or a controlled entity (within the
meaning of Section 512(b)(13)) in the same partnership will be taken into account in determining the tax-exempt
organization’s percentage interest.

“Transition Rule”: Treat Each Current Holding as One Trade or Business. Regardless of whether the *de
minimis* test or control test is met, a tax-exempt organization may treat a partnership interest acquired prior to
August 21, 2018 as constituting a single trade or business, whether or not the partnership directly or indirectly
conducts more than one trade or business. These partnership interests are not “qualifying partnership interests”
and therefore are not automatically eligible for aggregation with other interests; however, they may be eligible
for aggregation with other interests under the general good-faith reasonable grouping standard discussed above.
The Notice does not specifically state whether capital contributions made subsequent to August 21 affect a
partnership’s eligibility to qualify under the transition rule.

Practical Implications. In practical terms, the interim rule would permit an organization to aggregate all private
investment fund interests for funds in which it holds no more than 20% of the fund’s capital and over which it
does not have control or influence. “Funds of one,” direct investments and certain joint ventures, by contrast,
may qualify only for the transition rule permitting each partnership interest to be treated as comprising a single
trade or business, and may not be covered by either the interim or the transition rule if acquired on or after
August 21, 2018. However, it may be possible to group transition rule-eligible interests or newly acquired
partnership interests with other activities into a single trade or business under the general, good-faith
interpretation rule described above.

Other Issues

**Aggregation of Debt Financed Income.** The Notice states that a tax-exempt organization may aggregate unrelated
debt-financed income from a qualifying partnership interest with other UBTI from its qualifying partnership
interests, and may aggregate unrelated debt-financed income from a transition rule-eligible partnership interest with
other unrelated business income or loss from that partnership interest. The Notice does not address the treatment of
debt-financed income outside the partnership context.

**Ordering of Net Operating Losses.** NOLs generated in taxable years beginning before January 1, 2018 may be used
in subsequent years with no siloing limitation. However, because UBTI must be calculated separately for each trade
or business before calculating total UBTI for taxable years beginning on or after January 1, 2018, it appears post-
2017 NOLs should be calculated and taken before pre-2018 NOL carryovers are taken. However, if read as imposing
such an ordering rule, Section 512(a)(6) could lead to the expiration of unused pre-2018 NOLs that remain subject to
20-year expiration under prior law. The Notice requests comments on this issue and any other issues relating to the
interaction of Section 512(a)(6) with Section 172, but does not provide guidance.

**Transportation and Parking Fringes.** The Tax Cuts and Jobs Act enacted new Section 512(a)(7), which requires tax-
exempt organizations to include as UBTI costs incurred associated with providing certain employee fringe benefits.
The Notice states that while Section 512(a)(7) imposes UBTI, the IRS does not consider providing employee
transportation or parking benefits to be an unrelated trade or business, and therefore UBTI arising from these fringe
benefits under Section 512(a)(7) is not subject to the Section 512(a)(6) silo rule.
Global Intangible Low-Taxed Income (GILTI). The Notice states that GILTI income inclusions under new Section 951A of the Code are treated as dividends, and are not treated as UBTI unless they constitute debt-financed income under Section 512(b)(4). In addition, GILTI income inclusions attributable to insurance income will not be treated as UBTI unless provided otherwise in proposed regulations.

Comments Requested. The Notice also outlines the current thinking of the Treasury and IRS relating to the contents of proposed regulations to be issued in the future on these issues, and requests public comments. Comments should be submitted on or before December 3, 2018.

While the Notice provides clarity on certain of the issues presented by the UBTI silo rule and the other issues discussed above, the guidance provided in the Notice is complex and leaves some questions unanswered. If you have any questions about the Notice or tax reform more generally, please contact a member of the tax group or the tax-exempt organizations practice.
Supplement 4

Notice 2019-9
Interim Guidance Under Section 4960

Notice 2019-09

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I. PURPOSE AND OVERVIEW

This notice provides interim guidance regarding section 4960 of the Internal Revenue Code (Code), enacted on December 22, 2017, pursuant to section 13602 of Tax Cuts and Jobs Act, Pub. L. No. 115-97 (the Act). Section 4960(a) imposes an excise tax equal to the rate of tax under section 11 (currently 21 percent) on the amount of remuneration in excess of $1 million and any excess parachute payment paid by an applicable tax-exempt organization to a covered employee.

The interim guidance is intended to assist taxpayers in applying section 4960 while the Department of the Treasury (Treasury Department) and the Internal Revenue Service (IRS) develop further guidance on the application of section 4960, and addresses certain issues under section 4960 on which stakeholders have indicated that they would benefit from interim guidance. Specifically, the Treasury Department and the IRS intend to issue proposed regulations on the amendments made by section 13602 of the Act that will incorporate the guidance provided in this notice. However, as provided in Section IV of this notice, any future guidance under section 4960 will be prospective and will not apply to taxable years beginning before the issuance of that guidance. Until further guidance is issued, to comply with the requirements of section 4960, taxpayers may base their positions upon a good faith, reasonable interpretation of the statute, including consideration of the legislative history, if appropriate. The positions reflected in this notice constitute a good faith, reasonable interpretation of the statute. Whether a taxpayer’s position that is inconsistent with this notice constitutes a good faith, reasonable interpretation of the statute generally will be determined based upon all of the relevant facts and circumstances, including whether...
the taxpayer has applied the position consistently and the extent to which the taxpayer has resolved interpretive issues based on consistent principles and in a consistent manner. Notwithstanding the previous sentence, this preamble describes certain positions that the Treasury Department and the IRS have concluded are not consistent with a good faith, reasonable interpretation of the statutory language. The Treasury Department and the IRS intend to embody these positions as part of the forthcoming proposed regulations.

Comments are requested on all aspects of this notice. See Section III of this notice regarding requests for comments on specific aspects of this notice and for information on how to submit comments.

A. **Section 4960 — In General**

Section 4960(a) of the Code generally provides that an applicable tax-exempt organization (ATEO), or a related organization, that pays remuneration in excess of $1 million or any excess parachute payment to a covered employee is subject to an excise tax on the amount of the excess remuneration and excess parachute payments at a rate equal to the rate of tax imposed on corporations under section 11 (currently 21 percent).

Section 4960(a)(1) refers to remuneration paid “for the taxable year,” but does not specify which taxpayer's taxable year is used, what it means for remuneration to be paid “for” a taxable year, or how to measure remuneration if an ATEO and a related organization have different taxable years. Q/A–2 provides that the excise tax imposed on excess remuneration and excess parachute payments is determined based on remuneration paid and excess parachute payments made in the calendar year ending
with or within the taxable year of the employer. This measurement period, as commenters suggested, will reduce the administrative burdens that would arise if taxpayers were required to allocate remuneration paid during a single calendar year to multiple non-calendar taxable years. Moreover, this approach will reduce administrative burdens by aligning more closely with the calendar year reporting of compensation on Form W-2, Wage and Tax Statement, and Form 990, Return of Organization Exempt From Income Tax.

Some commenters recommended that ATEOs and related organizations be allowed, but not required, to treat remuneration paid during the calendar year ending with or within the taxable year of the employer as remuneration paid “for the taxable year” under section 4960(a)(1). Commenters recommended this rule be elective in order for non-calendar year taxpayers to avoid the potential inclusion of remuneration for a period prior to the effective date of section 4960 (the first taxable year beginning after December 31, 2017). Q/A–13 and Q/A–39 avoid that result by treating remuneration in which the covered employee vested before the effective date of section 4960 as paid before that effective date. Because these Q/As address the issue raised by the commenters, the Treasury Department and the IRS have concluded that an election for the remuneration measurement period is unnecessary.

The guidance in this notice provides rules regarding the entity that is liable for the excise tax under section 4960, and how that excise tax is calculated. Q/A–3 provides that the common-law employer, as determined generally for federal tax purposes, is liable for the excise tax imposed under section 4960. A common-law employer may not avoid treating a payment as remuneration under section 4960 by reason of a third party
payor arrangement. A payment to the employer’s employee from a third party payor (including a payroll agent, common paymaster, statutory employer under section 3401(d)(1), or certified professional employer organization) or from an unrelated management company, is considered a payment to the employee from the common-law employer. Similarly, a payment to the employee from a related entity, including a related entity that is an ATEO, for services rendered to the common-law employer, is considered a payment to the employee from the common-law employer for purposes of calculating remuneration and determining liability for the excise tax. Q/A–3 also clarifies that calculation of the excise tax is separate from any arrangement that an ATEO and any related organization may have for bearing the cost of the excise tax under section 4960.

One commenter requested guidance providing that remuneration paid by a separate employer that is a related for-profit or governmental entity (other than an ATEO) is taken into account in determining whether a covered employee has remuneration in excess of $1 million, but that the related entity is not liable for its share of the excise tax under section 4960. There is no statutory support for creating such an exception for for-profit and governmental entities. Section 4960(c)(4)(B), which defines related organizations, applies to any “person or governmental entity” that meets any of the relationship tests in section 4960(c)(4)(B)(i)-(v). Unlike the definition of an ATEO under section 4960(c)(1)(C), which applies only to a governmental entity that excludes
income from taxation under section 115(1),\textsuperscript{1} section 4960(c)(4)(B) applies to any “governmental entity” that is related to an ATEO. Similarly, a for-profit entity is a “person” under generally applicable tax principles. In addition, excepting for-profit entities from liability as related organizations would be inconsistent with section 4960(c)(6), which coordinates the tax on excess parachute payments with the section 162(m) deduction limitation (which only applies to for-profit entities). Further, section 4960(c)(4)(C), which describes the liability for the excise tax, refers to any case in which remuneration from more than one employer is taken into account, stating that “each such employer” shall be liable, without qualification as to the employer’s status as an ATEO. For these reasons, the Treasury Department and the IRS have concluded that the position that a for-profit or governmental entity that is a related organization with regard to an ATEO is not liable for its share of the excise tax under section 4960 is not consistent with a good faith, reasonable interpretation of the statute.

Some ATEOs will not be impacted by section 4960 because they do not pay an employee enough remuneration to trigger the tax. There can be no excess remuneration under section 4960(a)(1) if an ATEO (together with any related organization) pays remuneration of less than $1 million to each of its employees for a

\textsuperscript{1} Section 4960(c)(1)(C) refers to an entity that “has income excluded from taxation under section 115(1).” However, section 115(1) refers to income that is excluded from gross income. For consistency with the language in section 115(1), this notice refers to an entity that “has income excluded from gross income under section 115(1),” except where directly quoting section 4960(c)(1)(C).
taxable year, and there can be no excess parachute payment under section 4960(a)(2) if the employer does not have any “highly compensated employees” under section 414(q)\(^2\) for the taxable year. In that case, no excise tax under section 4960 is owed. For example, an ATEO that does not pay compensation (within the meaning of section 414(q)) of $125,000 or more to any employee in 2018 and 2019 is not subject to excise tax under section 4960 for 2019.

However, there is no minimum dollar threshold for an employee to be a covered employee. Even if an ATEO has no liability under section 4960 for one year, the ATEO may later need to determine its five highest-compensated employees for that taxable year, as those employees continue be covered employees in all future years and may be paid excess remuneration or excess parachute payments in a future year.

**B. Applicable Tax-Exempt Organizations and Related Organizations**

Section 4960(c)(1) provides that an “applicable tax-exempt organization” is any organization that for the taxable year—(A) is exempt from taxation under section 501(a), (B) is a farmers’ cooperative organization described in section 521(b)(1), (C) has income excluded from taxation under section 115(1), or (D) is a political organization described in section 527(e)(1).

One commenter requested clarification on the application of section 4960 to governmental entities. Q/A–5 clarifies that certain governmental entities are not ATEOs within the meaning of section 4960(c)(1). A governmental entity (including a state

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\[\text{\hspace{1cm}2 The limitation used in the definition of highly compensated employee under section 414(q)(1)(B) is adjusted for inflation. For 2019, the limitation is } $125,000. \text{ Notice 2018-83, 2018-47 I.R.B. 774.}\]
college or university) that is not recognized as exempt from taxation under section 501(a) and does not exclude income from gross income under section 115(1) is not an ATEO described in section 4960(c)(1). Conversely, a governmental entity that excludes income from gross income under section 115(1) (even if the entity has other income that is not excluded from gross income under section 115(1)), or is recognized as exempt from taxation under section 501(a), is an ATEO described in section 4960(c)(1).

Q/A–6 clarifies that a governmental entity that sought and received a determination letter recognizing its tax-exempt status under section 501(c)(3) may relinquish this status pursuant to the procedures described in section 3.01(12) of Rev. Proc. 2018-5, 2018-1 I.R.B. 233, 239. However, an entity that excludes income from gross income under section 115(1) is an ATEO regardless of whether it has a private letter ruling to that effect.

Section 4960(c)(4)(A) provides that remuneration paid to a covered employee by an ATEO includes any remuneration paid with respect to employment of the employee by any related person or governmental entity. The Treasury Department and the IRS interpret the phrase “any related person or governmental entity” to include not only related ATEOs but also related taxable organizations and related governmental units or other governmental entities. Section 4960(c)(4)(B) provides that a person or governmental entity is related to an ATEO if such person or governmental entity—

(i) controls, or is controlled by, the organization; (ii) is controlled by one or more persons which control the organization; (iii) is a supported organization (as defined in section 509(f)(3)) during the taxable year with respect to the organization; (iv) is a
supporting organization described in section 509(a)(3) during the taxable year with respect to the organization; or (v) in the case of an organization which is a voluntary employees’ beneficiary association described in section 501(c)(9), establishes, maintains, or makes contributions to such voluntary employees’ beneficiary association.

For purposes of defining “control” within the meaning of section 4960(c)(4)(B)(i)-(ii), Q/A–8 provides rules based on the definition of control under section 512(b)(13)(D). Thus, the definition of related organization for purposes of section 4960 generally aligns with the definition of related organization for purposes of the annual reporting requirements on Form 990, reducing the burden on organizations in identifying related organizations, calculating compensation from related organizations, and determining liability under section 4960.

Q/A–8 does not adopt the test for control under section 414(b) and (c), which generally uses the same test for control of a nonprofit organization as section 512(b)(13)(D) except that it replaces the 50 percent threshold with an 80 percent threshold. Instead, Q/A–8 adopts the control test under section 512(b)(13)(D) for the administrative convenience of taxpayers, to align more closely with other exempt organization control tests, and to prevent abuse that may occur in the section 4960 context under the higher 80 percent control threshold that was established for qualified plans.

C. **Covered Employees**

Section 4960(c)(2) defines a covered employee as any employee who is one of an ATEO’s five highest-compensated employees for the current taxable year or who was a covered employee of the ATEO (or any predecessor) for any preceding taxable
year beginning after December 31, 2016. Therefore, once an employee is a covered employee, he or she continues to be a covered employee for all subsequent taxable years. There is no minimum dollar threshold for an employee to be a covered employee; thus, an employee need not be paid excess remuneration or an excess parachute payment nor be a highly compensated employee within the meaning of section 414(q) to be a covered employee for a taxable year and all future years.

Commenters requested that the Treasury Department and the IRS provide a rule of administrative convenience under which a covered employee is no longer considered a covered employee of an ATEO after a certain period of time. The guidance in this notice does not adopt that suggestion because it is inconsistent with the statute. For this reason, the Treasury Department and the IRS have concluded that the position that a covered employee ceases to be a covered employee after a certain period of time is not consistent with a good faith, reasonable interpretation of the statute.

Section 4960 does not provide rules for identifying an ATEO’s five highest-compensated employees for a taxable year. Q/A–10 provides that whether an employee is one of an ATEO’s five highest-compensated employees is based on remuneration paid in the calendar year ending with or within the employer’s taxable year. The Treasury Department and the IRS considered using certain existing reporting standards for determining the amount of compensation paid, such as the Securities and Exchange Commission standards that are used for section 162(m) purposes or the standards that are used for Form 990 reporting purposes. However, Q/A–10 uses remuneration paid for purposes of identifying an ATEO’s five highest-compensated employee because, as defined in Q/A-12, remuneration is a fair representation of
compensation earned by an employee and it is more administrable to use a single standard for both identifying covered employees and computing the tax, if any, imposed by section 4960(a)(1). In addition, having the calendar year ending with or within the ATEO’s or related organization’s taxable year as the measurement period for identifying the ATEO’s five highest-compensated employees is consistent with the measurement period for purposes of determining remuneration paid for a taxable year.

Q/A-10 provides that remuneration paid for medical services is not taken into account for purposes of identifying the five highest-compensated employees. One commenter requested that remuneration paid for medical services be taken into account for purposes of determining the five highest-compensated employees. An interpretation that remuneration for medical services is taken into account for purposes of identifying the five-highest compensated employees would be inconsistent with the statutory structure and the legislative intent, and therefore the Treasury Department and the IRS have concluded that this interpretation is not consistent with a good faith, reasonable interpretation of section 4960. As the Conference Report to accompany H.R. 1 (Conference Report) states, “[f]or purposes of determining a covered employee, remuneration paid to a licensed medical professional which is directly related to the performance of medical or veterinary services by such professional is not taken into account, whereas remuneration paid to such a professional in any other capacity is taken into account.” H.R. Rep. No. 115-466, at 494 (2017) (Conf. Rep.).

As set forth in Q/A–9, only an ATEO’s common law employees (including officers) can be one of an ATEO’s five highest-compensated employees. To identify its five highest-compensated employees, the ATEO must include remuneration paid for the
taxable year by any related organization, including remuneration paid by a related for-profit organization or governmental entity, for services performed as an employee of such related organization. Q/A–12(c) also provides that remuneration paid by a separate organization on behalf of the ATEO, whether related to the ATEO or not, for services performed as an employee of the ATEO is treated as remuneration paid by the ATEO for purposes of section 4960. To prevent circumstances in which an employee to whom the ATEO paid minimal remuneration displaces an employee who would otherwise be a covered employee of the ATEO, Q/A–10(b) provides a limited services exception under which, unless an ATEO pays at least 10 percent of the total remuneration paid by the ATEO and all related organizations to an employee during the calendar year, the employee is not treated as one of the ATEO’s five highest-compensated employees. However, if no ATEO pays at least 10 percent of an employee’s total remuneration during a calendar year, this exception does not apply to the ATEO that paid the most remuneration to the employee during the calendar year.

Whether an employee is one of the five highest-compensated employees is determined separately for each ATEO, and not for the entire group of related organizations; thus, each ATEO has its five highest-compensated employees. As a result, in many cases, a group of related organizations will have more than five covered employees. Some commenters suggested that a group of related ATEOs should have only five highest-compensated employees among all of the related ATEOs, noting that this is the case for purposes of section 162(m)(1)-(4), as Treas. Reg. § 1.162-27(c)(1)(ii) treats a publicly held corporation and all nonpublic corporations related to the publicly held corporation as a single corporation. Section 4960 does not provide for such
treatment. Further, under Treas. Reg. § 1.162-27(c)(1)(ii), each related subsidiary within an affiliated group of corporations that is itself a publicly held corporation is separately subject to the deduction limitation, just as each ATEO within a group of related organizations is separately subject to section 4960. Accordingly, this notice does not adopt the commenter’s suggestion, and the Treasury Department and the IRS have concluded that the position that a group of related organizations with more than one ATEO has a single set of five highest-compensated employees is not consistent with a good faith, reasonable interpretation of section 4960.

D. Excess Remuneration

In general, the excise tax imposed under section 4960(a)(1) is based on the remuneration paid (other than any excess parachute payment) by an ATEO for the taxable year with respect to employment of any covered employee in excess of $1 million. Q/A–11 provides that this amount is referred to as “excess remuneration.” Consistent with the statute, the $1 million threshold is not adjusted for inflation.

Section 4960(c)(3)(A) generally defines “remuneration” as wages under section 3401(a) (wages subject to federal income tax withholding), but excluding designated Roth contributions under section 402A(c) and including amounts required to be included in gross income under section 457(f). Q/A–12 clarifies that remuneration includes a parachute payment that is not an excess parachute payment, but remuneration does not include certain retirement benefits (see section 3401(a)(12)) or certain directors’ fees (see Rev. Rul. 57-246, 1957-1 C.B. 338).

The flush language at the end of section 4960(a) provides that, for purposes of section 4960(a), remuneration is treated as paid when there is no substantial risk of
forfeiture of the rights to the remuneration. The term “substantial risk of forfeiture” is defined by cross-reference to section 457(f)(3)(B). Proposed regulations under section 457(f) were published in 2016 (81 FR 40548 (Jun. 22, 2016)). The preamble to the proposed regulations states that taxpayers may rely on them before they are finalized. Q/A–13 provides that the definition of substantial risk of forfeiture under Prop. Treas. Reg. § 1.457-12(e)(1) is the definition of substantial risk of forfeiture within the meaning of section 457(f)(3)(B) for purposes of section 4960(a). Under Prop. Treas. Reg. § 1.457-12(e)(1), an amount of compensation is subject to a substantial risk of forfeiture only if entitlement to the amount is conditioned on the future performance of substantial services, or upon the occurrence of a condition that is related to a purpose of the compensation if the possibility of forfeiture is substantial. Consistent with common usage, Q/A–13 refers to an amount the right to which is not subject to a substantial risk of forfeiture as being “vested” and the lapsing of a substantial risk of forfeiture as “vesting.”

Q/A–13 clarifies that although section 4960(a) cross-references the definition of substantial risk of forfeiture in section 457(f)(3)(B), the rule under section 4960(a) providing that remuneration is treated as paid upon vesting is not limited to remuneration that is otherwise subject to section 457(f), nor is it limited to nonqualified deferred compensation under section 457(f) or section 409A. Rather, this timing rule for determining when remuneration is treated as paid applies to all forms of remuneration.

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3 Any changes to the proposed regulations under section 457(f) when finalized will be taken into account for purposes of section 4960, and further guidance may be issued if appropriate.
Some commenters argued that section 4960(c)(3), which defines remuneration largely by cross-reference to the definition of wages under section 3401(a), should be interpreted as a timing rule. Section 3401(a) primarily focuses on whether, not when, amounts are includible in wages; the basic timing rule for wage inclusion appears in regulations under section 3402(a), not section 3401(a). Specifically, Treas. Reg. § 31.3402(a)-1(b) provides that wages are paid when actually or constructively paid and explains what it means for an amount to be constructively paid. Thus, the Treasury Department and the IRS conclude that the cross-reference to section 3401(a) (and not section 3402(a)) in section 4960(c)(3) establishes the scope of the term “remuneration” without regard to timing, and that the flush language in section 4960(a) establishes the timing rule that applies to all forms of remuneration. Accordingly, Q/A–13 provides that, for purposes of determining when remuneration is treated as paid, the timing rule in section 4960(a) applies and the timing rule for wage inclusion under Treas. Reg. § 31.3402(a)-1(b) is not relevant.

Under Q/A–13, the amount of remuneration treated as paid at vesting is the present value of the remuneration in which the covered employee vests. The employer must determine the present value using reasonable actuarial assumptions regarding the time and likelihood of actual or constructive payment. The employer may use the rules set forth in Prop. Treas. Reg. § 1.457-12(c)(1) to determine the present value. In addition, for purposes of determining the present value of remuneration that is scheduled to be paid within 90 days of vesting, the employer may elect to treat the amount that is to be paid as the present value of the amount on the date of vesting.
Until actually or constructively paid, the amount treated as paid at vesting is referred to as “previously paid remuneration.”

Q/A–13 provides specific rules for timing of inclusion for earnings and losses on previously paid remuneration. Net earnings on previously paid remuneration are treated as paid at the close of the calendar year in which they accrue. For example, the present value of vested remuneration credited to an employee’s account under an account balance plan described in Treas. Reg. § 1.409A-1(c)(2)(i)(A) (under which the earnings and losses attributed to the account are based solely on a predetermined actual investment or a reasonable market interest rate) is treated as paid on the date credited to the employee’s account and, until subsequently actually or constructively paid, is treated as previously paid remuneration. However, at the close of each calendar year in which there is previously paid remuneration allocable to a covered employee, the present value of any net earnings accrued on that previously paid remuneration (the increase in present value due to the predetermined actual investment or a reasonable market interest rate) is treated as remuneration paid (and subsequently is treated as previously paid remuneration until actually or constructively paid). Similarly, the present value of a vested, fixed amount of remuneration under a nonaccount balance plan described in Treas. Reg. § 1.409A-1(c)(2)(i)(C) is treated as paid on the date of vesting and subsequently as previously paid remuneration until actually or constructively paid. But, at the close of each calendar year in which there is previously paid remuneration allocable to a covered employee, the net increase in the present value of that amount during the year constitutes earnings and is treated as remuneration paid (and subsequently is also treated as previously paid remuneration...
until actually or constructively paid). For this purpose, earnings and losses from one arrangement may be aggregated with earnings and losses from any other arrangement provided by the same employer in which the employee participates, resulting in a single amount of remuneration and one amount, if any, of carryover losses (but no carryover gains, since any net gain would be treated as remuneration for the taxable year). For purposes of determining earnings and losses, previously paid remuneration is reduced by the amount actually or constructively paid under the plan or arrangement granting the rights to such remuneration. Q/A–13 further illustrates the operation of these rules through examples.

One commenter requested a “grandfather” rule like the transition rule under section 13601 of the Act that amended section 162(m). Because section 13602 of the Act, which added section 4960 to the Code, does not provide a transition rule (in contrast to section 13601 of the Act), and there is no indication in the legislative history that Congress intended there to be a transition rule for section 4960, the Treasury Department and the IRS have concluded that it is inappropriate to provide an effective date exception similar to the one provided for purposes of section 13601 of the Act. However, Q/A–13 clarifies and demonstrates the grandfathering effect of the remuneration payment timing rule. Specifically, Q/A–13 clarifies that any vested remuneration, including vested but unpaid earnings on deferred amounts, that is treated as paid before section 4960 is applicable (January 1, 2018, in the case of a calendar year employer) is not subject to the excise tax imposed under section 4960(a)(1), although earnings after the effective date on those amounts are treated as remuneration paid for purposes of section 4960(a)(1). Similarly, Q/A–13 clarifies that vested amounts
that would have been treated as remuneration paid (including vested but unpaid earnings) before the year in which an employee first becomes a covered employee are not remuneration for the first year the employee becomes a covered employee or any subsequent year and, therefore, are not subject to the excise tax imposed under section 4960(a)(1). However, subsequent earnings on that vested remuneration may be subject to excise tax under section 4960(a)(1).

To reduce administrative burdens, some commenters recommended that remuneration be determined solely by reference to the amount reportable in Form W-2, box 1. For the following reasons, the Treasury Department and the IRS have concluded it is inappropriate to adopt that recommendation. In defining remuneration, section 4960(c)(3) explicitly cross-references and modifies the definition of wages under section 3401(a). Although the amount reportable in Form W-2, box 1 includes wages as defined under section 3401(a), it may also include amounts that are includible in the employee’s gross income but are not wages under section 3401(a). In addition, as explained previously, the timing rule for when remuneration is paid under section 4960(a) differs from the timing rule for when wages are paid under section 3401(a). Therefore, the amount reported in Form W-2, box 1 in many cases will not be the same as the employee’s remuneration for purposes of section 4960.

As an alternative to using the amount reported in Form W-2, box 1, some commenters recommended that remuneration be defined solely by reference to the amount reportable in Form W-2, box 5, which reports the amount of wages (as defined in section 3121(a)) subject to the Hospital Insurance tax under sections 3101(b) and 3111(b). However, there are differences between the definitions of wages under
sections 3401(a) and 3121(a), and there is no indication in the statute or legislative history that Congress intended that the definition of wages in section 3121(a) be used to determine remuneration under section 4960(a). In addition, the payment timing differences discussed previously apply so that the amounts reported in Form W-2, box 5 may not accurately reflect the remuneration paid for the applicable period for purposes of section 4960. For these reasons, the Treasury Department and the IRS have concluded it is not appropriate to adopt this recommendation.

An individual may perform services as a common-law employee for two different related organizations during the calendar year, one or both of which is an ATEO, in which case remuneration paid for the taxable year is aggregated for purposes of determining whether excess remuneration has been paid. To address these cases, Q/A–14 provides rules for allocating liability for the excise tax among the employers. As provided in section 4960(c)(4)(C), in any case in which an ATEO includes remuneration from one or more related organizations as separate employers of the individual in determining the excise tax imposed by section 4960(a), each employer is liable for its proportionate share of the excise tax.

The guidance in this notice provides specific instructions for calculating the excise tax on excess remuneration under section 4960(a)(1), including rules for allocating the excise tax among related employers and rules regarding a change in related status during the calendar year. As described further in Q/A–14, an employee may be a covered employee of more than one ATEO and each ATEO employer calculates its liability under section 4960(a)(1) taking into account the organizations to which it is related. In that case, Q/A–14 provides that, rather than owing tax as both an
ATEO and a related organization for the same remuneration paid to a covered employee, an employer is liable only for the greater of the excise tax it would owe as an ATEO or the excise tax it would owe as a related organization with respect to that covered employee.

E. Medical and Veterinary Services

Section 4960(c)(3)(B) and (c)(5)(C)(iii) exclude from remuneration and parachute payments, respectively, the portion of any compensation that is for the performance of medical or veterinary services by a licensed medical professional (including a veterinarian). The Conference Report states that “[f]or purposes of determining a covered employee, remuneration paid to a licensed medical professional which is directly related to the performance of medical or veterinary services by such professional is not taken into account, whereas remuneration paid to such a professional in any other capacity is taken into account.” Conf. Rep. at 494 (emphasis added).

Sections 4960(c)(3)(B) and (c)(5)(C)(iii) both use the phrase “medical or veterinary services.” Consistent with the legislative history quoted previously, Q/A–15 provides that remuneration for the direct performance of medical or veterinary services is excluded for purposes of section 4960. Commenters requested guidance as to the meaning of “licensed medical professional,” which is not defined in the statute. The Conference Report states that “[a] medical professional for this purpose includes a doctor, nurse, or veterinarian.” Conf. Rep. at 494. Q/A–15 provides that a licensed medical professional is an individual who is licensed under state or local law to perform medical or veterinary services. In addition to those professionals listed, this generally
includes dentists and nurse practitioners and may include other medical professionals depending on state or local law.

Commenters also requested guidance on the definition of medical services for purposes of section 4960. Q/A–15 adopts the definition of medical care under section 213(d) for purposes of determining whether services are medical services. This standard is consistent with the legislative intent that the exception apply only to remuneration for the direct performance of medical services and is a familiar standard for taxpayers. Section 213(d) provides that medical care consists of services for the diagnosis, cure, mitigation, treatment, or prevention of disease, including services for the purpose of affecting any structure or function of the body. For a veterinarian or other licensed veterinary professional, section 213(d)(1)(A) applies by analogy to determine whether the activity constitutes veterinary services.

In addition, commenters requested guidance on whether activities related to medical services, such as administrative, teaching, and research services, are medical services. Q/A–15 provides that these activities generally are not medical services. However, to the extent a licensed medical professional provides direct medical care to a patient in the course of these activities, he or she performs medical services, and remuneration allocable to those services is not taken into account for purposes of section 4960.

When a covered employee is compensated for both medical services and other services, the employer must allocate remuneration paid to such employee between medical services and such other services. Q/A–15 permits taxpayers to use any reasonable, good faith method to allocate remuneration between medical services and
other services. For this purpose, taxpayers may rely on a reasonable allocation set forth in an employment agreement that explicitly allocates a portion of the remuneration as for medical services or other services. If some or all of the remuneration is not reasonably allocated in an employment agreement, taxpayers must use a reasonable method of allocation. As an example of a reasonable method, a taxpayer may use records such as patient, insurance, and Medicare/Medicaid billing records or internal time reporting mechanisms to determine the time spent providing medical services, and then allocate remuneration to medical services in the proportion such time bears to the total hours the covered employee worked for the employer. The same rules apply with respect to veterinary services.

F. **Excess Parachute Payments**

Section 4960(a)(2) imposes an excise tax on “any excess parachute payment.” Section 4960(c)(5)(A) provides that the term “excess parachute payment” means an amount equal to the excess of any parachute payment over the portion of the base amount allocated to such payment. Section 4960(c)(5)(B) provides that the term “parachute payment” means any payment in the nature of compensation to (or for the benefit of) a covered employee if (i) such payment is contingent on such employee’s separation from employment with the employer, and (ii) the aggregate present value of the payments in the nature of compensation to (or for the benefit of) such individual which are contingent on such separation equals or exceeds an amount equal to three times the base amount. Section 4960(c)(5)(C) provides exceptions for certain
retirement plans, certain payments to licensed medical professionals, and payments to individuals who are not highly compensated employees as defined in section 414(q).

The excess parachute payment rules under section 4960 are modeled after section 280G. Section 280G disallows a deduction for any excess parachute payment. Although sections 280G and 4960 both use the term “parachute payment,” they define it differently. Whereas the section 4960 definition refers to payments contingent on an employee’s separation from employment, the section 280G definition refers to payments contingent on a change in the ownership or effective control of a corporation (or in the ownership of a substantial portion of the assets of the corporation). There are also other differences between sections 280G and 4960. For example, section 280G does not include exceptions for payments to licensed medical professionals or non-highly compensated employees. The guidance in this notice incorporates many of the questions and answers (Q/As) under Treas. Reg. § 1.280G-1, with modifications to reflect the statutory differences between sections 280G and 4960. However, certain Q/As under Treas. Reg. § 1.280G-1 are not incorporated into this notice because they address issues that do not arise under section 4960. Conversely, certain Q/As in this notice do not have parallel Q/As under Treas. Reg. § 1.280G-1 because they address issues that arise under section 4960 but not under section 280G.

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4 Under section 414(q), a highly compensated employee generally is defined as any employee who was a five-percent owner at any time during the year or the preceding year or who had compensation from the employer in the preceding year in excess of an inflation-adjusted amount. Notice 2017-64, 2017-45 I.R.B. 486, and Notice 2018-83, provide that the inflation-adjusted amounts for 2018 and 2019 are $120,000 and $125,000, respectively. See section 414(q) and the regulations thereunder for additional details, including the availability of an election to treat no more than the top 20 percent of an employer’s employees as highly compensated employees by reason of their compensation.
The discussion of Q/A–16 through Q/A–34 that follows provides an overview of the guidance in this notice for purposes of calculating the excise tax under section 4960(a)(2), noting certain similarities and differences between those Q/As and the Q/As under Treas. Reg. § 1.280G-1. As a preliminary matter, however, the following summarizes the basic steps used to determine the amount of excise tax (if any) under section 4960(a)(2):

Step 1: Determine if a covered employee is entitled to receive payments in the nature of compensation that are contingent on an involuntary separation from employment and are not subject to an exclusion.

Step 2: Calculate the total aggregate present value of the contingent payments, taking into account the special valuation rules that apply when an involuntary separation from employment accelerates payment or vesting of a right to a payment.

Step 3: Calculate the covered employee’s base amount with respect to the base period.

Step 4: Determine if the contingent payments are parachute payments. The contingent payments are parachute payments if their total aggregate present value equals or exceeds an amount equal to three times the covered employee’s base amount.

Step 5: Calculate the amount of excess parachute payments. A parachute payment is an excess parachute payment to the extent the payment exceeds the base amount allocated to the payment. (Note that this is the excess over 1 times the base amount, and not the excess over 3 times the base amount.)
Step 6: Calculate the amount of excise tax under section 4960(a)(2). The excise tax is the amount equal to the product of the rate of tax under section 11 and the sum of any excess parachute payments paid by an ATEO or related organization to the covered employee.

Q/A–16 defines the term “excess parachute payment,” and Q/A–17 defines the term “parachute payment.” Q/A–18, which defines a “payment in the nature of compensation,” is based on Treas. Reg. § 1.280G-1, Q/A–11. Q/A–19, which describes when a payment is considered made for purposes of section 4960(a)(2), including the treatment of section 83 property, stock options, and stock appreciation rights and the treatment of consideration paid by an employee, is based on Treas. Reg. § 1.280G-1, Q/A–12 through Q/A–14.

Q/A–20 describes when a payment is contingent on an employee’s separation from employment. Commenters requested that the Treasury Department and the IRS clarify what it means for a payment to be contingent on a separation from employment, noting that the statute does not provide a definition. One commenter suggested that the Treasury Department and the IRS issue guidance treating a payment as contingent on an employee’s separation from employment only if the payment is subject to a substantial risk of forfeiture (defined in a manner consistent with section 457(f) or section 409A) at the time of a separation from employment and the separation causes the risk of forfeiture to lapse. The guidance in this notice is generally consistent with that suggestion, with certain exceptions discussed in the next several paragraphs.

Separation from employment (whether voluntary or involuntary) is often used in compensation arrangements as the trigger to pay vested amounts. For example, it is
typical for a nonqualified deferred compensation plan to provide that payments will be
made or begin upon a separation from employment, including separation from
employment resulting from death or disability. In contrast, Treas. Reg. § 1.280G-1,
Q/A–22 generally treats a payment as contingent on a change in ownership or control if
the payment would not have been made had no change in ownership or control
occurred, taking into consideration whether vesting or payment is accelerated by reason
of the change in ownership or control. Similarly, in defining when a payment is
contingent on separation from employment, this notice does not focus solely on whether
the payment would not have been made but for a separation from employment, but
instead also takes into consideration whether the separation from employment results in
the employee becoming vested or otherwise accelerates the right to payment.

The guidance in this notice limits the payments treated as contingent on a
separation from employment to payments contingent on an involuntary separation from
employment because payments that vest upon a separation from employment typically
vest only upon an involuntary separation from employment. If an employee may
voluntarily separate from service and still be entitled to a payment, then the payment
either is not subject to a substantial risk of forfeiture or the forfeiture condition is not
related to the separation from employment. If, however, there are other types of
separation from employment conditions that may result in the lapse of a substantial risk
of forfeiture applicable to a payment, the standard in this notice may be expanded in
future guidance to ensure that those payments are also treated as contingent on a
separation from employment.
Specifically, Q/A–20 provides that a payment is contingent on a separation from employment if the payment would not have been made in the absence of an involuntary separation from employment. It further provides that if the right to a payment vests as a result of an involuntary separation from employment, the payment is treated as a payment that is contingent on a separation from employment. For example, a right to a severance payment provided in an employment agreement that vests upon an involuntary separation from employment is a payment contingent on a separation from employment.

However, not all payments that are made after an involuntary separation from employment are contingent on a separation from employment. For example, a payment of deferred compensation after an involuntary separation from employment that vested based on years of service completed before the involuntary separation from employment generally is not a payment that is contingent on a separation from employment because the payment would be paid at some point, and the separation from employment may impact the time of, but not the right to, the payment. Similarly, medical benefits that vested based on years of service completed before an involuntary separation from employment but that are provided after the involuntary separation from employment generally are not treated as payments that are contingent on a separation from employment.

Q/A–20 also provides that an amount that was included in gross income in a previous year and excess remuneration that was treated as paid under Q/A–13 before the separation from employment are not contingent on the separation from employment.
Therefore, while these amounts may be included in the employee’s base amount, payments of these amounts are not parachute payments.

Q/A–24 provides that if a payment is accelerated or a substantial risk of forfeiture lapses as a result of an involuntary separation from employment, the additional value due to the acceleration is treated as a payment contingent on a separation from employment. Q/A–24 is based on the rules of Treas. Reg. § 1.280G-1, Q/A–24(b) and (c) for purposes of determining the value of these accelerations.

Notwithstanding the foregoing, if the facts and circumstances demonstrate that either vesting or payment of an amount (whether before or after the involuntary separation from employment) would not have occurred but for the involuntary nature of the separation from employment, the amount will be treated as contingent on a separation from employment. For example, an employer’s exercise of discretion to accelerate vesting of an amount shortly before an involuntary separation from employment may indicate that the acceleration of vesting was due to the involuntary nature of the separation from employment and, thus, was contingent on the employee’s separation from employment. Similarly, payment of an amount in excess of an amount otherwise payable (for example, increased salary) shortly before or after an involuntary separation from employment may indicate that the amount was paid because the separation was involuntary and, thus, was contingent on the employee’s separation from employment.

Q/A–21 provides that payments pursuant to certain window programs are treated as payments contingent on a separation from employment and is based on Treas. Reg. § 1.409A-1(b)(9).
Q/A–23 generally adopts the standards of the regulations under section 409A for purposes of determining whether there has been a separation from employment, except that a bona fide change from employee to independent contractor status is treated as a separation from employment. However, the IRS may assert based on all the facts and circumstances that there was not a bona fide change from employee to independent contractor status. Specifically, Q/A–23 adopts the standards of Treas. Reg. § 1.409A-1(h)(1)(ii), providing that an anticipated reduction in the level of services of more than 80 percent is treated as a separation from employment and an anticipated reduction in the level of services of less than 50 percent is not treated as a separation from employment, with the treatment of an anticipated reduction between these two levels depending on the facts and circumstances. The guidance in this notice does not adopt the rule of Treas. Reg. § 1.409A-1(h)(1)(ii) under which an employer may modify the level of the anticipated reduction in future services that will be considered to result in a separation from employment. Instead, the default 80 percent and 50 percent levels provided under Treas. Reg. § 1.409A-1(h)(1)(ii) apply for purposes of section 4960.

Unlike Q/A–25 and Q/A–26 of Treas. Reg. § 1.280G-1, the guidance in this notice does not provide a presumption that a payment made pursuant to an agreement entered into or modified within twelve months of a separation from employment is a payment that is contingent on a separation from employment. However, as noted previously, if the facts and circumstances demonstrate that either the vesting or the payment of an amount would not have occurred but for the involuntary nature of the separation from employment, the amount will be treated as a payment contingent on a separation from employment.
In addition, the guidance in this notice does not incorporate Treas. Reg. § 1.280G-1, Q/A–9, excluding reasonable compensation for services from the definition of parachute payment. In many cases, whether payments after a separation from employment are reasonable compensation for services will not be an issue because the employee will not provide services after the separation from employment. However, if the employee continues to provide services (including as a bona fide independent contractor) after a separation from employment, payments for those services are not contingent on the involuntary separation from employment to the extent those payments are reasonable and are not made due to the involuntary nature of the separation from employment.

Finally, the guidance in this notice does not include a rule similar to Treas. Reg. § 1.280G-1, Q/A–16, under which a personal service corporation (PSC) is treated as an employee. Q/A–3 provides that section 4960 applies to amounts paid to common law employees who are covered employees of an ATEO. Although a PSC that performs services for an ATEO is not treated as an employee, the IRS may assert that the individual owner of a PSC is in fact a common law employee of an ATEO based on all the facts and circumstances.

G. Three-Times-Base-Amount Test for Parachute Payments

Section 4960(c)(5)(B) provides that a payment is a parachute payment only if the aggregate present value of the payments in the nature of compensation to (or for the benefit of) an individual that are contingent on a separation from employment equals or exceeds an amount equal to three times the base amount.
Section 4960(c)(5)(D) provides that rules similar to the rules of section 280G(b)(3) apply for purposes of determining the base amount, and section 4960(c)(5)(E) provides that rules similar to the rules of paragraphs (3) and (4) of section 280G(d) apply for purposes of present value determinations.

Section 280G(b)(3) provides that the term “base amount” means an individual’s annualized includible compensation for a base period. Section 280G(d)(2) defines “base period” as the period consisting of the five most recent taxable years of the service provider ending before the date on which the change in ownership or control occurs or the portion of such period during which the individual performed personal services for the corporation. Section 280G(d)(3) provides that any transfer of property is treated as a payment and is taken into account at its fair market value. Section 280G(d)(4) provides that present value is determined using a discount rate equal to 120 percent of the applicable Federal rate determined under section 1274(d), compounded semiannually.

Q/A–25 through Q/A–31 are based on the rules under Treas. Reg. § 1.280G-1, Q/A–30 through Q/A–35 (substituting an involuntary separation from employment for a change in control) for determining whether a payment is an excess parachute payment, including the rules for applying the three-times-base-amount test, determining the base amount and base period, and determining present value, including determining the present value of payments that are contingent on uncertain future events.

**H. Computation of Excess Parachute Payments**

Section 4960(c)(5)(A) provides that an “excess parachute payment” is an amount equal to the excess of any parachute payment over the portion of the base amount
allocated to such payment. Q/A–32(a) is based on Treas. Reg. § 1.280G-1, Q/A–38, regarding allocating the base amount to a parachute payment (that is, determining the portion that is not a parachute payment because it does not exceed the base amount). Q/A-2 provides that the excise tax on excess parachute payments for a taxable year is based on any excess parachute payments made in the calendar year ending with or within the taxable year of the ATEO.

I. Reporting Liability Under Section 4960

As requested by some commenters, Q/A-34 provides guidance as to the reporting and due date for paying the section 4960 excise tax. On November 7, 2018, the Treasury Department and the IRS issued proposed regulations under sections 6011 and 6071 (Prop. Treas. Reg. §§ 53.6011-1 and 53.6071-1, 83 F.R. 55653) to address reporting and the due date for paying the tax. The proposed regulations provide that the excise tax under section 4960 is reported on Form 4720, Return of Certain Excise Taxes Under Chapters 41 and 42 of the Internal Revenue Code, which is the form generally used for reporting and paying chapter 42 taxes. Each employer liable for section 4960 tax, whether an ATEO or a related organization described in section 4960(c)(4)(B), is responsible for separately reporting and paying its share of the tax. The proposed regulations provide that Form 4720 and payment are due when chapter 42 taxes ordinarily are due (the 15th day of the 5th month after the end of the taxpayer’s taxable year—May 15 for a calendar year employer), subject to an extension of time for filing that generally applies. This rule is also reflected in Q/A–34(a).

Q/A–34(b) provides that an employer may elect to prepay the excise tax imposed under section 4960(a)(2) in the year of separation from employment (or any taxable
year prior to the year in which the parachute payment is actually paid). This rule is similar to the rule in Treas. Reg. § 1.280G-1, Q/A–11(c), under which a disqualified employee may elect to prepay the excise tax under section 4999 based on the present value of the excise tax that would be owed by the employee when the parachute payments are actually made.

Some commenters requested clarification as to whether section 4960 excise tax is subject to quarterly payments of estimated tax under section 6655. Since section 6655 was not amended to include section 4960, no quarterly payments of estimated section 4960 tax are required under section 6655. See Q/A–35.

J. Miscellaneous Issues

Q/A–36 through Q/A–38 address coordination of section 4960 with other Code provisions. Commenters requested clarification of the relationship between the section 4960 excise tax and excise taxes for unreasonable or excessive compensation under section 4958 or, in the case of compensation to disqualified persons for personal services, section 4941. Q/A–36 and Q/A–37 confirm that there is no particular relationship between liability for excise tax under section 4960 and liability under these other provisions. In cases involving excessive compensation for purposes of section 4958 or section 4941, there may or may not be concurrent excise tax liability under section 4960, and in cases involving section 4960 excise tax liability, there may or may not be concurrent liability under section 4958 or section 4941.

Q/A–38 addresses the rule under section 4960(c)(6) that remuneration for which a deduction is disallowed under section 162(m) is not taken into account under section 4960. For example, an ATEO’s covered employee may also be a covered
employee of a publicly held corporation (as those terms are defined in section 162(m)(2) and (3)) if the publicly held corporation is related to the ATEO under section 4960(c)(4)(B). In that case, any portion of remuneration disallowed as a deduction by reason of section 162(m) is not taken into account under section 4960.

K. Effective Date

Section 4960 is effective for the first taxable year beginning after December 31, 2017. Q/A–39 provides that amounts paid before the beginning of that taxable year are not subject to the excise tax under section 4960. As described previously in the discussion of remuneration for purposes of section 4960(a)(1), remuneration that was vested before the effective date of section 4960 is not subject to excise tax under section 4960 because it is treated as having been paid at vesting. For example, amounts includible in gross income under section 457(f)(1)(A) and any vested earnings that accrued before the effective date of section 4960 are not subject to the excise tax under section 4960. However, earnings accrued on those amounts in taxable years beginning after December 31, 2017, may be subject to excise tax under section 4960(a)(1).

II. INTERIM GUIDANCE ON APPLICATION OF SECTION 4960

A. Section 4960 — In General

Q–1: What is the effect of section 4960?

A–1: An ATEO or related organization that pays excess remuneration or an excess parachute payment to a covered employee is subject to an excise tax on that amount at a rate equal to the rate of tax under section 11. For taxable years beginning after
December 31, 2017, the rate of tax under section 11 is 21 percent. See section 13001 of the Act.

**Q–2: What year is used in calculating the section 4960 excise tax?**

A–2: Excess remuneration paid and excess parachute payments made in the calendar year ending with or within the taxable year of an ATEO or a related organization, whichever is the applicable employer, are treated as paid for that taxable year. Thus, the excise tax on excess remuneration and excess parachute payments is calculated based on excess remuneration paid and excess parachute payments made during the calendar year ending with or within the employer’s taxable year.

**Q–3: Who is liable for the section 4960 excise tax?**

A–3: (a) **In general.** The common-law employer, as generally determined for federal tax purposes, is liable for the excise tax imposed under section 4960. Only an ATEO has covered employees, but a covered employee may also be an employee of a related organization. When an employer that is an ATEO or a related organization pays a covered employee either excess remuneration or an excess parachute payment, each employer is liable for the excise tax under section 4960. See Q/A–14 for rules that apply when more than one employer is liable for the excise tax on excess remuneration.

Whether a person or entity is the common-law employer generally depends on the facts and circumstances. A common-law employer may not avoid liability under section 4960 by reason of a third party payor arrangement, such as an arrangement with a payroll agent, common paymaster, statutory employer under section 3401(d)(1), or certified professional employer organization, or any similar arrangement. For purposes of section 4960, a payment to an employee by a third-party payor is
considered paid by the common-law employer with respect to the services for which the payment is made. Similarly, a payment to an employee on behalf of the common-law employer (such as a payment from a related organization for which the individual is not providing services as an employee or a payment from an unrelated management company), is considered paid by the common-law employer for purposes of section 4960.

(b) Disregarded entities. In the case of employment by a disregarded entity described in Treas. Reg. § 301.7701-3, the sole owner of the disregarded entity is treated as the common-law employer for purposes of section 4960.

(c) Arrangements between an ATEO and a related organization. Calculation of, and liability for, the excise tax based on excess remuneration or an excess parachute payment in accordance with this Q/A–3 is separate from and unaffected by any arrangement that the ATEO and any related organization may have for bearing the cost of any excise tax liability under section 4960.

B. Applicable Tax-Exempt Organizations and Related Organizations

Q–4: What is an applicable tax-exempt organization within the meaning of section 4960(c)(1)?

A–4: As provided in section 4960(c)(1), an ATEO is any organization which for its taxable year–

(A) is exempt from taxation under section 501(a),

(B) is a farmers' cooperative organization described in section 521(b)(1),

(C) has income excluded from taxation under section 115(1), or

(D) is a political organization described in section 527(e)(1).
Q–5: When is a governmental entity an applicable tax-exempt organization within the meaning of section 4960(c)(1)?

A–5: Governmental entities specifically described in section 4960(c)(1), that is, organizations that have income excluded from taxation under section 115(1) and organizations that are exempt from taxation under section 501(a), are ATEOs. For example, federal instrumentalities exempt from tax under section 501(c)(1) and public universities with IRS determination letters recognizing their tax-exempt status under section 501(c)(3) are governmental entities exempt from tax under section 501(a), and thus are ATEOs.

A governmental entity that is separately organized from a state or political subdivision of a state may meet the requirements to exclude income from gross income (and thereby have income excluded from taxation) under section 115(1). See Rev. Rul. 77-261, 1977-2 C.B.45. However, a state, political subdivision of a state, or integral part of a state or political subdivision, often referred to as a “governmental unit,” does not meet the requirements to exclude income from gross income under section 115(1) because section 115(1) does not apply to income from an activity that the state conducts directly, rather than through a separate entity. See Rev. Rul. 77-261; see also Rev. Rul. 71-131, 1971-1 C.B. 28 (superseding and restating the position stated in G.C.M. 14407, C.B. XIV-1 103).

Instead, under the doctrine of implied statutory immunity, the income of a governmental unit generally is not taxable in the absence of specific statutory authorization for taxing that income. See Rev. Rul. 87-2, 1987-1 C.B. 18; Rev. Rul. 71-131; Rev. Rul. 71-132, 1971-1 C.B. 29; and G.C.M. 14407. Section 511(a)(2)(B), which imposes tax on the unrelated business taxable income of state colleges and
universities, is an example of a specific statutory authorization for taxing income earned by a state, a political subdivision of a state, or an integral part of a state or political subdivision of a state.

Thus, a governmental unit (including a state college or university) that does not have a determination letter recognizing its exemption from taxation under section 501(a) and does not exclude income from gross income under section 115(1) is not an ATEO described in section 4960(c)(1). However, such a governmental unit may be liable for excise tax under section 4960 if it is a related organization under section 4960(c)(4)(B) with respect to an ATEO.

Q–6: May a governmental entity with a determination letter recognizing its tax exemption relinquish its section 501(c)(3) status?
A–6: Yes, a governmental entity may voluntarily relinquish its section 501(c)(3) tax-exempt status pursuant to section 3.01(12) of Rev. Proc. 2018-5, 2018-1 I.R.B. 233, 239 (or the analogous section in any successor revenue procedure), under the procedures described in that revenue procedure.

Q–7: What is a related organization for purposes of section 4960?
A–7: As provided in section 4960(c)(4)(B), a person or governmental entity is related to an ATEO if such person or governmental entity—

(i) controls, or is controlled by, the ATEO;

(ii) is controlled by one or more persons which control the ATEO;

(iii) is a supported organization (as defined in section 509(f)(3)) with respect to the ATEO;

(iv) is a supporting organization described in section 509(a)(3) with respect to the ATEO; or
(v) in the case of an ATEO which is a voluntary employees’ beneficiary association described in section 501(c)(9), establishes, maintains, or makes contributions to such voluntary employees’ beneficiary association.

See Q/A–14(c) for rules regarding a change in related status during the year.

Q–8: What is the meaning of “control” for purposes of section 4960(c)(4)(B)(i)-(ii) and Q/A–7 of this notice?

A–8: (a) In general. For purposes of section 4960(c)(4)(B)(i)-(ii) and Q/A–7 of this notice, the term “control” is defined as follows:

1. **Stock corporation.** In the case of a stock corporation, control means ownership (by vote or value) of more than 50 percent of the stock in such corporation.

2. **Partnership.** In the case of a partnership, control means ownership of more than 50 percent of the profits interest or capital interest in such partnership.

3. **Trust.** In the case of a trust with beneficial interests, control means ownership of more than 50 percent of the beneficial interests in the trust.

4. **Nonstock organization.** In the case of a nonprofit organization or other organization without owners or persons having beneficial interests (nonstock organization), including a governmental entity, control means that (i) more than 50 percent of the directors or trustees of the ATEO or nonstock organization are either representatives of, or are directly or indirectly controlled by, the other entity; or (ii) more than 50 percent of the directors or trustees of the nonstock organization are either representatives of, or are directly or indirectly controlled by, one or more persons that control the ATEO. For purposes of this paragraph, a “representative” means a trustee, director, agent, or employee, and control includes the power to remove a trustee or director and designate a new trustee or director.
(5) **Constructive ownership.** For purposes of Q/A-7 and this Q/A-8, section 318 (relating to constructive ownership of stock) applies for purposes of determining control of stock in a corporation. For purposes of determining control of any other entity, including a nonstock organization, under this Q/A–8, the principles of section 318 apply.

(b) **Examples.** The following examples illustrate how the rules of Q/A-7 and this Q/A–8 apply:

**Example 1.** A, B, and C are nonstock organizations and are ATEOs within the meaning of section 4960(c)(1). C owns 80 percent of the stock of corporation D. Eighty percent of B’s directors are representatives of A. In addition, 80 percent of C’s directors are representatives of A. A is a related organization with respect to B (and vice versa) because more than 50 percent of B’s directors are representatives of A; thus, A controls B. Based on the same analysis, A is also a related organization with respect to C (and vice versa). D is a related organization with respect to C because, as the owner of more than 50 percent of D’s stock, C controls D. Applying the principles of section 318, A is deemed to own 64 percent of the stock of D (80 percent of C’s stock in D). Thus, D is a related organization with respect to A because A controls D. B is a related organization with respect to C, C is a related organization with respect to B, and D is a related organization with respect to B because B, C, and D are all controlled by the same person (A).

**Example 2.** X, Y, and Z are nonstock organizations and are ATEOs within the meaning of section 4960(c)(1). Sixty percent of Y’s directors are representatives of X. In addition, 60 percent of Z’s directors are representatives of Y. X is a related organization with respect to Y (and vice versa) because more than 50 percent of Y’s directors are representatives of X; thus, X controls Y. Based on the same analysis, Z is a related organization with respect to Y (and vice versa). Applying the principles of section 318, X is deemed to control 36 percent of Z’s directors (60 percent of Y’s 60 percent control over Z). Because less than 50 percent of Z’s directors are representatives of or controlled by X, and absent any facts suggesting that X directly or indirectly controls Z, X is not a related organization with respect to Z.

**C. Covered Employees**

**Q–9: Who is a covered employee within the meaning of section 4960(c)(2)?**

**A–9:** The term “covered employee” means any employee (including any former employee) of an ATEO, if the employee—
(A) is one of the five highest-compensated employees of the organization for the taxable year of the ATEO, or

(B) was a covered employee of the ATEO (or any predecessor) for any of the ATEO’s preceding taxable years beginning after December 31, 2016.

Q–10: How are the five highest-compensated employees determined?

A–10: (a) In general. Except as provided in Q/A–10(b), the determination of whether an employee is one of the five highest-compensated employees of an ATEO is made on the basis of his or her remuneration for services performed as an employee of the ATEO, including remuneration for services performed as an employee of a related organization with respect to the ATEO. The remuneration used for purposes of identifying the five highest-compensated employees is the remuneration paid to an employee during the calendar year ending with or within the ATEO’s or related organization’s taxable year. Remuneration paid for medical services (or veterinary services) is not taken into account for purposes of identifying the five highest-compensated employees.

(b) Limited services exception. An employee is not one of an ATEO’s five highest-compensated employees for a taxable year if, during the calendar year ending with or within the taxable year, as described in Q/A–2, the ATEO paid less than 10 percent of the employee’s total remuneration for services performed as an employee of the ATEO and all related organizations. However, if an employee would not be treated as one of the five highest-compensated employees of any ATEO in an ATEO’s group of related organizations because no ATEO in the group paid at least 10 percent of the total...
remuneration paid by the group during the calendar year, then this exception does not
apply to the ATEO that paid the employee the most remuneration during that year.

(c) Examples. The following examples illustrate the rules of this Q/A–10:

Example 1. X and Y are both calendar year taxpayers and ATEOs that are related
organizations with respect to each other, and both employ E during calendar year 2020.
Of the total remuneration paid to E for services performed as an employee of X and Y,
50 percent was for services for X and 50 percent was for services for Y. Based on the
aggregate remuneration from X and Y, E is one of the five highest-compensated
employees of both X and Y. E is a covered employee of both X and Y for 2020 and all
future taxable years.

Example 2. Assume the same facts as Example 1, except that of the total
remuneration paid to E for services performed as an employee of X and Y, 95 percent
was for services for X and 5 percent was for services for Y. E is a covered employee of
X for 2020 and all future taxable years, but is not a covered employee of Y for 2020
because Y did not pay at least 10 percent of the total remuneration paid to E by Y and
all related organizations and at least one other related ATEO paid at least 10 percent of
that remuneration.

D. Excess Remuneration

Q–11: What is excess remuneration paid by an applicable tax-exempt
organization under section 4960(a)(1)?

A–11: For each covered employee, excess remuneration is the excess (if any) for a
taxable year of the remuneration that is paid (other than any excess parachute
payment) by an ATEO, including remuneration paid by a related organization, over $1
million for the taxable year.

Q–12: What is remuneration under section 4960(c)(3)?

A–12: (a) General rule. The term “remuneration” has the same meaning as the term
“wages,” as defined in section 3401(a), except that it excludes any designated Roth
contribution (as defined in section 402A(c)) and includes amounts required to be
included in gross income under section 457(f). Remuneration includes an amount that
is a parachute payment; however, a parachute payment is not subject to tax as excess
remuneration if it is also subject to tax as an excess parachute payment. Further, remuneration does not include the portion of any remuneration paid to a licensed medical professional (including a veterinarian) that is directly related to the performance of medical or veterinary services by such professional.

(b) **Section 3401(a) wages.** Section 3401(a) provides that the term “wages” generally means all remuneration for services performed by an employee for his employer (with certain exceptions provided under section 3401(a)(1) through (a)(23)), including the cash value of all remuneration (including benefits) paid in any medium other than cash. Among the more broadly applicable exclusions, section 3401(a)(12) provides that wages do not include remuneration paid to, or on behalf of, an employee or his beneficiary—

(1) from or to a trust described in section 401(a) which is exempt from tax under section 501(a) at the time of such payment unless such payment is made to an employee of the trust as remuneration for services rendered as such employee and not as a beneficiary of the trust;

(2) under or to an annuity plan which, at the time of such payment, is a plan described in section 403(a);

(3) for a payment described in section 402(h)(1) and (2) if, at the time of such payment, it is reasonable to believe that the employee will be entitled to an exclusion under such section for payment;

(4) under an arrangement to which section 408(p) applies; or
(5) under or to an eligible deferred compensation plan which, at the time of such payment, is a plan described in section 457(b) that is maintained by an eligible employer described in section 457(e)(1)(A) (governmental employer).

(c) Remuneration paid by related organizations. Remuneration includes remuneration paid to a covered employee by any related organization with respect to the employee’s employment by that related organization. (See Q/A–14(b) for rules on allocating the liability for the excise tax when remuneration from more than one employer is taken into account in determining the liability for the excise tax under section 4960(a)(1).) In contrast, remuneration paid by another organization, whether or not a related organization, with respect to an employee’s employment by an ATEO, is treated as remuneration paid by that ATEO for purposes of section 4960.

(d) Directors. Compensation paid by an organization to a member of its board of directors (or an individual holding a substantially similar position) for serving in that capacity is not remuneration because the fees received by the director for performing those services constitute self-employment income, rather than wages under section 3401(a). See Rev. Rul. 57-246, 1957-1 C.B. 338. If the individual also performs services for the organization as an employee, then the compensation paid for the services as an employee is remuneration. Moreover, for purposes of section 4960, compensation that an employer pays to an employee to serve as a director of another organization is remuneration.

Q–13: When is remuneration treated as paid for purposes of section 4960(a)(1)?
A–13: (a) General rule. For purposes of section 4960(a)(1), remuneration is paid for a taxable year if it is paid during the calendar year ending with or within the employer’s
taxable year. Remuneration is treated as paid on the first date that the right to the remuneration is not subject to a substantial risk of forfeiture within the meaning of section 457(f)(3)(B) (regardless of whether the arrangement under which the amount is or will be paid is subject to section 457(f) or section 409A). An amount of remuneration is subject to a substantial risk of forfeiture if the right to the remuneration would be treated as subject to a substantial risk of forfeiture under Prop. Treas. Reg. § 1.457-12(e)(1). In general, this means that the amount is subject to a substantial risk of forfeiture only if entitlement to the amount is conditioned on the future performance of substantial services, or upon the occurrence of a condition that is related to a purpose of the remuneration if the possibility of forfeiture is substantial. See Prop. Treas. Reg. § 1.457-12(e)(1) for further guidance on the application of this standard.\footnote{When the proposed regulations under section 457(f) are finalized, the Treasury Department and the IRS anticipate providing further guidance on how and when those final regulations apply for purposes of section 4960.}

(b) \textbf{Amount of remuneration treated as paid} – (1) \textbf{In general.} The amount of remuneration treated as paid upon vesting is the present value (on the vesting date) of the future payments to which the participant has a legally binding right. The present value of the right to future payments as of the vesting date includes any earnings that have accrued as of the vesting date. The present value must be determined using

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reasonable actuarial assumptions. Present value determined in accordance with the rules set forth in Prop. Treas. Reg. § 1.457-12(c)(1), including the assumptions regarding payment timing set forth in those proposed regulations, will be deemed to have been determined using reasonable actuarial assumptions. For purposes of determining the present value of remuneration under a nonaccount balance plan described in Treas. Reg. § 1.409A-1(c)(2)(i)(C) that is scheduled to be actually or constructively paid within 90 days of vesting, the employer may elect to treat the nominal amount that is to be paid as the present value of the amount on the date of vesting.

Net earnings, as defined in paragraph (b)(2)(C), on previously paid remuneration, as defined in paragraph (b)(2)(D)(i), are treated as paid at the close of the calendar year in which they accrue. For example, the present value of vested remuneration credited to an employee’s account under an account balance plan described in Treas. Reg. § 1.409A-1(c)(2)(i)(A) (under which the earnings and losses attributed to the account are based solely on a predetermined actual investment or a reasonable market interest rate) is treated as paid on the date credited to the employee’s account, but the present value of any net earnings accrued on that amount (the increase in value due to the predetermined actual investment or a reasonable market interest rate) is treated as paid at the close of the calendar year in which they accrue. Similarly, the present value of a vested, fixed amount of remuneration under a nonaccount balance plan described in Treas. Reg. § 1.409A-1(c)(2)(i)(C) is treated as paid on the date of vesting, but the present value of the net earnings on that amount (the increase in the present value) is treated as paid at the close of the calendar year in which they accrue.
(2) **Earnings and losses.** (A) **Earnings.** Earnings generally refer to any increase in the vested present value of any previously paid remuneration as of the close of a calendar year, regardless of whether the plan or arrangement denominates such increase as earnings, to the extent the employee’s right to payment of the increase is vested. For example, an increase in the vested account balance of a nonqualified deferred compensation plan based solely on the investment return of a predetermined actual investment (and disregarding any additional contributions) constitutes earnings. Similarly, an increase in the vested present value of a benefit under a nonqualified nonaccount balance plan described in Treas. Reg. § 1.409A-1(c)(2)(i)(C) due solely to the passage of time (and disregarding any additional benefit accruals) constitutes earnings. However, an increase in an account balance of a nonqualified deferred compensation plan due to a salary reduction contribution or an employer contribution does not constitute earnings. Likewise, an increase in the benefit under a nonaccount balance plan described in Treas. Reg. § 1.409A-1(c)(2)(i)(C) due to an additional year of service or an increase in compensation that is reflected in a benefit formula does not constitute earnings.

(B) **Losses.** Losses generally refer to any decrease in the vested present value of any previously paid remuneration as of the close of the calendar year, regardless of whether the plan denominates that decrease as losses.

(C) **Net earnings and losses.** Net earnings and losses for each covered employee are determined on a net aggregate basis for each taxable year based on the previously paid remuneration paid by the employer. For example, losses under an account balance plan described in Treas. Reg. § 1.409A-1(c)(2)(i)(A) may offset
earnings under a nonaccount balance plan described in Treas. Reg. § 1.409A-1(c)(2)(i)(C) maintained by the same employer for the same employee, but earnings and losses from a plan maintained by another employer are disregarded.

Net earnings refer to the amount (if any) by which the earnings accrued during a calendar year ending with or within the taxable year (as described in Q/A–2) on any previously paid remuneration exceeds the sum of the losses accrued on those amounts during that calendar year and any net losses carried forward from a previous taxable year. Net losses refer to the amount (if any) by which the sum of the losses accrued during a calendar year ending with or within the taxable year (as described in Q/A–2) on any previously paid remuneration and the net losses carried forward from a previous taxable year exceeds the earnings accrued on those amounts during that calendar year. Losses do not reduce the remuneration treated as paid in a calendar year except to the extent of the earnings for that calendar year. Thus, if an employee vests in an amount of earnings under a nonaccount balance plan within the meaning of Treas. Reg. § 1.409A-1(c)(2)(i)(C), and also has losses under an account balance plan within the meaning of Treas. Reg. § 1.409A-1(c)(2)(i)(A) that exceed the vested earnings treated as remuneration under the nonaccount balance plan, those excess losses are carried forward to the next following taxable year and offset vested earnings for purposes of determining net earnings or losses for that taxable year. If, for the next following year, there are not sufficient earnings to offset the entire amount of losses carried forward from the previous year (and any additional losses), the offset process repeats for each later year until there are earnings for the calendar year in excess of the losses carried forward.
(D) **Previously paid remuneration** – (i) **In general.** Remuneration is treated as previously paid remuneration for a taxable year to the extent that, by the close of the calendar year ending with or within such taxable year (as described in Q/A–2), it is treated as paid under Q/A–13(b)(1) but is not actually or constructively paid.

(ii) **Employee who becomes a covered employee.** Any remuneration that is vested but is not actually or constructively paid as of the close of the calendar year preceding the calendar year ending with or within the taxable year of the employer for which an employee first becomes a covered employee of an ATEO is treated as paid for the employer’s preceding taxable year. For example, if an employee first becomes a covered employee of an employer for the employer’s taxable year ending June 30, 2022, any remuneration that was vested but was not actually or constructively paid as of December 31, 2020, is treated as paid for the taxable year ending June 30, 2021, and thus is not subject to the excise tax. Net losses from the preceding taxable year do not carry forward to the taxable year an employee becomes a covered employee.

(iii) **Pre-effective date remuneration.** Any remuneration that was vested but was not actually or constructively paid as of the close of the taxable year preceding the first taxable year in which section 4960 is effective for the employer is treated as paid for the preceding taxable year and is not subject to the excise tax. Thus, for an employer that uses a calendar year taxable year, the present value of any remuneration that was vested but was not actually or constructively paid as of December 31, 2017, is treated as paid for taxable year 2017. For an employer that uses a non-calendar year taxable year, the present value of any remuneration that was vested but was not actually or constructively paid as of the close of the taxable year that includes December 31, 2017.
(for example, June 30, 2018 in the case of an employer with a taxable year beginning July 1 and ending June 30) is treated as paid for that taxable year. Regardless of the employer’s taxable year, there is no carryover of net losses from the preceding taxable year to the first taxable year for which section 4960 is effective.

(c) **Examples.** The following examples illustrate the rules described in this Q/A–13.

**Example 1.** E is a covered employee of R, an ATEO that uses a calendar year taxable year. E participates in a nonqualified deferred compensation plan in which the account balance is adjusted based on the investment returns on predetermined actual investments chosen by the employee. On January 1, 2019, R credits $100,000 to E’s account under the plan, subject to the requirement that E remain employed through June 30, 2021. On June 30, 2021, the vested account balance is $110,000. Due to earnings or losses on the account balance, the closing account balance on each of the following dates is: (i) $115,000 on December 31, 2021, (ii) $120,000 on December 31, 2022, (iii) $100,000 on December 31, 2023, and (iv) $110,000 on December 31, 2024. During 2025, E defers an additional $10,000 under the plan, which is vested at the time of deferral. On December 31, 2025, the closing account balance is $125,000. In 2026, R distributes $10,000 to E under the plan. On December 31, 2026, the closing account balance is $135,000 due to earnings on the account balance.

**2019 and 2020 (nonvested amounts).** For 2019 and 2020, R pays no remuneration to E under the plan. The substantial future services condition is not met; thus, any amount deferred under the plan, including unvested earnings, remains subject to a substantial risk of forfeiture within the meaning of section 457(f)(3)(B) as of December 31, 2019, and December 31, 2020.

**2021 (amounts in year of vesting).** For 2021, R pays E $115,000 of remuneration, including (i) $110,000 of remuneration on June 30, 2021, when the substantial future services condition is met and the amount is no longer subject to a substantial risk of forfeiture within the meaning of section 457(f)(3)(B), and (ii) an additional $5,000 of earnings on the previously paid remuneration ($110,000) on December 31, 2021.

**2022 (earnings).** For 2022, R pays E $5,000 of remuneration, the additional earnings on the previously paid remuneration ($115,000) as of December 31, 2022.

**2023 (losses).** For 2023, R pays no remuneration to E since the vested present value of the previously paid remuneration ($120,000) declines to $100,000 as of December 31, 2023. The $20,000 loss for 2023 does not reduce any amount previously treated as remuneration but is available for carry over to future taxable years.
2024 (recovery of losses through earnings). For 2024, R pays no remuneration to E, since the vested present value of the previously paid remuneration ($120,000) was $110,000 as of December 31, 2024. Due to earnings on the account balance, R recovers $10,000 of the $20,000 of losses carried over from 2023. The net losses as of December 31, 2024, are $10,000, and none of the $10,000 in earnings during 2024 is remuneration paid in 2024.

2025 (no recovery of losses against additional deferrals of compensation). For 2025, R pays E $10,000 of remuneration to E. The additional $10,000 deferral is not subject to a substantial risk of forfeiture within the meaning of section 457(f)(3)(B), and thus is remuneration paid on the date deferred. This deferral increases the amount previously treated as remuneration from $120,000 to $130,000. Additionally, due to earnings on the account balance, R recovers $5,000 of losses of the $10,000 of losses carried over from 2024, none of which was remuneration for 2025, so that the net losses as of December 31, 2025 is $5,000.

2026 (distributions, recovery of remainder of losses through earnings and additional earnings). For 2026, R pays E $15,000 in remuneration. The vested present value of the account balance increases by $20,000 to $135,000 as of December 31, 2026. Therefore, due to earnings on the account balance, R recovers the remaining $5,000 of losses carried over from 2025 and pays E an additional $15,000 of remuneration as earnings. The $10,000 distribution reduces the amount of previously paid remuneration ($130,000) to $120,000, and the additional remuneration paid in 2026 increases the amount of previously paid remuneration by $15,000 to $135,000.

Example 2. F is a covered employee of S, an ATEO, and is also employed by corporation C, a related organization. S and C are calendar year taxpayers. On January 1, 2018, C and F enter into an agreement under which C will pay F $100,000 on December 31, 2021, if F remains employed by C through January 1, 2020. F remains employed by C through January 1, 2020. On January 1, 2020, the present value based on reasonable actuarial assumptions of the $100,000 to be paid on December 31, 2021 is $75,000. On December 31, 2020, the vested present value increases to $85,000 due solely to the passage of time. On December 31, 2021, C pays F $100,000.

2018 and 2019. For 2018 and 2019, C pays F no remuneration because the amount deferred under the plan remains subject to a substantial risk of forfeiture within the meaning of section 457(f)(3)(B).

2020. For 2020, C pays F $75,000 in remuneration on January 1, 2020, which is the vested present value of $100,000 payable on December 31, 2021. In addition C pays F an additional $10,000 in remuneration on December 31, 2020 as earnings based on the increase in the vested present value of the previously paid remuneration ($75,000) to $85,000 as of December 31, 2020.
2021. For 2021, C pays R $15,000 in additional remuneration and distributes $100,000 of previously paid remuneration. The $100,000 distribution is treated as reducing the amount of previously paid remuneration ($85,000) to zero, and the remaining $15,000 is a payment of earnings.

Example 3. G is a covered employee of T, an ATEO that uses a calendar year taxable year. G participates in a nonqualified deferred compensation plan in which the account balance is adjusted based on the investment returns on predetermined actual investments chosen by the employee. All amounts credited under the plan are vested when credited. On December 31, 2017, T credits $100,000 to G’s account and the closing account balance is $100,000. On June 30, 2018, T credits $50,000 to G’s account. On December 31, 2018, T credits $50,000 to G’s account and the closing account balance is $210,000.

2017. T is a calendar year taxpayer, so the present value of all remuneration in which G was vested but that was not actually or constructively paid to G as of December 31, 2017, ($100,000) is treated as paid for 2017 and is not subject to excise tax under section 4960.

2018. For 2018, T pays G $110,000 of remuneration, including $50,000 credited to G’s account on June 30 and $50,000 credited on December 31 (totaling $100,000), plus $10,000 in remuneration as earnings, as the vested present value of the $200,000 of previously paid remuneration ($100,000 as of December 31, 2017 + $100,000 in 2018) increases to $210,000 as of December 31, 2018.

Example 4. Assume the same facts as Example 3, except that T uses a non-calendar year taxable year that begins on July 1 and ends on June 30. The closing account balance on June 30, 2018 is $155,000.

Amounts paid through June 30, 2018. T is a non-calendar year taxpayer, so the present value of all remuneration in which G is vested but that is not actually or constructively paid as of the close of the first taxable year ending after December 31, 2017 (June 30, 2018) ($155,000) is treated as paid for that year and is not subject to excise tax under section 4960.

Amounts paid from July 1 through December 31, 2018. For the taxable year ending June 30, 2019, T pays G $55,000 in remuneration, including $50,000 credited to G’s account on December 31, 2018, plus $5,000 in remuneration as earnings, as the previously paid remuneration ($155,000 as of June 30, 2018 + $50,000 credited on December 31, 2018) increases to $210,000 as of December 31, 2018.

Example 5. H is an employee of U, an ATEO that uses a calendar year taxable year. H participates in a nonqualified deferred compensation plan in which the account balance is adjusted based on the investment returns on predetermined actual investments chosen by the employee. All amounts credited under the plan are vested when credited. On January 1, 2018, U credits $100,000 to H’s account under the plan. On December 31, 2018, the closing account balance is $105,000. On January 1, 2019,
U credits $100,000 to H's account. On December 31, 2019, the closing account balance is $210,000. H becomes a covered employee of U for U's taxable year ending December 31, 2019.

2018 (remuneration paid before becoming a covered employee). Remuneration that is vested as of the last day of the calendar year preceding the calendar year for which the employee becomes a covered employee is not subject to excise tax under section 4960. Thus, H's vested account balance on December 31, 2018 ($105,000) is not subject to excise tax under section 4960.

2019 (remuneration in the year an employee becomes a covered employee). For the taxable year ending December 31, 2019, U pays H $105,000 of remuneration, including the $100,000 credited to H's account on January 1, 2019, plus $5,000 in net earnings in 2019, the amount by which the vested account balance at the close of the calendar year ($210,000) exceeds the amount of previously paid remuneration ($205,000, consisting of $105,000 as of December 31, 2018 + $100,000 paid on January 1, 2019).

Example 6. J is a covered employee of T, an ATEO that uses a calendar year taxable year. J participates in a nonqualified deferred compensation plan under which T agrees to pay J $100,000 two months after the date a specified performance goal that is a substantial risk of forfeiture within the meaning of section 457(f)(3)(B) is satisfied. J satisfies the performance goal on November 30, 2019. T elects to treat the amount to be paid as the present value of the amount at vesting.

Election to treat amount payable within 90 days treated as paid at vesting. For taxable year 2019, T pays J $100,000 of remuneration. J vests in the $100,000 amount in 2019 upon meeting the performance goal. Under the general rule, T would be required to treat the present value as of November 30, 2019 of $100,000 payable in 2020 (two months after the performance goal was met) as paid in 2019, the difference between that amount and the present value as of December 31, 2019 as earnings for 2019, and any difference between the sum of the two present values and $100,000 as earnings for 2020. However, because T elected to treat the amount of remuneration payable within 90 days of vesting as paid at vesting in 2019, the $100,000 payable to J in 2020 is treated as remuneration paid in 2019 for purposes of section 4960(a)(1).

Q–14: How is liability for the section 4960(a)(1) excise tax determined if remuneration is paid to a covered employee by both an applicable tax-exempt organization and a related organization?

A–14: (a) In general. As provided in section 4960(c)(4)(C), in any case in which an ATEO includes remuneration from one or more other employers of a covered employee that are related organizations in determining the excise tax imposed by section
4960(a)(1), each employer is liable for the excise tax in an amount that bears the same ratio to the total excise tax determined with respect to the remuneration as—

(1) the amount of remuneration paid by the employer with respect to that employee, bears to

(2) the amount of remuneration paid by all the employers to that employee.

(b) Calculation of excise tax involving multiple related organizations. Each ATEO calculates liability for the excise tax under section 4960(a)(1) with respect to a covered employee by including remuneration paid by the ATEO and any related organization that employs the covered employee and then allocating that excise tax liability among each of the employers. However, the ATEO may also be liable for the excise tax under section 4960(a)(1) as a related organization with respect to another ATEO that calculates the excise tax for its own covered employees. If an employer is liable for the excise tax under section 4960(a)(1) as an ATEO and as a related organization for the same remuneration to a covered employee, the employer is not liable for the excise tax in both capacities; rather it is liable for the greater of the excise tax it would owe as an ATEO or the excise tax it would owe as a related organization with respect to that covered employee.

In order to calculate liability under this provision, an ATEO should take the following steps:

(1) calculate remuneration paid (other than any excess parachute payment) for each of its covered employees, including remuneration from any related organization (if remuneration for any covered employee calculated in this step (1) is more than $1
million, then the remuneration over $1 million is subject to the excise tax under section 4960(a)(1) at the rate of tax under section 11);

(2) calculate the share of liability for each employer that employs the covered employee that was included in step (1) as a fraction of the total excise tax liability that bears the same ratio to the total excise tax as the amount of remuneration paid by the employer bears to the total remuneration calculated in step (1);

(3) inform any related organization of its share of liability calculated in step (2);

(4) obtain information on the ATEO’s share of liability as a related organization for any covered employee of another ATEO. If the ATEO is a related organization to more than one other ATEO, treat the ATEO’s highest share of liability as a related organization as its liability as a related organization for the covered employee; and

(5) compare the ATEO’s liability as an ATEO in step (2) to its share of liability as a related organization under step (4) for each of the ATEO’s covered employees. The ATEO reports the greater of the share calculated under step (4) or the share calculated under step (2) (or the share calculated under step (2) if they are the same) as the ATEO’s share of liability for remuneration paid to the covered employee.

(c) Change in related status during the year. If an employer becomes or ceases to be a related organization with respect to an ATEO during the calendar year ending with or within the ATEO’s taxable year, then only the remuneration paid by the related organization to a covered employee with respect to services performed during that portion of the calendar year that the employer is a related organization is included for purposes of calculating liability for the excise tax under section 4960(a)(1). Thus, only
remuneration that vests while the employer is a related organization with regard to the ATEO is taken into account for purposes of section 4960.

(d) Examples. The following examples illustrate the rules of this Q/A–14.

Assume for purposes of these examples that the rate of excise tax under section 4960 is 21 percent.

**Example 1.** F and G are each ATEOs; G is a related organization with respect to F. E is a covered employee of both F and G. F pays E $1.2 million of remuneration, and G pays E $800,000 of remuneration for a total of $2 million of remuneration, and $1 million of excess remuneration. The total excise tax is $210,000 (21 percent of the $1 million excess remuneration). F paid 3/5 of E’s total remuneration ($1.2 million / $2 million); thus, F is liable for 3/5 of the excise tax, which is $126,000. G is liable for 2/5 of the excise tax, which is $84,000.

**Example 2.** H, I, and J are each ATEOs. J owns 60 percent of the stock of Corporation K. Sixty percent of I’s directors are representatives of H. In addition, 60 percent of J’s directors are representatives of I. Employee L is a covered employee of H, I, and J. H, I, J, and K each pay Employee L $1.2 million per year. Under the rules described in Q/A–7 and Q/A–8, I determines that its related organizations are H and J. H determines that its related organization is I. J determines that its related organizations are I and K.

**ATEO I.** Under I’s calculation as an ATEO, Employee L receives a total of $3.6 million in remuneration from H, I, and J (3 x $1.2 million). The total excise tax is $546,000 (21 percent of the $2.6 million excess remuneration). H, I, and J each paid 1/3 of the total remuneration to Employee L ($1.2 million / $3.6 million); thus, H, I, and J are each liable for 1/3 of the excise tax, which is $182,000.

**ATEO H.** Under H’s calculation as an ATEO, Employee L receives a total of $2.4 million in remuneration from H and I (2 x $1.2 million). The total excise tax is $294,000 (21 percent of the $1,400,000 excess remuneration). H and I each paid 1/2 of the total remuneration to Employee L ($1.2 million / $2.4 million); thus, H and I are each liable for 1/2 of the excise tax, which is $147,000.

**ATEO J.** Under J’s calculation as an ATEO, L receives a total of $3.6 million in remuneration from I, J, and K (3 x $1.2 million). The total excise tax is $546,000 (21 percent of the $2.6 million excess remuneration). I, J, and K each paid 1/3 of the total remuneration to Employee L ($1.2 million / $3.6 million); thus, I, J, and K are each liable for 1/3 of the excise tax, which is $182,000.

**Liability of H, I, J, and K.** I is liable as a related organization for $147,000 of excise tax according to H’s calculation and $182,000 according to J’s calculation, but under I’s calculation, I is liable for $182,000 of excise tax. Thus, I’s excise tax liability is...
H is liable for $182,000 of excise tax under I’s calculation, which is greater than the $147,000 of excise tax H calculated under H’s calculation. Thus, H’s excise tax liability is $182,000. J is liable as a related organization for $182,000 of excise tax under I’s calculation, but is liable for $182,000 of excise tax under J’s calculation. Thus, J’s excise tax liability is $182,000. K is liable as a related organization for $182,000 of excise tax according to J’s calculation.

E. Medical and Veterinary Services

Q–15: How is remuneration for medical services treated under section 4960?

A–15: (a) In general. Remuneration paid to a licensed medical professional for the direct performance of medical services (including nursing services) or veterinary services by the professional is not remuneration for purposes of calculating the excess remuneration (if any) subject to the excise tax. However, remuneration paid to the professional for any other services, including administrative and management services associated with the performance of medical or veterinary services, is remuneration for purposes of calculating the excess remuneration (if any) subject to the excise tax. Remuneration for medical services is also disregarded for purposes of determining whether an individual is a covered employee and for purposes of determining whether a payment is a parachute payment.

(b) Licensed medical professional. A licensed medical professional is an individual who is licensed under state or local law to perform medical services (including nursing services) or veterinary services.

(c) Medical and veterinary services. A licensed medical professional directly performs medical services to the extent that the services constitute “medical care” as defined in section 213(d)(1)(A) and the regulations thereunder. Thus, medical services are services for the diagnosis, cure, mitigation, treatment, or prevention of disease, including services for the purpose of affecting any structure or function of the body. For
example, teaching or research services are not medical services to the extent the services performed do not relate directly to the diagnosis, cure, mitigation, treatment, or prevention of disease or affect a structure or function of the body. For purposes of section 4960, documenting the care and condition of a patient is part of the direct performance of medical services, as is accompanying another licensed professional as a supervisor while that medical professional performs medical services. But managing an organization’s operations, including scheduling, staffing, appraisal, and other similar functions that may relate to a particular medical professional or professionals who perform medical services, is not the performance of medical services. With respect to veterinary services, the rules in this paragraph apply by analogy to determine whether services performed with respect to an animal are veterinary services.

(d) **Allocation.** If during a calendar year an employer pays a covered employee remuneration for both medical services and other services, the employer must make a reasonable, good faith allocation between remuneration for medical services and other services. For example, if a medical doctor receives remuneration for both medical services and for administrative or management services, the employer must make a reasonable allocation between remuneration for the medical services and remuneration for the administrative or management services. For this purpose, if an employment agreement or similar written arrangement sets forth the remuneration to be paid for particular services, that allocation of remuneration must be applied unless the facts and circumstances demonstrate that the amount allocated for medical services is unreasonable for those services or that the allocation was established for purposes of avoiding application of the excise tax under section 4960. If some or all of the
remuneration is not reasonably allocated in an employment or other agreement, an employer may use any reasonable allocation method. For example, an employer may use a representative sample of records, such as patient, insurance, and Medicare/Medicaid billing records or internal time reporting mechanisms to determine the time spent providing medical services, and then allocate remuneration to medical services in the proportion such time bears to the total hours the covered employee worked for the employer for purposes of making a reasonable allocation of remuneration. Similarly, if some or all of the remuneration is not reasonably allocated in an employment or other agreement, an employer may use salaries or other remuneration for duties comparable to those the employee performs (for example, hospital administrator and physician) for purposes of making a reasonable allocation between remuneration for medical services and nonmedical services. These same allocation rules also apply with respect to veterinary services.

(e) Examples. The following examples illustrate the rules of this Q/A–15. Assume for purposes of these examples that there is no employment agreement or similar written arrangement allocating remuneration to any particular services.

Example 1. H is a hospital and is an ATEO. A is a covered employee of H. A provides patient care services to H and also provides management and administrative services to H as the head of a medical practice group within H. Based on a representative sample of insurance and Medicare billing records, as well as time reports that A submits to H, H determines that A spends half of her time providing medical care to patients and half of her time performing administrative and management services in her capacity as head of the practice group. H allocates half of A’s remuneration to medical services. H’s allocation of A’s remuneration is a reasonable, good faith allocation. Accordingly, only the portion of A’s remuneration allocated to the other, non-medical services is remuneration for purposes of the excise tax.

Example 2. R is a medical research organization and is an ATEO. B is a covered employee of R. B is employed to work on a research trial. B provides an experimental treatment to patients afflicted by a disease. B tracks the patients' individual conditions
in a manner that occurs ordinarily in a medical practice. As part of the research trial, B also compiles the patients' records on their individual conditions and prepares reports detailing both individual and overall results. These reports are not ordinarily prepared for patients or provided to patients in a medical practice. Although the primary purpose of B's activities is research, B is treating a patient's disease within the meaning of section 213(d) when B performs services that are ordinarily performed in a medical practice, and, thus, these services are medical services for purposes of section 4960. Accordingly, any remuneration allocable to the medical services is not remuneration for purposes of the excise tax. However, B does not directly perform medical services to the extent B performs research services that are not ordinarily performed in a medical practice; accordingly, any remuneration allocable to those services is remuneration for purposes of section 4960.

Example 3. C is a medical doctor who is employed by a university hospital that is an ATEO. C's duties include overseeing and teaching a group of resident physicians who have a restricted license to practice medicine. C's duties include supervising and instructing the resident physicians while they treat patients. C's other duties include instructing the resident physicians in a classroom setting. To the extent that C, in conjunction with the resident physicians, performs services directly related to the diagnosis, cure, mitigation, treatment or prevention of a patient's disease, or affecting a structure or function of the patient's body, those services constitute "medical care" for purposes of section 213(d), and, thus, C directly performs medical services. Accordingly, any remuneration allocable to those medical services is not remuneration for purposes of the excise tax. However, because classroom instruction does not involve actual patient treatment, those activities are not medical care for purposes of section 213(d), and, thus, do not constitute the direct performance of medical services. Accordingly, any remuneration allocable to those services is remuneration for purposes of section 4960.

F. Excess Parachute Payments

Q–16: What is an excess parachute payment under section 4960(c)(5)(A)?

A–16: The term “excess parachute payment” means an amount equal to the excess (if any) of the total amount of any parachute payment over the portion of the base amount allocated to such payment.

Q–17: What is a parachute payment under section 4960(c)(5)(B)?

A–17: (a) In general. The term “parachute payment” means any payment in the nature of compensation made by an ATEO (or a predecessor organization of the ATEO) or a related organization to (or for the benefit of) a covered employee if–
(1) the payment is contingent on the employee’s separation from employment with the employer; and

(2) the aggregate present value of the payments in the nature of compensation to (or for the benefit of) the individual that are contingent on the separation equals or exceeds an amount equal to three times the base amount.

(b) Exclusions. The term “parachute payment” does not include any payment: (1) to or from a plan described in section 401(a) that includes a trust exempt from tax under section 501(a), an annuity plan described in section 403(a), a simplified employee pension (as defined in section 408(k)), or a simple retirement account described in section 408(p);

(2) made under or to an annuity contract described in section 403(b) or a plan described in section 457(b);

(3) made to a licensed medical professional (including a veterinarian) for the performance of medical or veterinary services performed by such professional; or

(4) made to an individual who is not a highly compensated employee as defined in section 414(q). See generally Treas. Reg. § 1.414(q)-1T. Under Treas. Reg. § 1.414(q)-1T, Q/A-14(a)(1), for purposes of determining the group of highly compensated employees for a determination year, the determination year calculation is made on the basis of the applicable year of the plan or other entity for which a determination is made and the look-back year calculation is made on the basis of the twelve month period immediately preceding that year. An ATEO that maintains a qualified retirement plan should have already identified the employees who are HCEs for purposes of the plan and the same individuals are HCEs for purposes of section
4960. For an ATEO that does not maintain a qualified retirement plan, the rules are applied by analogy, substituting the calendar year for the plan year. Accordingly, in 2019, for an ATEO that does not maintain a qualified retirement plan, the ATEO would use the employees’ 2018 annual compensation (as defined in Treas. Reg. § 1.414(q)-1T Q/A–13, including any of the safe harbor definitions if applied consistently to all employees) to determine whether and which employees were HCEs for 2019 for purposes of section 4960. If an employee is an HCE at the time of the separation from employment, then any parachute payment made as a consequence of the separation from employment is treated as paid to an HCE, even if the payments occur during one or more later taxable years (that is, taxable years after the taxable year during which the employee separated from employment).

Q–18: What is a payment in the nature of compensation?
A–18: For purposes of section 4960(a)(2), any payment—in whatever form—is a payment in the nature of compensation if the payment arises out of an employment relationship, including holding oneself out as available to perform services and refraining from performing services. Thus, for example, payments made under a covenant not to compete or a similar arrangement are payments in the nature of compensation. A payment in the nature of compensation includes (but is not limited to) wages and salary, bonuses, severance pay, fringe benefits, life insurance, pension benefits, and other deferred compensation (including any amount characterized by the parties as interest or earnings thereon). A payment in the nature of compensation also includes cash when paid, the value of the right to receive cash, including the value of accelerated vesting, or a transfer of property. However, a payment in the nature of
compensation does not include attorney’s fees or court costs paid or incurred in connection with the payment of any parachute payment or a reasonable rate of interest accrued on any amount during the period the parties contest whether a payment will be made.

Q–19: When is a payment in the nature of compensation considered to be made?
A–19: (a) In general. A payment in the nature of compensation is considered made in the taxable year in which it is includible in the covered employee’s gross income (in the case of taxable non-cash fringe benefits, consistent with Announcement 85-113, 1985-31 I.R.B. 31) or, in the case of fringe benefits and other benefits that are excludible from income, in the taxable year the benefits are received.

(b) Transfers of section 83 property. A transfer of property in connection with the performance of services that is subject to section 83 is considered a payment made in the taxable year in which the property is transferred or would be includible in the gross income of the covered employee under section 83 and the regulations thereunder, disregarding any election made by the employee under section 83(b) or 83(i). Thus, in general, such a payment is considered made at the later of the date the property is transferred (as defined in Treas. Reg. § 1.83-3(a)) to the covered employee or the date the property becomes substantially vested (as defined in Treas. Reg. § 1.83-3(b) and (j)). The amount of the payment is the compensation income as determined under section 83 and the regulations thereunder, disregarding any amount includible in income pursuant to an election made by an employee under section 83(b).

(c) Stock options and stock appreciation rights. For purposes of this Q/A–19, an option (including an option to which section 421 applies) is treated as property that is
transferred when the option becomes vested (regardless of whether the option has a readily ascertainable fair market value as defined in Treas. Reg. § 1.83-7(b)). For purposes of determining the timing and amount of any payment related to the option, the principles of Treas. Reg. § 1.280G-1, Q/A–13 and Rev. Proc. 2003-68, 2003-2 C.B. 398, apply. Thus, the vesting of an option as a result of a covered employee’s separation from employment is a payment in the nature of compensation.

(d) Consideration paid by covered employee. Any payment in the nature of compensation is reduced by the amount of any money or the fair market value of any property (owned by the covered employee without restriction) that is (or will be) transferred by the covered employee in exchange for the payment.

Q–20: What is a payment that is contingent on an employee’s separation from employment?

A–20: (a) In general. A payment is contingent on an employee’s separation from employment if the facts and circumstances indicate that the employer would not make the payment in the absence of an involuntary separation from employment. A payment, the right to which is not subject to a substantial risk of forfeiture within the meaning of section 457(f)(3)(B) at the time of an involuntary separation from employment, generally is a payment that would have been made in the absence of a separation from employment (and, thus, is not contingent on a separation from employment), except that the increased value of an accelerated payment of a vested amount described in Q/A–24(b) resulting from an involuntary separation from employment is not treated as a payment that would have been made in the absence of a separation from employment. A payment the right to which is no longer subject to a substantial risk of forfeiture within the meaning of section 457(f)(3)(B) as a result of an involuntary separation from employment.
employment, including a payment the vesting of which would have occurred had the employee remained employed for a subsequent period of time but that is accelerated due to the separation from employment as described in Q/A–24(c), is not treated as a payment that would have been made in the absence of an involuntary separation from employment (and thus is contingent on a separation from employment). A payment would be made in the absence of a separation from employment if it is substantially certain at the time of the separation from employment that the payment would be made whether or not the separation occurred. A payment does not fail to be contingent on a separation from employment merely because the payment is conditioned upon the execution of a release of claims, noncompetition or nondisclosure provisions, or other similar requirements. If an employee separates from service and continues to provide services (including as a bona fide independent contractor), payments for those services are not payments that are contingent on a separation from employment to the extent those payments are reasonable and are not made because of the involuntary separation from employment.

(b) Employment agreements. (1) If a covered employee involuntarily separates from employment before the end of a contract term and is paid damages for breach of contract pursuant to an employment agreement, those damages are treated as a payment that is contingent on a separation from employment. For purposes of this paragraph (b), an employment agreement means an agreement between an employee and employer that describes, among other things, the amount of compensation or remuneration payable to the employee for services performed during the term of the agreement.
(2) The following example illustrates the rules of this Q/A–20(b):

**Example.** A, a covered employee, has a three-year employment agreement with X, an ATEO. Under the agreement, A will receive a salary of $200,000 for the first year of the agreement, and for each succeeding year, an annual salary that is $100,000 higher than the previous year. The agreement provides that, in the event of A’s involuntary separation from employment without cause, A will receive the remaining salary due under the agreement. At the beginning of the second year of the agreement, X involuntarily terminates A’s employment without cause and pays A $700,000 representing the remaining salary due under the employment agreement ($300,000 for the second year of the agreement + $400,000 for the third year of the agreement). The $700,000 payment is treated as a payment that is contingent on a separation from employment.

(c) **Noncompetition agreements.** A payment under an agreement requiring a covered employee to refrain from performing services (for example, a covenant not to compete) is a payment that is contingent on a separation from employment for purposes of this Q/A–20 if the payment would not have been made in the absence of an involuntary separation from employment. For example, if a covenant not to compete including one or more payments contingent on compliance in whole or in part with the covenant not to compete is negotiated as part of a severance arrangement arising from an involuntary separation from employment, generally the payment(s) will be treated as contingent on a separation from employment.

(d) **Payment of amounts previously included in income or excess remuneration.** Actual or constructive payment of an amount that was previously includible in gross income is not a payment contingent on a separation from employment. For example, payment of an amount includible in income under section 457(f)(1)(A) due to the lapsing of a substantial risk of forfeiture on a date before the separation from employment is not a payment that is contingent on a separation from employment, even if the amount is paid in cash or otherwise to the employee because of the separation from employment.
In addition, actual or constructive payment of an amount treated as excess remuneration is not a payment that is contingent on a separation from employment (and thus is not a parachute payment), even if the amount is paid to the employee because of the separation from employment.

(e) **Window programs.** A payment under a window program is contingent on a separation from employment.

(f) **Anti-abuse provision.** Notwithstanding the foregoing paragraphs (a) through (e) of this Q/A-20, if the facts and circumstances demonstrate that either vesting or the payment of an amount (whether before or after the involuntary separation from employment) would not have occurred but for the involuntary nature of the separation from employment, the payment of the amount will be treated as contingent on a separation from employment. For example, an employer’s exercise of discretion to accelerate vesting of an amount shortly before an involuntary separation from employment may indicate that the acceleration of vesting was due to the involuntary nature of the separation from employment and, thus, was contingent on the employee’s separation from employment. Similarly, payment of amount in excess of an amount otherwise payable (for example, increased salary), shortly before or after an involuntary separation from employment, may indicate that the amount was paid because the separation was involuntary and, thus, was contingent on the employee’s separation from employment.

**Q–21: What is a payment made under a window program?**

**A–21:** A window program is a program established by an employer in connection with an impending separation from employment to provide separation pay, where the
program is made available by the employer for a limited period of time (no longer than 12 months) to employees who separate from employment during that period or to employees who separate from service during that period under specified circumstances. A payment made under a window program is treated as a payment that is contingent on an employee’s separation from employment notwithstanding that the employee may not have had an involuntary separation from employment.

Q–22: What is an involuntary separation from employment?
A–22: An involuntary separation from employment means a separation from employment due to the independent exercise of the employer’s unilateral authority to terminate the employee’s services, other than due to the employee’s implicit or explicit request, if the employee was willing and able to continue performing services. An involuntary separation from employment may include an employer’s failure to renew a contract at the time the contract expires, provided that the employee was willing and able to execute a new contract providing terms and conditions substantially similar to those in the expiring contract and to continue providing services. The determination of whether a separation from employment is involuntary is based on all the facts and circumstances. An employee’s voluntary separation from employment for good reason (as defined in Prop. Treas. Reg. § 1.457-11(d)(2)(ii), 81 FR 40548, 40560) is treated as an involuntary separation from employment.

Q–23: What is a separation from employment?
A–23: For purposes of section 4960, separation from employment generally has the same meaning as separation from service as defined in Treas. Reg. § 1.409A-1(h), without regard to Treas. Reg. § 1.409A-1(h)(2) and (5) (application to independent
contractors), since generally only an employee may have a separation from employment and a change from employee status to bona fide independent contractor status would also be a separation from employment. See Q/A–12(d) regarding the treatment of an employee who also serves as a director (or in a substantially similar position). In addition, the definition of termination of employment in Treas. Reg. § 1.409A-1(h)(1)(ii) is modified such that an employer may not set the level of the anticipated reduction in future services that will give rise to a separation from employment and that the defaults set forth in the regulations apply. Thus, an anticipated reduction of the level of service of less than 50 percent is not treated as a separation from employment, an anticipated reduction of more than 80 percent is treated as a termination of employment, and the treatment of an anticipated reduction between those two levels is determined based on the facts and circumstances. Pursuant to Treas. Reg. § 1.409A-1(h), an employee generally separates from employment with the employer if the employee dies, retires, or otherwise has a termination of employment with the employer. Treas. Reg. § 1.409A-1(h) provides additional rules addressing leaves of absence, including military leaves of absence (Treas. Reg. § 1.409A-1(h)(1)(i)), asset purchase transactions (Treas. Reg. § 1.409A-1(h)(4)), and employees participating in collectively bargained plans covering multiple employers (Treas. Reg. § 1.409A-1(h)(6)). This notice adopts the rules provided in Treas. Reg. § 1.409A-1(h)(3), under which an employee separates from employment only if the employee has a separation from employment with the employer and all employers that would be considered a single employer under section 414(b) and (c), except that for purposes of section 4960, this notice uses the “at least 80 percent” rule
under section 414(b) and (c) rather than replacing it with “at least 50 percent.”

However, for purposes of determining whether there has been a separation from employment, a purported ongoing employment relationship between a covered employee and an ATEO or a related organization will be disregarded if the facts and circumstances demonstrate that the purported employment relationship is not bona fide or the primary purpose of the establishment or continuation of the relationship is avoidance of the application of section 4960.

Q–24: How is an accelerated payment or accelerated vesting resulting from an involuntary separation from employment treated?

A–24: (a) In general. As described in Q/A–24(b) and (c), if a payment is accelerated or a substantial risk of forfeiture lapses as a result of an involuntary separation from employment, only the value due to the acceleration is treated as contingent on a separation from employment. For purposes of this Q/A–24, the terms “vested” and “substantial risk of forfeiture” have the same meaning as provided in Q/A–13(a).

(b) Vested payments. If an involuntary separation from employment accelerates actual or constructive payment of an amount that vested without regard to the separation, the portion of the payment, if any, that is contingent on the separation from employment is the amount by which the present value of the accelerated payment exceeds the present value of the payment absent the acceleration. For this purpose, the payment of an amount otherwise due upon a separation from employment (whether voluntary or involuntary) is not treated as an acceleration of the payment because the payment timing was not accelerated due to the involuntary nature of the separation from employment. If the value of the payment absent the acceleration is not reasonably ascertainable, and the acceleration of the payment does not significantly increase the
present value of the payment absent the acceleration, the present value of the payment absent the acceleration is the amount of the accelerated payment (so the amount contingent on the separation from employment is zero). If the present value of the payment absent the acceleration is not reasonably ascertainable, but the acceleration significantly increases the present value of the payment, the future value of the payment contingent on the separation from employment is treated as equal to the amount of the accelerated payment. For this purpose, the acceleration of a payment by 90 days or less is not treated as significantly increasing the present value of the payment. For rules on determining present value, see Q/A–24(f) and Q/A–26 through Q/A–28.

(c) **Nonvested payments subject to a vesting service condition**—(1) If—

(A) a payment vests as a result of an involuntary separation from employment;

(B) disregarding the separation from employment, the payment was contingent only on the continued performance of services for the employer for a specified period of time; and

(C) the payment is attributable, at least in part, to the performance of services before the date the payment is made or becomes certain to be made;

then the portion that is contingent on the separation from employment is the amount described in Q/A–24(b), plus the value of the lapse of the obligation to continue to perform services described in paragraph (c)(3). The portion of the payment that is contingent on the separation from employment under this Q/A–24(c) cannot exceed the amount of the accelerated payment, or, if the payment is not accelerated, the present value of the payment.
(2) For purposes of paragraph Q/A–24(b), the acceleration of the vesting of a stock option or the lapse of a restriction on restricted stock is considered to significantly increase the value of a payment.

(3) The value of the lapse of the obligation to continue to perform services (described in Q/A–24(c)(1)) is one percent of the amount of the accelerated payment multiplied by the number of full months between the date that the employee’s right to receive the payment is vested and the date that, absent the acceleration, the payment would have been vested. This paragraph (c)(3) applies to the accelerated vesting of a payment in the nature of compensation even if the time when the payment is made is not accelerated. In that case, the amount reflecting the lapse of the obligation to continue to perform services is one percent of the present value of the future payment multiplied by the number of full months between the date that the individual's right to receive the payment is vested and the date that, absent the acceleration, the payment would have been vested.

(d) Nonvested payments subject to a vesting condition other than a service condition. Neither Q/A–24(b) nor (c) applies to a payment if (without regard to the separation from employment) vesting of the payment depends on an event other than the performance of services, such as the attainment of a performance goal, and the vesting event does not occur prior to the separation from employment. For example, neither Q/A-24(b) nor (c) apply if the payment not only vests due to the involuntary separation from employment (despite not having met a separate alternative vesting condition other than the continued performance of services) but the payment also is accelerated due to the involuntary separation from employment. In these
certain circumstances, the full amount of the accelerated payment is treated as contingent on the separation from employment under this Q/A–24(d).

(e) Application to benefits under a nonqualified deferred compensation plan. In the case of a payment of benefits under a nonqualified deferred compensation plan, Q/A–24(b) applies to the extent benefits under the plan are vested without regard to the separation from employment but the payment of benefits is accelerated due to the involuntary separation from employment. Q/A–24(c) applies to the extent benefits under the plan become vested as a result of the separation from employment and are attributable, at least in part, to the performance of services prior to vesting. For any other payment of benefits under a nonqualified deferred compensation plan (such as a contribution made due to the employee’s involuntary separation from employment) the full amount of the payment is contingent on the employee’s separation from employment.

(f) Present value. For purposes of this Q/A–24, if an accelerated payment is made, the increase in the present value of the payment due under the original payment schedule is determined based on the date on which the accelerated payment is made. The amount that is treated as contingent on the separation from employment is the amount by which the present value of the accelerated payment exceeds the present value of the payment absent the acceleration.

(g) Examples. See Treas. Reg. § 1.280G, Q/A–24(f) for examples that may be applied by analogy to illustrate the rules of this Q/A–24.
G. Three-Times-Base-Amount Test for Parachute Payments

Q–25: Are all payments that are in the nature of compensation, made to a covered employee, and contingent on a separation from employment, parachute payments?

A–25: (a) In general. To determine whether payments in the nature of compensation made to a covered employee that are contingent on the covered employee separating from employment with the ATEO are parachute payments, they must be compared to the individual’s base amount. To do this, the aggregate present value of all payments in the nature of compensation that are made or to be made to (or for the benefit of) the same covered employee by an ATEO (or any predecessor of the ATEO) or related organization and that are contingent on the separation from employment must be determined. If this aggregate present value equals or exceeds the amount equal to three times the individual’s base amount, the payments are parachute payments. If this aggregate present value is less than the amount equal to three times the individual’s base amount, no portion of the payments is a parachute payment. See Q/A–26 and Q/A–27 for rules on determining present value.

(b) Examples. The following examples illustrate the rules of this Q/A–25:

Example 1. A is a covered employee with respect to M, an ATEO. A’s base amount is $200,000. Payments in the nature of compensation that are contingent on a separation from employment totaling $800,000 are made to A on the date of the separation from employment. The payments are parachute payments because they have an aggregate present value at least equal to three times A’s base amount of $200,000 (3 x $200,000 = $600,000).

Example 2. Assume the same facts as in Example 1, except that the payments contingent on the separation from employment total $580,000. Because the payments do not have an aggregate present value at least equal to three times A’s base amount, no portion of the payments is a parachute payment.
Q–26: As of what date is the present value of a payment determined?

A–26: (a) In general. Except as otherwise provided in this Q/A–26, for purposes of determining if a parachute payment exceeds three times the base amount, the present value of a payment is determined as of the date of the separation from employment, or, if the payment is made prior to that date, the date on which the payment is made.

(b) Deferred payments. For purposes of determining whether a payment is a parachute payment, if a payment in the nature of compensation is the right to receive payments in a year (or years) subsequent to the year of the separation from employment, the value of the payment is the present value of the payment (or payments) calculated on the basis of reasonable actuarial assumptions and using the applicable discount rate for the present value calculation that is determined in accordance with Q/A–27.

(c) Health care. If the payment in the nature of compensation is an obligation to provide health care (including an obligation to purchase or provide health insurance), then for purposes of this Q/A–26 and for applying the three-times-base-amount test under Q/A–25, the present value of the obligation should be calculated in accordance with generally accepted accounting principles. For purposes of Q/A–25 and this Q/A–26, the obligation to provide health care is permitted to be measured by projecting the cost of premiums for health care insurance, even if no health care insurance is actually purchased. If the obligation to provide health care is made in coordination with a health care plan that the employer makes available to a group, then the premiums used for this purpose may be the allocable portion of group premiums.
Q–27: What discount rate is used to determine present value?

A–27: For purposes of computing the excise tax under section 4960(a)(2), present value generally is determined by using a discount rate equal to 120 percent of the applicable Federal rate (determined under section 1274(d) and the regulations thereunder) compounded semiannually. The applicable Federal rate to be used is the Federal rate that is in effect on the date as of which the present value is determined, using the period until the payment is expected to be made as the term of the debt instrument under section 1274(d). See Q/A–26. However, for any payment, the employer and the covered employee may elect to use the applicable Federal rate that is in effect on the date that the contract that provides for the payment is entered into, if that election is made in the contract.

Q–28: If the present value of a payment to be made in the future is contingent on an uncertain future event or condition, how is the present value of the payment determined?

A–28: (a) Treatment based on the estimated probability of payment. In certain cases, it may be necessary to apply the three-times-base-amount test or to allocate a portion of the base amount to a payment that is contingent on separation from employment at a time when the aggregate present value of all the payments is uncertain because the time, amount, or right to receive one or more of the payments is also contingent on the occurrence of an uncertain future event or condition. In that case, the employer must reasonably estimate whether it will make the payment. If the employer reasonably estimates there is a 50-percent or greater probability that it will make the payment, the full amount of the payment is considered for purposes of the three-times-base-amount test and the allocation of the base amount. If the employer reasonably estimates there
is a less than 50-percent probability that the payment will be made, the payment is not considered for either purpose.

(b) **Correction of incorrect estimates.** If the ATEO later determines that the estimate made under Q/A–28(a) was incorrect, it must reapply the three-times-base-amount test described in Q/A–25 (and, if necessary, reallocate the portion of the base amount allocated to previous payments in accordance with Q/A–32) to reflect the actual time and amount of the payment. In reapplying the three-times-base-amount test (and, if necessary, reallocating the base amount), the ATEO must determine the aggregate present value of payments paid or to be paid as of the date described in Q/A–26, using the discount rate described in Q/A–27. This redetermination may affect the amount of any excess parachute payment for a prior taxable year. However, if, based on the application of the three-times-base-amount test without regard to the payment described in this Q/A–28, an ATEO has determined it will pay an employee an excess parachute payment or payments, then the three-times-base-amount test does not have to be reapplied when a payment described in this Q/A–28 is made (or becomes certain to be made) if no base amount is allocated to such payment.

(c) **Initial option value estimate.** To the extent provided in published guidance of general applicability under § 601.601(d)(2) of this Chapter, an initial estimate of the value of an option subject to Q/A–19(c) is permitted to be made, with the valuation subsequently redetermined, and the three-times-base-amount test reapplied. Until such guidance is published, the guidance under section 280G applies by analogy.

(d) **Examples.** See Treas. Reg. § 1.280G–1, Q/A–33(d), for examples that may be applied by analogy to illustrate the rules of this Q/A–28.
Q–29: What is the base amount for purposes of section 4960(c)(5)(D)?

A–29: (a) **In general.** A covered employee’s base amount is the average annual compensation for services performed as an employee of the ATEO (including compensation for services performed for a predecessor entity of the ATEO), or a related organization with respect to which there has been a separation from employment, if the compensation was includible in the gross income of the individual for taxable years in the base period (including amounts that were excluded under section 911), or would have been includible in the individual’s gross income if the individual had been a United States citizen or resident. See Q/A–30 for the definition of base period and for examples of base amount computations.

(b) **Short or incomplete taxable years.** If the base period of a covered employee includes a short taxable year or less than all of a taxable year of the employee, compensation for the short or incomplete taxable year must be annualized before determining the average annual compensation for the base period. In annualizing compensation, the frequency with which payments are expected to be made over an annual period must be taken into account. Thus, any amount of compensation for a short or incomplete taxable year that represents a payment that will not be made more often than once per year is not annualized.

(c) **Excludable fringe benefits.** Because the base amount includes only compensation that is includible in gross income, the base amount does not include certain items that constitute parachute payments. For example, payments in the form of excludible fringe benefits or excludible health care benefits are not included in the base amount but may be treated as parachute payments.
Section 83(b) income. The base amount includes the amount of compensation included in income under section 83(b) during the base period.

Q–30: What is the base period?

A–30: (a) In general. The base period of a covered employee is the covered employee’s five most recent taxable years ending before the date on which the separation from employment occurs. However, if the covered employee was not an employee of the ATEO for this entire five-year period, the individual’s base period is the portion of the five-year period during which the covered employee performed services for the ATEO, a predecessor entity, or a related organization.

(b) Examples. The following examples illustrate the rules of Q/A–29 and this Q/A–30:

Example 1. C, a covered employee, receives an annual salary of $500,000 per year during the base period. C defers $100,000 of salary each year under a nonqualified deferred compensation plan (none of which is includible in C’s income until paid). C’s base amount is $400,000 ($400,000 x 5 / 5).

Example 2. D, a covered employee, was employed by an ATEO for two years and four months preceding the year in which D separates from employment. D’s compensation includible in gross income was $100,000 for the four–month period, $420,000 for the first full year, and $450,000 for the second full year. D’s base amount is $390,000 ((3 x $100,000) + $420,000 + $450,000) / 3).

Example 3. Assume the same facts as in Example 2, except that D also received a $60,000 signing bonus when D’s employment with the ATEO commenced at the beginning of the four-month period. D’s base amount is $410,000 ((($60,000 + (3 x $100,000)) + $420,000 + $450,000) / 3). Since the bonus is a payment that will not be paid more often than once per year, the bonus is not taken into account in annualizing D’s compensation for the four-month period.

Example 4. E, a covered employee with respect to ATEO X, was not an employee of X for the full five-year base period. In 2024 and 2025, E is a director of X and receives $30,000 per year for E’s services. On January 1, 2026, E becomes an officer and covered employee of X. E’s includible compensation for services as an officer of X is $250,000 for each of 2026 and 2027, and $300,000 for 2028. In 2028, E separates from employment. E’s base amount is $250,000 ((2 x $250,000) / 2). The $300,000
salary paid in 2028 does not affect the base amount because it was paid in the year of separation.

Q–31: How is the base amount determined in the case of a covered employee who did not perform services for the applicable tax-exempt organization (or a predecessor entity or a related organization), prior to the calendar year in which the separation from employment with the applicable tax-exempt organization occurred?

A–31: (a) In general. In that case, the covered employee’s base amount is the annualized compensation for services performed for the ATEO (or a predecessor entity or related organization) that—

(1) was includible in the employee’s gross income for that portion of the employee’s taxable year prior to the employee’s separation from employment (including amounts that were excluded under section 911), or would have been includible in the employee’s gross income if the employee had been a United States citizen or resident; and

(2) was not contingent on the separation from employment.

(b) Examples. The following examples illustrate the rules of this Q/A–31:

Example 1. On January 1, 2026, A, a covered employee, enters into a four-year employment contract with ATEO M as an officer of the organization. A did not previously perform services for M (or any predecessor entity or related organization). Under the employment contract, A is to receive an annual salary of $420,000 for each of the four years that A remains employed by M, with any remaining unpaid balance to be paid immediately in the event that A’s employment is terminated without cause. On July 1, 2026, after A has worked six months and received compensation of $210,000, A’s employment is involuntarily terminated without cause, and A receives a payment of $1,470,000. The payment of $1,470,000 is contingent on A’s separation from employment from M. In this case, A’s base amount is $420,000 (2 x $210,000). Since the present value of the payment that is contingent on A’s separation from employment with M ($1,470,000) is more than three times A’s base amount of $420,000 (3 x $420,000 = $1,260,000), the payment is a parachute payment.

Example 2. Assume the same facts as in Example 1, except that A also receives a signing bonus of $500,000 from M on January 1, 2026. The bonus is not contingent on A’s separation from employment with M. When A’s separation occurs on July 1, 2026,
A has received compensation of $710,000 (the $500,000 bonus + $210,000 in salary). A’s base amount is $940,000 ($500,000 + (2 x $210,000)). Because the $500,000 bonus will not be paid more than once per year, the amount of the bonus is not taken into account in annualizing A’s compensation. The present value of the potential parachute payment ($1,470,000) is less than three times A’s base amount of $940,000 (3 x $940,000 = $2,820,000), and therefore no portion of the payment is a parachute payment.

**H. Computation of Excess Parachute Payments**

**Q–32: How is the amount of an excess parachute payment computed?**

A–32: (a) **Calculation.** The amount of an excess parachute payment is the excess of the amount of any parachute payment made by an ATEO (or related organization or predecessor organization) over the portion of the covered employee’s base amount that is allocated to the payment. For this purpose, the portion of the base amount allocated to any parachute payment is the amount that bears the same ratio to the base amount as the present value of the parachute payment bears to the aggregate present value of all parachute payments made or to be made to (or for the benefit of) the same covered employee. Thus, the portion of the base amount allocated to any parachute payment is determined by multiplying the base amount by a fraction, the numerator of which is the present value of the parachute payment and the denominator of which is the aggregate present value of all parachute payments.

(b) **Examples.** The following examples illustrate the rules of this Q/A–32:

**Example 1.** E is a covered employee of ATEO X and an employee of related organization Y. E’s base amount is $200,000 with respect to X and $400,000 with respect to Y. E receives $1 million from X and $1 million from Y contingent upon E’s involuntary separation from employment from X and Y. For purposes of determining the excise tax under section 4960(a)(2), E has a base amount of $600,000 ($200,000 + $400,000). The two $1 million payments are parachute payments because their aggregate present value is at least three times E’s base amount (3 x $600,000 = $1.8 million). The portion of the base amount allocated to each parachute payment is $300,000 (($1 million / $2 million) x $600,000). Thus, the amount of each excess parachute payment is $700,000 ($1 million - $300,000).
Example 2. A covered employee with a base amount of $200,000 is entitled to receive two parachute payments, one of $200,000 and the other of $900,000. The $200,000 payment is made upon separation from employment, and the $900,000 payment is to be made on a date in a future taxable year. The present value of the $900,000 payment is $800,000 as of the date of the separation from employment. The portions of the base amount allocated to these payments are $40,000 (($200,000 / $1 million) x $200,000) and $160,000 (($800,000 / $1 million) x $200,000), respectively. Thus, the amount of the first excess parachute payment is $160,000 ($200,000 − $40,000) and that of the second is $740,000 ($900,000 − $160,000).

I. Reporting Liability Under Section 4960

Q–33: How do applicable tax-exempt organizations or related organizations report and pay the excise tax imposed under section 4960?

A–33: (a) In general. Taxes imposed under section 4960 are reported and paid using Form 4720, Return of Certain Excise Taxes Under Chapters 41 and 42 of the Internal Revenue Code. See also Prop. Treas. Reg. §§ 53.6011–1 and 54.6071–1, 83 F.R. 55653. In any case in which remuneration from a related organization is included to determine the excise tax imposed by section 4960, each ATEO and related organization (including a related taxable organization) must file a separate Form 4720 to report its share of liability. ATEOs and related organizations that are not liable for excise tax under section 4960 for the taxable year need not a file Form 4720 for the taxable year unless filing is required under other provisions of the Code or regulations.

(b) Examples. The following examples illustrate the rules of this Q/A–33:

Example 1. P, an ATEO, pays $250,000 of remuneration to Employee A for the taxable year for services performed as a common-law employee of P. A is a covered employee of P and is a highly-compensated employee within the meaning of section 414(q) for the taxable year. P also pays A an excess parachute payment of $550,000 for the taxable year. Q is a for-profit entity that is a related organization with respect to P. P and Q both use a calendar year taxable year. Q pays A $1 million of remuneration for the taxable year for services rendered as a common-law employee of Q, and pays no other remuneration to or parachute payment to any covered employee of P.

P and Q must report their respective liabilities for the excise tax for the taxable year on separate Forms 4720. P must report liability for the $50,000 of excess remuneration it
paid to A (($250,000 / $1.25 million) x $250,000) and the $550,000 excess parachute payment it paid to A. Even though Q has no covered employees because it is not an ATEO, Q must report liability for the $200,000 of excess remuneration it paid to A (($1 million / $1.25 million) x $250,000) as a related organization of P.

Example 2. R, an ATEO, pays $25,000 of remuneration each to five employees (the highest-compensated group) for each of the taxable year and the preceding taxable year for services performed as common-law employees of R and pays less than $10,000 of remuneration each to all other employees for each of the taxable year and the preceding taxable year. The amount described in section 414(q)(1)(A), adjusted for inflation for the taxable year, is $125,000. In addition, for the taxable year, R pays B, a member of the highest-compensated group, an $80,000 payment in the nature of compensation that was contingent on B involuntarily separating from employment and that exceeds three times B’s base amount.

R is not liable for tax under section 4960 and therefore does not need to file a Form 4720 for the taxable year (assuming R is not liable for excise tax under a provision other than section 4960). R paid no excess remuneration for the taxable year because it did not pay any employee remuneration in excess of $1 million. R paid no excess parachute payment for the taxable year, even though B received a parachute payment that was more than three times the base amount, because B (who received $105,000 of remuneration in the year of the separation from employment) is not a highly-compensated employee within the meaning of section 414(q).

Q–34: When is the excise tax imposed under section 4960 due?

A–34: (a) In general. The section 4960 excise tax must be paid and reported by filing Form 4720 by the 15th day of the 5th month after the end of the employer’s taxable year. An employer may file Form 8868, Application for Automatic Extension of Time to File an Exempt Organization Return, to request an automatic extension of time to file Form 4720. The automatic extension will be granted if Form 8868 is properly completed, and timely filed. Form 8868 does not extend the time to pay tax. To avoid interest and penalties, an employer must pay the tax due by the original due date of Form 4720.

(b) Election to prepay tax. Notwithstanding the general rule described in Q/A–2 and Q/A–34(a), an employer may prepay the excise tax under section 4960(a)(2) for the
taxable year of the separation from employment or any later taxable year before the taxable year for which the parachute payment is actually or constructively paid (see Q/A–2). (However, an employer may not prepay the excise tax on a payment to be made in cash if the present value of the payment is not reasonably ascertainable under section 3121(v)(2) and Treas. Reg. § 31.3121(v)(2)-1(e)(4) or on a payment related to health coverage.) Any prepayment must be based on the present value of the excise tax that would be due for the taxable year for which the employer will pay the excess parachute payment, and be calculated using the discount rate equal to 120 percent of the applicable Federal rate (determined under section 1274(d) and regulations thereunder; see Q/A–27) and the tax rate in effect under section 11 for the year in which the excise tax is paid. For purposes of projecting the future value of a payment that provides for interest to be credited at a variable interest rate, the employer may make a reasonable assumption regarding the variable rate. An employer is not required to adjust the excise tax paid under this Q/A–34(b) merely because the actual future interest rates are not the same as the rate used for purposes of projecting the future value of the payment.

(c) Example. The following example illustrates the rules of this Q/A–34:

Example. A covered employee with a base amount of $200,000 is entitled to receive two parachute payments, one of $200,000 and the other of $900,000. The $200,000 payment is made upon separation from employment, and the $900,000 payment is to be made on a date in a future taxable year. The present value of the $900,000 payment is $800,000 as of the date of the separation from employment. The employer elects to prepay the excise tax on the $900,000 future parachute payment (of which $740,000 is an excess parachute payment). The tax rate under section 11 is 21 percent for the taxable year the excise tax is paid and, using a discount rate determined under Q/A–27, the present value of the $155,400 ($740,000 x 21 percent) excise tax on the $740,000 future excess parachute payment is $140,000. To prepay the excise tax on the $740,000 future excess parachute payment, the employer must satisfy its $140,000 obligation under section 4960 with respect to the future payment, in addition to the
$33,600 excise tax ($160,000 x 21 percent) on the $160,000 excess parachute payment made upon separation from employment. For purposes of determining the amount of excess remuneration (if any) under Q/A–11, the amount of remuneration paid by the employer to the covered employee for the taxable year of the separation from employment is reduced by the $900,000 of total excess parachute payments ($160,000 + $740,000).

Q–35: Are applicable tax-exempt organizations or related organizations required to pay estimated taxes for the excise tax imposed under section 4960?

A–35: No. There is no requirement under section 6655 for ATEOs or related organizations to pay estimated taxes on excise taxes imposed under section 4960. Instead, the excise tax is reported and paid annually on Form 4720.

J. Miscellaneous Issues

Q–36: Does the payment of remuneration subject to excise tax under section 4960 automatically constitute an excess benefit transaction under section 4958?

A–36: No, the imposition of excise tax under section 4960 is not determinative as to whether the remuneration paid to the covered employee is excessive or unreasonable compensation for purposes of section 4958. Similarly, there is no presumption, inference, or basis for concluding that remuneration paid to a covered employee that is not subject to excise tax under section 4960 is reasonable compensation for purposes of determining liability for excise tax under section 4958.

Q–37: Does the payment of remuneration subject to excise tax under section 4960 necessarily constitute an act of self-dealing described in section 4941?

A–37: No, if the covered employee is a disqualified person described in section 4946, the imposition of excise tax under section 4960 is not determinative as to whether the remuneration paid to the covered employee is excessive or unreasonable compensation for purposes of section 4941. Similarly, there is no presumption, inference, or basis for concluding that remuneration paid to a covered employee that is not subject to excise
tax under section 4960 is reasonable compensation for purposes of determining excise
tax under section 4941.

Q–38: Does section 4960 apply to amounts to which section 162(m) applies?  
A–38: (a) In general. Remuneration paid by a publicly held corporation within the 
meaning of section 162(m)(2) to a covered employee within the meaning of section 
162(m)(3) generally is taken into account for purposes of section 4960. Similarly, 
remuneration paid by a covered health insurance provider within the meaning of section 
162(m)(6)(C) to an applicable individual within the meaning of section 162(m)(6)(F) 
generally is taken into account for purposes of section 4960. However, any amount of 
remuneration for which a deduction is not allowed by reason of section 162(m) is not 
taken into account for purposes of section 4960.

(b) Example. The following example illustrates the rules of this Q/A–38:

Example. Employee A is an officer of Corporation X. Corporation X is a related 
organization as described in Q/A–7 with respect to an ATEO. A is also a covered 
employee of the ATEO. A receives compensation of $1.5 million from X, of which 
$500,000 is nondeductible by reason of section 162(m)(1). The amount of deduction 
disallowed under section 162(m) ($500,000) is not treated as remuneration for purposes 
of section 4960. However, the remuneration paid by X that is not disallowed by reason 
of section 162(m)(1) ($1 million) is treated as remuneration for section 4960 purposes.

K. Effective Date

Q–39: What is the effective date of section 4960?  
A–39: (a) In general. Section 4960 applies to taxable years of an employer beginning 
after December 31, 2017. Remuneration paid before the beginning of the first taxable 
year that begins after December 31, 2017, is not subject to the excise tax under section 
4960.

(b) Examples. The following examples illustrate the rules of this Q/A–39:
Example 1. ATEO X uses a calendar year taxable year. ATEO Y is a related organization with respect to X and uses a taxable year beginning July 1 and ending June 30. X and Y each pay covered employee L $1.2 million of remuneration in calendar year 2018 ($2.4 million total) in equal monthly amounts.

X and Y’s liability under section 4960(a)(1) is determined by taking into account only remuneration paid during their respective taxable years beginning after December 31, 2017. X pays L a total of $1.2 million in remuneration during X’s first taxable year beginning after December 31, 2017 (January 1, 2018 through December 31, 2018). Y pays L $600,000 during the portion of the calendar year ending with or within Y’s first taxable year beginning after December 31, 2017 (July 1, 2018 through December 31, 2018), resulting in $800,000 ($1.2 million + $600,000 - $1 million) of excess remuneration paid in calendar year 2018.

Example 2. ATEO Z uses a calendar year taxable year. On January 1, 2017, Z credits $1 million of remuneration to an account under a nonqualified account balance plan on behalf of covered employee M. Under the plan, M will not vest in the amount unless M performs substantial services through December 31, 2018. On December 31, 2017, the account balance is $1.1 million. On December 31, 2018, the account balance is $1.2 million. Although M’s account balance as of December 31, 2017 was $1.1 million, the entire $1.2 million is treated as remuneration paid in calendar year 2018, because vesting did not occur until December 31, 2018. If instead the $1.1 million had vested during 2017, only the $100,000 increase in the account balance during 2018 would have been treated as remuneration paid in 2018 potentially subject to the excise tax under section 4960(a)(1).

III. REQUEST FOR COMMENTS

The Treasury Department and the IRS intend to issue proposed regulations with respect to section 4960. The Treasury Department and the IRS request comments on the topics addressed in this notice and any other issues arising under section 4960. The Treasury Department and the IRS specifically request comments regarding the following topics:

(1) Whether, for purposes of determining whether an employee is a covered employee, calculating remuneration, and calculating excess parachute payments, an employer should be permitted to rely on the employee’s written representation that the
employee did not perform services for any other employer during the calendar year ending with or within the ATEO’s taxable year (or did not perform services for one or more specified employers). If so, whether there are circumstances (for example, an employer has reason to know that the written representation was incorrect) under which an employer should not be permitted to rely on such a representation, and in what manner such a written representation must be documented in order to be relied upon.

(2) Whether, for purposes of calculating remuneration from a related organization with a change in status as a related organization during the year, there should be an alternative to calculating the actual amount paid while the employer was a related organization with respect to the ATEO and, if so, what alternative(s) should be available that would continue to provide a useful calculation with respect to both the ATEO and the related organizations without creating opportunities for abusive reallocations of remuneration among the related organizations.

(3) How remuneration based on the appreciation and depreciation of the fair market value of the stock underlying stock options and stock appreciation rights (or other similar equity rights) should be taken into account.

(4) How a related organization should treat remuneration on which it was subject to excise tax under section 4960 in a prior taxable year and for which it is denied a deduction under section 162(m) in the current taxable year.

(5) How the term “predecessor” should be defined for purposes of defining covered employees.

(6) How remuneration paid to medical service providers should be reasonably allocated between medical services and other services, including how reasonable
allocations can be made taking into account comparable salaries, time spent performing medical services and other services, and any applicable employment agreements.

All materials submitted will be available for public inspection and copying. Public comments should be submitted no later than April 2, 2019. Comments should include a reference to Notice 2019-09. Comments may be submitted electronically via the Federal eRulemaking Portal at www.regulations.gov (type IRS-2019-0001 in the search field on the regulations.gov homepage to find this notice and submit comments). Alternatively, submissions may be sent to CC:PA:LPD:PR (Notice 2019-09), Room 5203, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions also may be hand delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (Notice 2019-09), Courier’s Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC 20044. All recommendations for guidance submitted by the public in response to this notice will be available for public inspection and copying in their entirety.

IV. RELIANCE

The Treasury Department and the IRS intend to issue further guidance regarding section 4960 in the form of proposed regulations. Until further guidance is issued, taxpayers may rely on the rules in this notice for purposes of section 4960 effective from December 22, 2017 (the date of enactment). Further guidance will be prospective and will not apply to taxable years beginning before the issuance of such guidance.
V. PAPERWORK REDUCTION ACT

The collection of information in this notice is the requirement under section 4960 that an ATEO determine and keep records of its covered employees, related organizations, and excess remuneration and excess parachute payments paid to covered employees by the ATEO and related organizations, disclose this information to each related organization, and that each ATEO and related organization report excise tax liability to the IRS. The collection of information contained in this notice is reflected in the collection of information for Form 4720 that has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. 3507(c)) under control number 1545-0052.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid OMB control number.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by § 6103.

VI. DRAFTING INFORMATION

The principal authors of this notice are William McNally and Chelsea Rubin of the Office of Associate Chief Counsel (Tax Exempt and Government Entities). For Executive Compensation questions, contact Mr. McNally at (202) 317-5600 (not a toll-free number). For Exempt Organizations questions, contact Ms. Rubin at (202) 317-5800 (not a toll-free number).
Supplement 5

ABA Tax Section Comments on Notice 2019-9
Submitted on July 12, 2019
Re: Comments on Section 4960, Notice 2019-9 and Volunteers Providing Services to Tax-Exempt Organizations

Dear Commissioner Rettig:

Enclosed please find comments in response to the request in Notice 2019-9 with respect to section 4960 of the Internal Revenue Code, specifically focusing on examples of volunteers providing services to tax-exempt organizations. These comments are submitted on behalf of the Section of Taxation and have not been approved by the House of Delegates or the Board of Governors of the American Bar Association. Accordingly, they should not be construed as representing the position of the American Bar Association.

The Section of Taxation would be pleased to discuss these comments with you or your staff.

Sincerely,

Eric Solomon
Chair, Section of Taxation

Enclosure

cc: Hon. David Kautter, Assistant Secretary (Tax Policy), Department of the Treasury
Krishna P. Vallabhaneni, Tax Legislative Counsel, Department of the Treasury
Carol Weiser, Benefits Tax Counsel, Department of the Treasury
Elinor Ramey, Attorney Advisor, Department of the Treasury
Amber Salotto, Attorney Advisor, Department of the Treasury
Hon. Michael Desmond, Chief Counsel, Internal Revenue Service
William M. Paul, Deputy Chief Counsel (Technical), Internal Revenue Service
Victoria A. Judson, Associate Chief Counsel, Employee Benefits, Exempt Organizations and Employment Taxes, Internal Revenue Service
Janine Cook, Deputy Associate Chief Counsel, Employee Benefits, Exempt Organizations and Employment Taxes, Internal Revenue Service
Stephen B. Tackney, Deputy Associate Chief Counsel, Employee Benefits, Exempt Organizations and Employment Taxes, Internal Revenue Service
William L. McNally, Attorney, Employee Benefits, Exempt Organizations and Employment Taxes, Internal Revenue Service
ABSTRACT OF TAXATION
COMMENTS ON SECTION 4960, NOTICE 2019-9
AND VOLUNTEERS PROVIDING SERVICES
TO TAX-EXEMPT ORGANIZATIONS

These comments (“Comments”) are submitted on behalf of the American Bar Association Section of Taxation (the “Section of Taxation”) and have not been approved by the House of Delegates or Board of Governors of the American Bar Association. Accordingly, they should not be construed as representing the position of the American Bar Association.

Principal responsibility for preparing these Comments was exercised by Gil J. Ghatan, Catherine E. Livingston, Alexander L. Reid, David A. Shevlin, and Maura L. Whelan of the Exempt Organizations Committee, and Kurt L. Lawson and Helen H. Morrison of the Employee Benefits Committee of the Section of Taxation. The Comments were reviewed by Morey Ward, Chair of the Exempt Organizations Committee, and Martha N. Steinman, Chair of the Employee Benefits Committee. The Comments were further reviewed by Ellen P. Aprill of the Section’s Committee on Government Submissions, and by Melissa Wiley, Council Director for the Exempt Organizations Committee.

Although the members of the Section of Taxation who participated in preparing these Comments have clients who might be affected by the federal income tax principles addressed by these Comments, no such member or the firm or organization to which such member belongs has been engaged by a client to make a government submission with respect to, or otherwise to influence the development or outcome of, the specific subject matter of these Comments.

Contact: Carolyn O. (Morey) Ward
(202) 508-4645
Morey.ward@ropesgray.com

Martha N. Steinman
(212) 918-5580
Martha.steinman@hoganlovells.com

Date: July 12, 2019
EXECUTIVE SUMMARY

These comments (“Comments”) are submitted in response to a request in Notice 2019-9\(^1\) (the “Notice”) by the Department of the Treasury (“Treasury”) and the Internal Revenue Service (the “Service”) for comments on topics addressed in the Notice and on any other issues arising under section 4960,\(^2\) as added to the Internal Revenue Code by Public Law Number 115-97 (the “Act”). These Comments are not intended to provide technical analysis of the topics addressed in the Notice. Rather, these Comments respond to public requests made by representatives of Treasury and the Service for fact patterns involving exempt organizations potentially affected by section 4960 that could inform their analysis of the section. We anticipate that the Section of Taxation will provide more extensive analysis in response to proposed regulations issued under section 4960.

We thank Treasury and the Service for the time and attention that has already gone into implementing section 4960. The Notice provides a significant amount of information about the operation of the statute and the interpretative issues that Treasury and the Service expect to address in regulations. The Notice has also been helpful in prompting further thought about the reach of section 4960 and its potential to create tax liability for for-profit taxable companies.

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\(^2\) References to a “section” are to a section of the Internal Revenue Code of 1986, as amended (the “Code” or “I.R.C.”), unless otherwise indicated.
DISCUSSION

The examples provided below are intended to illustrate some of the ways in which an employee of a taxable entity may volunteer or otherwise perform services for a tax-exempt organization without any additional remuneration. This scenario is a common one, with many variations that extend beyond volunteer service as a board member or corporate officer of an affiliated tax-exempt organization. We note that, while all of the examples provided in these Comments involve private foundations, we expect that there will be situations that involve public charities as well.

Three of the four examples involve company foundations or family foundations. Company foundations are private foundations that are created and typically largely funded by for-profit corporations or other taxable companies. Companies establish foundations (and direct giving programs) to have a positive impact on society. Company foundations tend to make grants in fields related to the companies’ business activities or in communities where they operate, or where their employees live. Modern corporate law treats charitable donations as appropriate uses of corporate assets as long as the amounts in question are reasonable and serve a plausible business purpose. There were about 2,500 company foundations in the United States, responsible for about $5.5 billion in giving, in 2015. About 40 percent of U.S. corporations are estimated to have company foundations.

Typically, family foundations are private foundations that are created and largely funded by endowments from a family. They might receive services from family offices, if one exists, and the family office, in turn might oversee family-owned businesses. There were about 42,000 family foundations in the United States, responsible for about $28.5 billion in giving, in 2015.

Companies often ask or direct their employees to provide volunteer services to company foundations, and family offices and family-owned businesses often ask their employees to provide volunteer services to family foundations, in both cases in order to foster the mission of the foundations. These arrangements are not undertaken to avoid any income or employment tax, and most especially not to avoid section 4960, which did not exist in the decades when these arrangements became a common practice. Usually, the services are provided on a volunteer or other uncompensated basis (1) to avoid any concern that the payment of remuneration could be an act of self-dealing under section 4941, where the company, family office or family-owned

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business is a “disqualified person” of the foundation within the meaning of section 4946,7 and (2) to allow all of the foundation’s resources to be used for charitable grants and programs, instead of for operational expenses. In some instances, the services rendered to the charitable organization might be considered “minimal,” but in other cases, the services make a meaningful contribution to the operation of the charitable organization. Indeed, that is the point – to give resources to the charitable organization so it can serve others in need.

The fourth example involves an independent foundation that could be treated as controlled by a corporation solely because the two directors, who are also the only officers, of the foundation both work for that corporation. There were about 79,500 independent foundations in the United States, responsible for about $44 billion in giving, in 2015.8

Example 1: Company A Foundation – Donated Services

Company A is a large privately held corporation. It established Company A Foundation, which has been recognized as exempt from federal income taxation under section 501(c)(3) and classified as a private foundation within the meaning of section 509(a). Company A Foundation has a self-perpetuating board of directors. Each member of the board of directors of Company A Foundation is an employee of Company A.

Company A Foundation does not have its own personnel. Instead, Company A donates the services of certain Company A employees to Company A Foundation, as needed from time to time. Certain of the Company A employees whose services are donated to Company A Foundation devote substantially all of their business time to Company A Foundation matters. Others, including members of Company A’s accounting, finance, and legal departments, allocate only a portion of their business time to Company A Foundation. Further, the specific Company A employees who devote business time to Company A Foundation matters change over time, based upon the needs of Company A Foundation and the needs of Company A. In addition, to enhance morale, Company A allows long-tenured Company A employees with relevant expertise to apply to work exclusively with Company A Foundation for six-month rotational positions, during which time Company continues to pay them their regular remuneration, and they receive no additional remuneration from Company A Foundation.

Company A is a disqualified person of Company A Foundation within the meaning of section 4946. Although Company A Foundation could pay reasonable compensation to Company A for personal services in compliance with the self-dealing rules section 4941, Company A previously determined to bear the costs of the services performed by Company. As a result, Company A Foundation does not reimburse or otherwise make any payments to

7 A private foundation may pay compensation to a disqualified person if the services are “reasonable and necessary to carrying out the foundation’s exempt purposes” and the amount is not “excessive” within the meaning of section 162, see I.R.C. § 4941(d)(2)(E); Reg. § 53.4941(d)-3(c), but it is not always possible to be sure that these requirements are met.

Company A for any of the services provided to Company A Foundation by Company A employees.

Certain of the Company A employees whose services are donated to Company A Foundation from time to time are paid more than $1 million in remuneration by Company A, or may be expected to receive such pay in the future. Also, Company A might involuntarily terminate certain of those employees, for example because of a downsizing, or might be expected to do so in the future, and give them separation pay.

**Example 2: Company B Foundation – Volunteer Officers**

Company B is a large privately held corporation. It established Company B Foundation, which has been recognized as exempt from federal income taxation under section 501(c)(3) and classified as a private foundation within the meaning of section 509(a). Company B serves as the sole corporate member of Company B Foundation for purposes of applicable state law. In its capacity as sole corporate member, Company B appoints, and has the power to remove, the members of the board of directors of Company B Foundation, which in turn elects the officers of Company B Foundation.

The Company B Foundation by-laws provide that Company B Foundation will have the following corporate officers: President, Secretary, and Treasurer. The by-laws ascribe customary duties to each office. All of the appointed members of the board of directors and elected officers of Company B Foundation are employees of Company B. The by-laws further provide that none of the Company B Foundation directors or officers will be compensated by Company B Foundation for their services as directors or officers.

As of January 1, 2017, the Chief Executive Officer (“CEO”) of Company B also served as President of Company B Foundation; the General Counsel of Company B also served as Secretary of Company B Foundation; and the Chief Financial Officer (“CFO”) of Company B also served as Treasurer of Company B Foundation. Each served as an officer of Company B Foundation on a voluntary basis. In addition, Company B Foundation has five employees: an Executive Director, three Grants Managers, and a Bookkeeper.

In 2018, Company B paid $10 million in remuneration to the CEO for her services as CEO, $3 million in remuneration to the General Counsel for his services as General Counsel, and $7 million in remuneration to the CFO for her services as CFO. Company B does not require any of them to serve as an officer of Company B Foundation as a condition of employment, and no portion of his or her remuneration from Company B is related in any manner to his or her service as an officer of Company B Foundation. Company B Foundation does not make any payments to Company B for the services of the President, Secretary, or Treasurer. Consistent with the Company B Foundation by-laws, none of the President, Secretary, or Treasurer is compensated by Company B Foundation for his or her services to Company B Foundation.

In 2018, the Company B Foundation paid $300,000 in remuneration to the Executive Director, $200,000 in remuneration to one of the Grants Managers, $150,000 each in remuneration to the two remaining Grants Managers, and $100,000 in remuneration to the Bookkeeper.
Example 3: Family C Foundation – Volunteer Officers

Company C is a privately held corporation, established by Founder, who serves as CEO of, and owns a controlling interest in, Company C. Founder also established Family C Foundation, which has been recognized as exempt from federal income taxation under section 501(c)(3) and classified as a private foundation within the meaning of section 509(a). Founder serves as the sole member of Family C Foundation. Family C Foundation has a calendar year taxable year. Company C and Family C Foundation are operated entirely independently of each other. In his capacity as sole member of Family C Foundation, Founder appoints, and has the power to remove, the members of the board of directors of Family C Foundation. The appointed members of the board of directors of Family C Foundation are Founder, Founder’s wife, Founder’s son, and Founder’s daughter.

The Family C Foundation by-laws provide that Family C Foundation will have the following corporate officers: President, Secretary, and Treasurer. The by-laws ascribe customary duties to each office. The by-laws further provide that Family C Foundation officers will not be compensated for their services to Family C Foundation. Family C Foundation does not have any other personnel. Family C Foundation makes two to three large grant payments annually to local public charities, and as a result, has modest administrative needs. Grant payments and other administrative matters are discharged by the officers of Family C Foundation, as well as the personal accountant of Founder’s wife, without charge to Family C Foundation.

As of January 1, 2017, Founder’s wife served as President of Family C Foundation, Founder’s son served as Secretary of Family C Foundation, and Founder’s daughter served as Treasurer of Family C Foundation. At that time, none of Founder’s wife, Founder’s son, or Founder’s daughter had any role with Company C.

Founder’s daughter resigned as Treasurer of Family C Foundation as of January 30, 2017. On June 30, 2018, Founder’s daughter joined Company C as Chief Information Officer (“CIO”). In 2018, Company C paid Founder’s daughter $2.5 million in remuneration for her services as CIO.

Founder remains the controlling shareholder of Company C. Founder also remains the sole member of Family C Foundation. Founder’s wife continues to serve as President of Family C Foundation. Founder’s son serves as both Secretary and Treasurer of Family C Foundation. Founder’s daughter has no ongoing role with Family C Foundation.

Example 4: Unrelated Foundation

Company D is a large privately held corporation. Two senior executives of Company D, Employee X and Employee Y, establish Unrelated Foundation, which has been recognized as exempt from federal income taxation under section 501(c)(3) and classified as a private foundation within the meaning of section 509(a).

Other than through establishment by Employee X and Employee Y, Unrelated Foundation has no connection with Company D. Employee X and Employee Y are the sole
members of the board of directors of Unrelated Foundation, and serve as the sole officers of Unrelated Foundation. There are no other employees of Unrelated Foundation.

In 2018, Company D paid Employee X $2 million in remuneration, and Employee Y $3 million in remuneration, for their services as employees of Company D. Unrelated Foundation did not pay any remuneration to either Employee X or Employee Y.

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We hope that these examples are valuable in analyzing the statute further and developing proposed regulations.
Supplement 6

Ropes & Gray LLP Alert on Notice 2019-9
January 7, 2019

**IRS Issues Guidance on Executive Compensation Excise Tax for Tax-Exempt Organizations**

In Notice 2019-09, issued December 31, 2018 (the “Notice”), Treasury and the IRS have provided interim guidance on the excise tax on certain executive compensation arrangements under section 4960 of the Internal Revenue Code. This new provision was enacted as part of the Tax Cuts and Jobs Act at the end of 2017. The Notice, which spans more than ninety pages, is primarily structured in a question and answer format and clarifies many ambiguities in section 4960. The Notice requests comments by April 2, 2019.

Treasury and the IRS intend to issue proposed regulations, but any future regulations will be prospective and will not apply to taxable years beginning before they are issued. Until further guidance is issued, employers may base their positions with respect to the excise tax on a good faith, reasonable interpretation of section 4960. Positions reflected in the Notice constitute a good faith, reasonable interpretation of section 4960.

**Summary of Section 4960**

Section 4960 imposes an excise tax equal to the corporate tax rate (currently, 21 percent) on certain tax-exempt organizations (“applicable tax-exempt organizations” or “ATEOs”) and related organizations that pay excess compensation to employees of the ATEO. The excise tax generally applies if, during the taxable year, the ATEO pays remuneration in excess of $1 million or any “excess parachute payment” to any of the ATEO’s employees who are among the five highest paid for the current year and any prior taxable year beginning after December 31, 2016 (“covered employees”). Compensation paid by any related organization to an ATEO employee is taken into account in determining whether such employee is a covered employee and in determining total compensation subject to the excise tax.

**General Clarifications**

The Notice answers certain key questions regarding how to interpret section 4960, including the following:

- **Taxable year**: The statute was ambiguous as to whether the relevant taxable year for measuring remuneration and excess parachute payments, and for purposes of determining who are an ATEO’s covered employees, should be that of the covered employee or the ATEO. The Notice clarifies that the period for measuring remuneration paid and parachute payments is the calendar year that ends with or within the taxable year of the employer. This approach should be familiar to all ATEOs that already file the annual IRS Form 990, as this is generally the same method used for reporting compensation on that form.

- **Effective date**: Section 4960 is effective for an ATEO’s first taxable year beginning after December 31, 2017. The Notice clarifies that remuneration that (1) was paid or (2) is treated as having been paid because it vested, in each case prior to the effective date of section 4960, is not subject to section 4960.

- **Government entities**: The Notice indicates that certain government entities are not ATEOs. Specifically, government entities that are not recognized as tax exempt under section 501(a) and those that do not exclude income under section 115(1) are not ATEOs. This means that certain state colleges and universities may not be ATEOs subject to section 4960. This interpretation of the statutory language of section 4960 is inconsistent with the statute’s legislative history, which indicates that section 4960 was intended to cover highly paid employees at public universities. Even if it is not considered an ATEO, a government entity, including a state college or university, could be a related organization of an ATEO and, as a result, become subject to the tax (see below).

- **Related organizations – control**: The excise tax is triggered by compensation paid not only by the ATEO but also by any related organization, which is defined as a person or government entity that (1) controls or is controlled
by the ATEO, (2) is controlled by one or more persons that control the ATEO, (3) is a supported or supporting organization of the ATEO, or (4) in the case of a voluntary employees’ beneficiary association (VEBA), that establishes, maintains or makes contributions to the VEBA. In establishing a definition of control for these purposes, the Notice applies the greater than 50 percent control threshold from the unrelated business income tax rules for payments from controlled entities, which also generally reflects the definition of related organization for IRS Form 990 reporting purposes.

- Related organizations – for-profit and government entities: The Notice makes clear that for-profit and government entities can be considered related organizations, meaning that compensation paid by these entities to an ATEO employee must be considered in determining whether such employee is a covered employee and whether such employee receives excess remuneration or an excess parachute payment. The Notice further clarifies that for-profit and government entities (as well as any other related organizations) are liable for their proportionate share of any resulting excise tax based on the portion of the employee’s total compensation paid by each related organization.

- Covered employee: Only an ATEO has covered employees, and the Notice clarifies that only common law employees (including officers) can be covered employees. An employee need not be paid excess remuneration or an excess parachute payment during a taxable year to be treated as a covered employee. The Notice makes clear that once an ATEO employee is a covered employee, he or she will always be a covered employee of such ATEO, with no expiration date. This means that ATEOs will need to keep track of their covered employees at all times, regardless of whether those covered employees are paid excess remuneration or excess parachute payments in a given year, as the excise tax could be triggered if the covered employee receives excess remuneration or an excess parachute payment in any future year. Over time, this may become increasingly likely, as the $1 million threshold for excess remuneration is not indexed for inflation.

- Limited services exception: The Notice provides an exception that excludes from the group of covered employees certain employees of an ATEO and related organizations, if the ATEO pays only a small portion of the total remuneration paid to the employee. Under this exception, an ATEO employee is not treated as one of the ATEO’s five highest-compensated employees unless the ATEO pays at least 10 percent of the total remuneration paid by the ATEO and all related organizations to the employee during the year. However, if no ATEO pays at least 10 percent of an employee’s total remuneration during the year, this exception does not apply to the ATEO that paid the most remuneration to the employee during the year.

- Medical services exception: Remuneration paid to a licensed medical professional (including a veterinarian) for the performance of medical or veterinary services by such professional is disregarded for purposes of determining whether excess remuneration or excess parachute payments have been paid. The Notice clarifies that such remuneration is also excluded when determining which ATEO employees are its five highest-compensated and therefore covered employees. The Notice indicates that administrative, teaching, and research services generally are not considered medical services for purposes of the exception and provides rules for allocating time spent by medical professionals between medical and non-medical services. The employer must make a reasonable, good faith allocation of such services, and if any remuneration allocation is set forth in an employment agreement or similar written arrangement, such allocation must be used to the extent the amount allocated to medical services is not unreasonable.
Remuneration in Excess of $1 Million

- **Scope**: The Notice provides guidance on what constitutes remuneration for purposes of section 4960 and makes clear that remuneration is not limited to amounts reported on IRS Form W-2 in boxes 1 or 5.

- **Timing**: Remuneration is treated as paid when it is no longer subject to a substantial risk of forfeiture (i.e., when it vests), using the definition in proposed Treasury Regulations under section 457(f) for this purpose, regardless of whether the arrangement under which the amount is or will be paid is subject to section 457(f) or section 409A. Under this definition, compensation is subject to a substantial risk of forfeiture only if it is conditioned on the performance of substantial future services or if it is conditioned upon the occurrence of a condition related to a purpose of the compensation and the possibility of forfeiture is substantial.

- **Amount**: The amount of remuneration treated as paid when such remuneration ceases to be subject to substantial risk of forfeiture is the present value of such remuneration, determined using reasonable actuarial assumptions. Subsequent earnings on such amounts are treated as paid at the end of the calendar year in which they accrue.

**Excess Parachute Payments**

- The excise tax is imposed on excess parachute payments, which is defined as any payment in the nature of compensation made by an ATEO or a related organization to a covered employee if (1) the payment is contingent on the employee’s separation from employment with the employer and (2) the aggregate present value of the parachute payments equals or exceeds an amount equal to three times the “base amount” (generally, an employee’s average annual compensation over the most recent five-year period). The Notice emphasizes that an excess parachute payment equals the excess of the parachute payment over the base amount (i.e., not only on the portion of the payment in excess of three times the base amount).

- The Notice provides guidance on what constitutes a payment in the nature of compensation, when the payment is considered to be made, when it is contingent upon an employee’s separation from employment, and what constitutes a separation from employment, as well as rules on how to calculate the base amount and excess parachute payments that are modeled on, but differ in some respects from, the rules under section 280G. In particular, the Notice indicates that a payment is contingent on separation from employment under section 4960 only if the separation is involuntary. The Notice also clarifies that parachute payments include unvested deferred compensation that is accelerated as a result of the involuntary separation.

- The preamble to the Notice provides helpful step-by-step instructions for how to determine whether any excise tax is due as a result of making a payment contingent on separation from employment.

**Payment and Reporting**

- The Notice provides that employers must report their excise tax liability on IRS Form 4720 and makes clear that each employer liable for tax is responsible for separately reporting and paying its share of the tax. The Notice further clarifies that no quarterly estimated payments are required with respect to the tax.

If you have any questions about the Notice, please contact a member of the tax-exempt organizations practice.
Supplement 7

Department of Treasury and Internal Revenue Service
2019-2020 Priority Guidance Plan
We are pleased to announce the release of the 2019–2020 Priority Guidance Plan. As described below, the 2019-2020 Priority Guidance Plan sets forth guidance priorities for the Department of the Treasury (Treasury) and the Internal Revenue Service (IRS). This plan continues to prioritize implementation of the Tax Cuts and Jobs Act, Pub. L. 115-97, 131 Stat. 2054, enacted on December 22, 2017, and is based on public input from solicited comments as well as Treasury and IRS’s continued engagement with taxpayers since the enactment of tax reform. This plan also prioritizes implementation of the Taxpayer First Act, Pub. L. 116-25, 133 Stat. 981, enacted on July 1, 2019. In addition, the 2019–2020 Priority Guidance Plan continues to reflect the deregulatory policies and reforms described in Section 1 of Executive Order 13789 (April 21, 2017; 82 FR 19317) and Executive Order 13777 (February 24, 2017; 82 FR 12285).

The 2019-2020 Priority Guidance Plan contains guidance projects that will be the focus of efforts during the twelve-month period from July 1, 2019, through June 30, 2020 (the plan year). The 2019-2020 Priority Guidance Plan contains 203 guidance projects. As of September 30, 2019, 31 guidance items have been released. In addition to the projects on the 2019-2020 plan, the Appendix lists routine or ministerial guidance that is generally published each year.

We may further update the 2019-2020 plan during the plan year to reflect additional items that have become priorities and guidance that we have published during the plan year. The periodic updates allow us flexibility to consider comments received from taxpayers and tax practitioners relating to additional guidance priorities and to respond to developments arising during the plan year.
The published guidance process can be fully successful only if we have the benefit of the insight and experience of taxpayers and practitioners who must apply the internal revenue laws. Therefore, we invite the public to continue to provide us with their comments and suggestions as we develop guidance throughout the plan year.

OFFICE OF TAX POLICY
AND
INTERNAL REVENUE SERVICE

2019-2020 PRIORITY GUIDANCE PLAN
Publication Information Released or Published Through September 30, 2019

PART 1. IMPLEMENTATION OF TAX CUTS AND JOBS ACT (TCJA)

1. Regulations under §§36B and 6011 given the enactment of §151(d)(5).

2. Regulations and other guidance under §42 regarding the low-income housing credit average income test.

3. Regulations to address the amendments to §47, the rehabilitation credit.

4. Final regulations and other guidance under §59A concerning the base-erosion and anti-abuse tax. Proposed regulations were published on December 21, 2018.

5. Regulations to set maximum vehicle values under §1.61-21(d) and (e), to reflect amendments made to §280F by sections 11002 and 13202 of the TCJA.

   • PUBLISHED 08/23/19 in FR as REG-101378-19 (NPRM).

6. Regulations clarifying the deductibility of certain expenses described in §67(b) and (e) that are incurred by estates and non-grantor trusts. Notice 2018-61 was published on July 30, 2018.


8. Guidance under §152(d) concerning the definition of “qualifying relative.”

9. Regulations under §162(m), as amended by section 13601 of the TCJA.

10. Regulations under amended §162(f) and §6050X.

11. Regulations under §§162, 164 and 170.

13. Guidance on applying the state and local deduction cap under §164.

14. Guidance under §§168(f)(2) and (i)(9) addressing excess deferred income taxes and public utility companies. Notice 2019-33 was published on May 28, 2019.

15. Final regulations and other guidance under §168(k). Proposed regulations were published on August 8, 2018.
   - PUBLISHED 08/19/19 in IRB 2019-34 as REV. PROC. 2019-33 (RELEASED 07/31/19).
   - PUBLISHED 09/24/19 in FR as TD 9874
   - PUBLISHED 09/24/19 in FR as REG-106808-19 (NPRM)

16. Regulations under §172 for computing the net operating loss deduction to reflect changes made by TCJA.


19. Final regulations and other guidance concerning the participation exemption system for the taxation of foreign source income under §§245A, 1248(j) and (k), and 91. Temporary and proposed regulations were published on June 18, 2019.

20. Final regulations and other guidance under §250 regarding the deduction for foreign derived intangible income and global intangible low-taxed income. Proposed regulations were published on March 6, 2019.

21. Regulations and other guidance under §§263A, 448, 460, and 471 to reflect TCJA changes affecting small businesses.

22. Final regulations and other guidance under §267A addressing certain related-party amounts paid or accrued in hybrid transactions or by or to hybrid entities. Proposed regulations were published on December 28, 2018.

23. Regulations under §274 concerning meal expenses.
24. Regulations under §274 concerning qualified transportation fringes, including the application of § 512(a)(7), and other issues under §274.

25. Regulations under §§367 and 482, including regulations addressing the changes to §§367(d) and 482 under the TCJA. Temporary and proposed regulations were published on September 16, 2015.

26. Guidance under §382(h)(6) in response to TCJA.
   - PUBLISHED 09/10/19 in FR as REG-125710-18 (NPRM).

27. Regulations relating to Qualified Plan Loan Offset Amounts under §402(c)(3)(C), as added by section 13613 of the TCJA.

28. Regulations and other guidance under §451(b) and (c).
   - PUBLISHED 07/15/19 in FR as TD 9870 (§1.451-5 Removal).
   - PUBLISHED 09/09/19 in FR as REG-104870-18 (451(b) NPRM).
   - PUBLISHED 09/09/19 in FR as REG-104554-18 (451(c) NPRM).

29. Regulations on computation of unrelated business taxable income for separate trades or businesses under §512(a)(6), as added by section 13702 of the TCJA.

30. Regulations on the increased contribution limit under §529A as amended by section 11024 of the TCJA, and final regulations under §529A on Qualified ABLE Programs, as added by section 102 of the ABLE Act of 2014. Proposed regulations were published on June 22, 2015.

31. Regulations under §704(d) regarding charitable contributions and foreign taxes in determining limitation on allowance of partner’s share of loss.

32. Guidance under §807 regarding the determination of life insurance reserves for life insurance and annuity contracts, including guidance to implement changes under section 13517 of the TCJA.
   - PUBLISHED 08/26/19 in IRB 2019-35 as REV. PROC. 2019-34 (RELEASED 08/06/19).
33. Revenue procedure providing guidance for an insurance company to obtain automatic consent to change its method of accounting to comply with §846, as amended by section 13523 of the TCJA.
   - PUBLISHED 08/12/19 in IRB 2019-33 as REV. PROC. 2019-30 (RELEASED 07/22/19).

34. Regulations under §§863(b) and 865(e)(2) regarding the source of sales of personal property.

35. Final regulations under §§864(c)(8) and 1446(f) on the treatment of gain or loss of foreign persons from the sale or exchange of an interest in a partnership that is engaged in a trade or business within the United States. Proposed regulations under §864(c)(8) were published on December 27, 2018. Proposed regulations under §1446(f) were published on May 13, 2019.

36. Final regulations and other guidance on certain foreign tax credit issues arising under the TCJA under §§901 and 960, and related provisions, including §§78, 861, 904, and 905. Proposed regulations were published on December 7, 2018.

37. Final regulations and other guidance under §951A regarding the inclusion of global intangible low-taxed income by United States shareholders. Proposed regulations were published on June 21, 2019.

38. Regulations and other guidance addressing modifications to subpart F, including coordination with the enactment of §951A, the repeal of §958(b)(4) and the modification of § 951(b). Proposed regulations were published on June 21, 2019.


40. Guidance under §1031 concerning the definition of “real property.”

41. Regulations addressing partnership interests held in connection with the performance of services under §1061.
42. Regulations under §§1295, 1297, and 1298, including regulations addressing when foreign insurance income is excluded from passive income under §1297(f).

- PUBLISHED 07/11/19 in FR as REG-105474-18 (NPRM).

43. Guidance under §1371(f) on the treatment of earnings and profits in the after post-termination transition period when an entity converts from an S corporation to a C corporation.

44. Guidance under §§1400Z–1 and 1400Z–2 concerning Opportunity Zones. Proposed regulations were published on October 29, 2018 and May 1, 2019.

45. Regulations under §1502 and §1.1502-21(b) and §1.1502-47 regarding absorption of consolidated net operating losses and consolidated group computations under multiple TCJA provisions.

46. Final regulations under §2010 addressing the computation of the estate tax in the event of a difference between the basic exclusion amount applicable to gifts and that applicable at the donor’s date of death. Proposed regulations were published on November 23, 2018.

47. Regulations and other guidance regarding withholding under §§3402 and 3405 as a result of the amendments made by sections 11001 and 11041 of the TCJA.

48. Regulations on aircraft management services under §4261.

49. Regulations under §4960, as added by section 13602 of the TCJA.

50. Final regulations on the excise tax on net investment income of certain private colleges and universities under §4968, as added by section 13701 of the TCJA. Proposed regulations were published on July 3, 2019.

51. Revenue procedure to update the standard mileage rate procedures to reflect changes made by TCJA.

52. Revenue procedure to update the per diem procedures in Rev. Proc. 2011-47 to reflect changes made by TCJA.
PART 2. E.O. 13789 - IDENTIFYING AND REDUCING REGULATORY BURDENS

1. Delay and proposed removal of documentation regulations under §385 and review of other regulations under §385. Final, temporary, and proposed regulations were published on October 21, 2016. Proposed regulations were published on September 24, 2018.

2. Final regulations removing temporary regulations under §707 concerning the treatment of partnership liabilities for disguised sale purposes. Temporary and proposed regulations were published on October 5, 2016. Proposed regulations were published on June 19, 2018.

3. Proposed modification of regulations under §987 on income and currency gain or loss with respect to a §987 qualified business unit. Final regulations were published on December 8, 2016. Notice 2017-57 (regarding the applicability dates of the final regulations) was published on October 16, 2017. Notice 2018-57 (providing additional guidance regarding the applicability date of the final regulations) was published on June 25, 2018.

4. Proposed regulations under §7602 to implement the Taxpayer First Act regarding summons interviews and sharing of summoned information with person authorized under §6103(n).

PART 3. BURDEN REDUCTION

1. Regulations under §42 relating to compliance monitoring. Final regulations were published on February 26, 2019.

2. Regulations under §86 regarding rules for lump-sum elections.

3. Regulations updating the classification system for the line of business determination under §1.132-4 for purposes of qualified employee discounts and no-additional-cost services.

4. Final regulations on bond reissuance under §150. Proposed regulations were published on December 31, 2018.

5. Guidance under §170(e)(3) regarding charitable contributions of inventory.


7. Guidance concerning the effect of momentary ownership of the stock of an S corporation by another corporation during a transaction described in §§355 and 368(A)(1)(D).
8. Final regulations on the application of the normal retirement age regulations under §401(a) to governmental plans. Proposed regulations were published on January 27, 2016.

9. Final regulations streamlining the §754 election statement. Proposed regulations were published on October 12, 2017.

10. Guidance regarding application of the cure provisions under §851(i) for regulated investment companies (RICs) and §856(c)(7) and (g)(5) for real estate investment trusts (REITs).

11. Regulations under §871(m), including with respect to non-delta-one transactions. Final and temporary regulations were issued January 24, 2017. Notice 2018-72 (delaying the applicability date of portions of the final regulations) was published on October 1, 2018.

12. Guidance under §954, including regarding the use of foreign statement reserves for purposes of measuring qualified insurance income under §954(i).

13. Final regulations under §§1014(f) and 6035 regarding basis consistency between estate and person acquiring property from decedent. Proposed and temporary regulations were published on March 4, 2016.

14. Guidance under §1362(f) regarding the validity or continuation of an S corporation election in certain situations involving disproportionate distributions, inconsistent tax return filings, or omissions on Form 2553, Election by a Small Business Corporation.

15. Final regulations under Chapter 3 (§§1441–1446) and Chapter 4 (§§1471–1474), including rules addressing withholding on gross proceeds and foreign passthrough payments under Chapter 4; withholding requirements on insurance premiums under Chapter 4; and certain due diligence requirements of withholding agents under Chapter 3, including issues related to refunds and credits. Proposed regulations were published on December 18, 2018.

16. Regulations under §1502 removing obsolete rules and updating regulations to reflect statutory changes.

17. Final regulations under §2642(g) describing the circumstances and procedures under which an extension of time will be granted to allocate GST exemption.

18. Final Regulations under §3405 regarding distributions made to payees, including military and diplomatic payees, with an address outside the United States. Proposed regulations were published on May 31, 2019.
19. Final regulations under §§4051 and 4071 on heavy trucks, tractors, trailers, and tires. Proposed regulations were published on March 31, 2016.

20. Guidance under §301.9100 regarding relief for late regulatory elections.


23. Notice providing relief on compliance for low-income housing projects affected in the 2018 California Wildfires Major Disaster.

24. Regulations under subchapter S to conform with statutory changes and provide further guidance on the calculation of certain items of income, loss, and deduction.

25. Regulations on check the box rules for REITs and RICs.

**PART 4. TAXPAYER FIRST ACT GUIDANCE**


2. Regulations under §6011 as amended by the Taxpayer First Act.

3. Regulations under §6311 as amended by the Taxpayer First Act regarding payment of taxes by debit and credit cards.

4. Regulations under §6402(n) as enacted by the Taxpayer First Act related to misdirected tax refund deposits.

5. Regulations regarding the Independent Office of Appeals established under the Taxpayer First Act.


PART 5. BIPARTISAN BUDGET ACT OF 2015 - PARTNERSHIP AUDIT REGULATIONS

1. Regulations under §6232(f).

2. Regulations under §6241.

3. Extension of the time to file partnership return.

4. Final regulations addressing adjustments to bases and capital accounts and the tax and book basis of partnership property. Proposed regulations were published on February 2, 2018. (Reproposed on August 17, 2018, in combination with proposed regulations addressing revisions to chapter 63 made by the Tax Technical Corrections Act of 2018.)

PART 6. GENERAL GUIDANCE

CONSOLIDATED RETURNS

1. Regulations under §1.1502-75(d) regarding group continuation.

CORPORATIONS AND THEIR SHAREHOLDERS

1. Updating §301 regulations to reflect statutory changes. Proposed regulations we published on March 26, 2019.

2. Revising regulations under §1.337(d)-7 regarding the treatment of certain foreign corporations. Final regulations were published on August 2, 2013.

3. Regulations relating to the requirements under §355, including the active trade or business requirement and the prohibition on device for the distribution of earnings and profits.

4. Final regulations regarding predecessors and successors under §355(e). Proposed regulations were published on December 19, 2016.
EMPLOYEE BENEFITS

A. Retirement Benefits

1. Guidance relating to certain IRS, Tax Exempt and Government Entities, Employee Plans programs, including the Pre-approved Plan Program, the Determination Letter Program, and the Employee Plans Compliance Resolution System (EPCRS).

2. Regulations under §§219, 408, 408A, and 4973 regarding IRAs.

3. Regulations under §401(a)(9) updating life expectancy and distribution period tables for purposes of the required minimum distribution rules and addressing certain other issues under §401(a)(9).

4. Final regulations on hardship distributions under §401(k) to reflect modifications made by sections 41113 and 41114 of the Bipartisan Budget Act of 2018. Proposed regulations were published on November 14, 2018.
   - PUBLISHED 09/23/19 in FR as TD 9875.

5. Guidance on student loan payments and qualified retirement plans and §403(b) plans.

6. Guidance on missing participants, including guidance on uncashed checks.
   - PUBLISHED 09/03/2019 in IRB 2019-36 as REV. RUL. 2019-19 (RELEASED 08/14/19).

7. Guidance on the timing of amendments to §403(b) plans.

8. Regulations updating rules for service credit and vesting under §411.

9. Regulations on the treatment of future interest credits and annuity conversion factors under a hybrid defined benefit plan and adjustments under a variable annuity plan for purposes of satisfying certain qualification requirements.

10. Regulations and related guidance on the unified plan rule for §413(c) multiple employer plans.
   - PUBLISHED 07/03/19 in FR as REG-121508-18 (NPRM).
11. Regulations on the definition of governmental plan under §414(d). An ANPRM was published on November 8, 2011.

12. Regulations relating to church plans.

13. Guidance regarding the aggregation rules under §414(m).

14. Final regulations under §415 regarding §7873 treaty fishing rights income. Proposed regulations were published on November 15, 2013.

15. Final regulations under §417(e) that update the minimum present value requirements for defined benefit plans. Proposed regulations were published on November 25, 2016.

17. Regulations relating to the reporting requirements under §6057. Proposed regulations were published on June 21, 2012.

B. Executive Compensation, Health Care and Other Benefits, and Employment Taxes

1. Regulations under §§119 and 132 regarding employer-provided meals.

2. Guidance under §125 on Health FSAs.

3. Guidance on HSAs and preventive care for chronic conditions.
   - PUBLISHED 08/05/19 in IRB 2019-32 as NOTICE 2019-45 (RELEASED 07/17/19).

4. Regulations on income inclusion and various other issues under §409A. Proposed regulations were published on December 8, 2008, and on June 22, 2016.

5. Regulations and other guidance under §§419A and 501(c)(9) relating to welfare benefit funds, including voluntary beneficiary associations (VEBAs).

6. Regulations under §457(f) and related guidance on ineligible plans. Proposed regulations were published on June 22, 2016.

7. Final regulations under §512 explaining how to compute unrelated business taxable income of voluntary employees’ beneficiary associations described in §501(c)(9). Proposed regulations were published on February 6, 2014.

8. Guidance on contributions to and benefits from paid family and medical leave programs.

10. Regulations under §§4980H and 105(h) related to HRAs.
   - PUBLISHED 09/30/19 in FR as REG-136401-18 (NPRM).

11. Guidance under §4980I regarding the excise tax on high cost employer-provided coverage.


**EXCISE TAX**

1. Regulations under §4261(e)(3)(C) regarding the application of the domestic air transportation excise tax under §4261 to the purchase of mileage awards.

2. Guidance under PPACA §9010.

**EXEMPT ORGANIZATIONS**


2. Guidance on circumstances under which an LLC can qualify for recognition under §501(c)(3).

3. Final regulations on §506, as added by the PATH Act of 2015. Temporary and proposed regulations were published on July 12, 2016.
   - PUBLISHED 07/23/19 in FR as TD 9873.

4. Final regulations on §509(a)(3) supporting organizations. Proposed regulations were published on February 19, 2016.

5. Guidance under §4941 regarding a private foundation's investment in a partnership in which disqualified persons are also partners.

6. Regulations regarding the excise taxes on donor advised funds and fund management.

7. Regulations and other guidance under §6033.
   - PUBLISHED 09/10/2019 in FR as REG-102508-16 (NPRM).
8. Final regulations under §6104(c). Proposed regulations were published on March 15, 2011.

9. Final regulations designating an appropriate high-level Treasury official under §7611. Proposed regulations were published on August 5, 2009.

FINANCIAL INSTITUTIONS AND PRODUCTS

1. Final regulations relating to the definition of registered form under §§149(a) and 163(f). Proposed regulations were published on September 19, 2017.

2. Guidance under §166 on the conclusive presumption of worthlessness for bad debts. Notice 2013-35, which requested comments on the existing rules, was published on June 10, 2013.

3. Regulations under §249 relating to the amount of a repurchase premium attributable to the cost of borrowing.

4. Guidance under §§446, 1275, and 6050H to address the treatment and reporting of capitalized interest on modified home mortgages.

5. Guidance addressing issues relating to mark-to-market accounting under §475.

6. Guidance clarifying the definition of income in §856(c)(3) for purposes of the REIT qualification tests.

7. Guidance under §860G(e) for modifications of certain mortgage loans held by a real estate mortgage investment conduit.

8. Regulations under §1001 on the modification of debt instruments, including issues relating to disregarded entities.


10. Guidance on the constant yield election under §1276(b).


GENERAL TAX ISSUES

2. Regulations under §45D that revise and clarify certain rules relating to the new markets tax credit.


4. Regulations on the definition of qualifying energy property under §48.

5. Final regulations regarding the interaction of the rules under §50(d)(5) and subchapter K. Proposed and temporary regulations were published on July 22, 2016.
   - PUBLISHED 07/19/19 in FR as TD 9872.

6. Final regulations under §152 regarding dependency deduction.

7. Final regulations under §165(i) providing procedures for making an election to take into account losses sustained in a Federally declared disaster area.

8. Regulations under §213 concerning expenses related to certain types of arrangements, potentially including direct primary care arrangements and healthcare sharing ministries.

9. Guidance clarifying whether the business use of an aircraft by a lessee that is a five percent owner or related party of the lessor of the aircraft is qualified business use for purposes of §280F.

10. Final regulations under §468A involving the decommissioning costs of a nuclear power plant.

11. Guidance under §7701 providing criteria for treating an entity as an integral part of a state, local, or tribal government, and guidance on tribally chartered corporations.


**GIFTS AND ESTATES AND TRUSTS**

1. Guidance on basis of grantor trust assets at death under §1014.

2. Regulations under §2032(a) regarding imposition of restrictions on estate assets during the six month alternate valuation period. Proposed regulations were published on November 18, 2011.
3. Regulations under §2053 regarding personal guarantees and the application of present value concepts in determining the deductible amount of expenses and claims against the estate.

4. Regulations under §7520 regarding the use of actuarial tables in valuing annuities, interests for life or terms of years, and remainder or reversionary interests.

INSURANCE COMPANIES AND PRODUCTS

1. Regulations under §72 on the exchange of property for an annuity contract. Proposed regulations were published on October 18, 2006.

2. Guidance relating to the diversification requirements under §817(h) for certain mortgage-backed securities purchased in the To-Be-Announced (TBA) market and for certain TBA contracts. Rev. Proc. 2018-54 was published on November 5, 2018.

INTERNATIONAL

A. Subpart F/Deferral

1. Final regulations under §954 concerning the definition of related person and the active rents exception to foreign personal holding company income. Proposed regulations were published on May 20, 2019.

B. Inbound Transactions

1. Final regulations under §§897 and 1445 relating to changes in the Protecting Americans from Tax Hikes Act of 2015. Proposed regulations were published on June 7, 2019.

C. Outbound Transactions

1. Final regulations on transfers of property to partnerships with related foreign partners and controlled transactions involving partnerships. Temporary and proposed regulations were published on January 19, 2017.

D. Foreign Tax Credits

1. Final regulations under §704 relating to the allocation by a partnership of creditable foreign taxes. Temporary and proposed regulations were published on February 4, 2016.

• PUBLISHED 07/24/19 in FR as TD 9871.
2. Final regulations under §901(m) on covered asset acquisitions. Temporary and proposed regulations were published on December 7, 2016.

E. Transfer Pricing


F. Sourcing and Expense Allocation

1. Regulations under §861, including on the character and source of income arising in transactions involving intellectual property and the provision of digital goods and services.

   - PUBLISHED 08/14/19 in FR as REG-130700-14 (NPRM).

G. Other

1. Regulations under §1256(g)(2) regarding the definition of a foreign currency contract, in light of the decision in Wright v. Commissioner, 809 F.3d 877 (6th Cir. 2016).

2. Final regulations and other guidance under Chapter 3 (§§1441-1446) and Chapter 4 (§§1471–1474), including: final regulations relating to due diligence requirements and allowances for withholding agents (including requirements related to (i) entity payees claiming benefits under treaties and (ii) the collection of foreign TINs of account holders maintaining accounts at U.S. offices and branches of financial institutions); and updates to the qualified intermediary withholding agreement (primarily relating to regulations under §1446(a) and (f)). Temporary and proposed regulations were published on January 6, 2017. Notice 2017-46 (regarding obtaining and reporting taxpayer identification numbers and dates of birth by financial institutions) was published on October 10, 2017. Revenue Procedure 2017-15 (setting forth the qualified intermediary withholding agreement) was published on January 17, 2017.

3. Guidance under §§6039F, 6048, and 6677 on foreign trust reporting and reporting with respect to foreign gifts, and regulations under §§643(i) and 679 relating to certain transactions between U.S. persons and foreign trusts.

4. Guidance under Chapter 61, including rules to require payors that are financial institutions and that maintain financial accounts at offices or branches within the United States to report information concerning certain account holders.
PARTNERSHIPS

1. Final regulations regarding the stock of a corporate partner under §337(d). Proposed regulations were published on March 25, 2019.

2. Final regulations on the fractions rule under §514(c)(9)(E). Proposed regulations were published on November 23, 2016.

3. Final regulations under §§704, 734, 743, and 755 arising from the American Jobs Creation Act of 2004, regarding the disallowance of certain partnership loss transfers and no reduction of basis in stock held by a partnership in a corporate partner. Proposed regulations were published on January 16, 2014.

4. Guidance under §707 on disguised sales, including disguised sales of partnership interests.

5. Final regulations under §§704 and 752 concerning partnership recourse liabilities, including bottom dollar payment obligations. Temporary and proposed regulations were published on October 5, 2016.

6. Final regulations under §752 regarding related person rules. Proposed regulations were published on December 16, 2013.

7. Final regulations under §§761 and 1234 on the tax treatment of noncompensatory partnership options. Proposed regulations were published on February 5, 2013.

TAX ACCOUNTING

1. Revenue procedure under §263(a) concerning the capitalization of natural gas transmission and distribution property.

2. Regulations under §472 concerning dollar-value last-in, first-out (LIFO) inventories, including rules for combining pools as a result of a change in method of accounting, certain corporate acquisitions, and certain nonrecognition transactions.

3. Final regulations amending §1.472-8 concerning the inventory price index computation (IPIC) method.
TAX ADMINISTRATION

1. Update to Notice 2011-26 regarding forms required to be e-filed.

2. Final regulations on electronic reporting under PPACA section 9010. Proposed regulations were published on December 9, 2016.

3. Guidance regarding information reporting on virtual currency under §6045.

4. Final regulations under §§6051 and 6052 regarding truncated taxpayer identification numbers. Proposed regulations were published on September 20, 2017.
   - PUBLISHED as TD 9861 on 07/03/19.

5. Final regulations under section 2006 of the Fixing America's Surface Transportation Act of 2015 regarding due dates and extensions for certain forms. Temporary and proposed regulations were published on July 20, 2017.

6. Update §6212 regulations regarding last known address for business taxpayers.

7. Update to Revenue Ruling 71-533.

8. Final regulations on safe harbors for de minimis errors on information returns and payee statements under section 202 of the Protecting Americans from Tax Hikes Act of 2015. Proposed regulations were published on October 17, 2018.

9. Revenue Procedures under §7123 concerning alternative dispute resolution.

10. Regulations updating the offer in compromise user fee.

11. Regulations updating the PTIN user fee.

TAX-EXEMPT BONDS

1. Guidance on private activity bonds under §141.

2. Guidance under §§144(b) and 150 on qualified student loan bonds.

3. Revenue procedure on the recovery of rebate under §148.
4. Guidance on direct payments for tax-advantaged bonds under §6431.

5. Guidance on tax-advantaged bond appeals procedures.

APPENDIX – Regularly Scheduled Publications

JULY 2019

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of §§42, 382, 1274, 1288, and 7520.
   - PUBLISHED 07/08/19 in IRB 2019-28 as REV. RUL. 2019-16 (RELEASED 06/18/19).

2. Notice setting forth updates for the corporate bond yield curve for plan years beginning in July 2019, the 24-month average segment rates, the funding segment rates applicable for July 2019, the spot segment rates for June 2019 that are used for determining minimum present values, and the 30-year Treasury rates.

AUGUST 2019

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of §§42, 382, 1274, 1288, and 7520.
   - PUBLISHED 08/05/19 in IRB 2019-32 as REV. RUL. 2019-17 (RELEASED 07/17/19).

2. Notice setting forth updates for the corporate bond yield curve for plan years beginning in August 2019, the 24-month average segment rates, the funding segment rates applicable for August 2019, the spot segment rates for July 2019 that are used for determining minimum present values, and the 30-year Treasury rates.
   - PUBLISHED 09/03/19 in IRB 2019-36 as NOT. 2019-48 (RELEASED 08/13/19).

3. Revenue procedure providing the domestic asset/liability percentages and the domestic investment yield percentages for taxable years beginning after December 31, 2017, for foreign companies conducting insurance business in the United States.
4. Revenue ruling providing the average annual effective interest rates charged by each Farm Credit Bank District.

- PUBLISHED 08/20/18 in IRB 2018-34 as REV. RUL. 2018-22.

SEPTEMBER 2019

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of §§42, 382, 1274, 1288, and 7520.

- PUBLISHED 09/03/19 in IRB 2019-36 as REV. RUL. 2019-20 (RELEASED 08/16/19).

2. Notice under §274 regarding the deemed substantiation of travel expenses using per diem rates.


3. Notice identifying the counties that experienced exceptional, extreme, or severe drought during the preceding 12-month period ending August 31, 2019, for purposes of determining whether the replacement period within which to replace livestock sold on account of drought is extended under §1033(e)(2)(B) and Notice 2006-82.

4. Revenue ruling under §6621 regarding the applicable interest rates for overpayments and underpayments of tax for the period October through December 2018.

- PUBLISHED 09/04/18 in IRB 2018-36 as REV. RUL. 2018-23 (RELEASED 08/17/18).

5. Update of Notice 2004-83 to add approved applicants for designated private delivery service status under §7502(f). Will be published only if any new applicants are approved.

6. Notice setting forth updates for the corporate bond yield curve for plan years beginning in September 2019, the 25-year average segment rates for 2020, the 24-month average segment rates, the funding segment rates applicable for September 2019, the spot segment rates for August 2019 that are used for determining minimum present values, and the 30-year Treasury rates.
7. Revenue ruling setting forth the terminal charge and the standard industry fare level (SIFL) cents-per-mile rates for the second half of 2019 for use in valuing personal flights on employer-provided aircraft.


8. Notice on annual adjustment in the fee imposed to fund the Patient Centered Outcomes Research Trust Fund.

- Published 11/26/18 in IRB 2018-48 as NOT. 2018-85 (Released 11/05/18).

OCTOBER 2019

1. Revenue procedure under §1 and other sections of the Code regarding inflation adjusted items for 2020.

2. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of §§42, 382, 1274, 1288 and 7520.

- Published 10/07/19 in IRB 2019-41 as Rev. Rul. 2019-23 (Released 09/17/19).

3. Revenue procedure providing the amounts of unused housing credit carryover allocated to qualified states under §42(h)(3)(D) for the calendar year.

4. Update of Revenue Procedure 2005-27 listing the tax deadlines that may be extended by the Commissioner under §7508A in the event of a Presidentially-declared disaster or terrorist attack. Will be published only if there are any updates.

5. Notice setting forth updates for the corporate bond yield curve for plan years beginning in October 2019, the 24-month average segment rates, the funding segment rates applicable for October 2019, the spot segment rates for September 2019 that are used for determining minimum present values, and the 30-year Treasury rates.
6. Revenue procedure providing the revised unpaid loss discount factors and salvage discount factors for the 2018 accident year and the unpaid loss discount factors and salvage discount factors for the 2019 accident year to be used for computing discounted unpaid losses under §846 and discounted estimated salvage recoverable under §832. Rev. Proc. 2019-06, which provided the initial 2018 accident year discount factors, was published on January 7, 2019.

- PUBLISHED 08/12/19 in IRB 2019-33 as REV. PROC. 2019-31 (RELEASED 07/22/19).

**NOVEMBER 2019**

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of §§42, 382, 1274, 1288 and 7520.

2. Notice under §274 regarding the 2020 optional standard mileage rates

3. Revenue ruling setting forth covered compensation tables under §401(l)(5)(E) that are used for purposes of applying the permitted disparity rules under §401(l) to defined benefit plans for the 2020 plan year.

4. Notice setting forth required amendment deadlines for §401(a) plans with respect to certain changes in qualification requirements.

5. Revenue ruling providing the “base period T-Bill rate” as required by §995(f)(4).

6. Update of Revenue Procedure 2016-13 regarding adequate disclosure for purposes of the §6662 substantial understatement penalty and the §6694 preparer penalty. Will be published only if there are any updates.

7. Notice setting forth updates for the corporate bond yield curve for plan years beginning in November 2019, the 24-month average segment rates, the funding segment rates applicable for November 2019, the spot segment rates for October 2019 that are used for determining minimum present values, and the 30-year Treasury rates.

8. Notice setting forth cost-of-living adjustments effective January 1, 2020, applicable to the dollar limits on benefits under qualified defined benefit pension plans and other provisions affecting certain plans of deferred compensation.

10. Notice updating mortality improvement rates and static mortality tables to be used by defined benefit plans for 2021.

DECEMBER 2019

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of §§42, 382, 1274, 1288, and 7520.

2. Revenue ruling under §6621 regarding the applicable interest rates for overpayments and underpayments of tax for the period January through March 2018.
   • PUBLISHED 12/17/18 in IRB 2018-51 as REV. PROC. 2018-32 (RELEASED 12/06/18).

3. Notice setting forth updates for the corporate bond yield curve for plan years beginning in December 2019, the 24-month average segment rates, the funding segment rates applicable for December 2019, the spot segment rates for November 2019 that are used for determining minimum present values, and the 30-year Treasury rates.

JANUARY 2020

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of §§42, 382, 1274, 1288, and 7520.

2. Revenue procedure under §280F providing limitations on depreciation deductions for owners of passenger automobiles first placed in service during the calendar year and amounts to be included in income by lessees of passenger automobiles first leased during the calendar year.

3. Revenue procedure updating the procedures for issuing private letter rulings, determination letters, and information letters on specific issues under the jurisdiction of the Chief Counsel.

4. Revenue procedure updating the procedures for furnishing technical advice, including technical expedited advice, to certain IRS offices, in the areas under the jurisdiction of the Chief Counsel.
5. Revenue procedure updating the previously published list of “no-rule” issues under the jurisdiction of certain Associate Chief Counsel (Corporate), Associate Chief Counsel (Financial Institutions and Products), Associate Chief Counsel (Income Tax and Accounting), Associate Chief Counsel (Passthroughs and Special Industries), Associate Chief Counsel (Procedure and Administration), and Associate Chief Counsel (Tax Exempt and Government Entities) on which advance letter rulings or determination letters will not be issued.

6. Revenue procedure updating the procedures for issuing determination letters and letter rulings on issues under the jurisdiction of the Office of the Commissioner, Tax Exempt and Government Entities Division, Employee Plans Rulings and Agreements Office.

7. Revenue procedure updating the procedures for issuing determination letters under the jurisdiction of the Office of the Commissioner, Tax Exempt and Government Entities Division, Exempt Organizations Rulings and Agreements Office.

8. Revenue procedure updating the previously published list of “no-rule” issues under the jurisdiction of the Associate Chief Counsel (International) on which advance letter ruling or determination letters will not be issued.

9. Notice setting forth updates for the corporate bond yield curve for plan years beginning in January 2020, the 24-month average segment rates, the funding segment rates applicable for January 2020, the spot segment rates for December 2019 that are used for determining minimum present values, and the 30-year Treasury rates.

FEBRUARY 2020

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of §§42, 382, 1274, 1288, and 7520.


3. Notice setting forth updates for the corporate bond yield curve for plan years beginning in February 2020, the 24-month average segment rates, the funding segment rates applicable for February 2020, the spot segment rates for January 2020 that are used for determining minimum present values, and the 30-year Treasury rates.

MARCH 2020

1. Revenue procedure providing annual indexing required under §36B.
2. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of §§42, 382, 1274, 1288, and 7520.

3. Notice providing the 2020 calendar year resident population estimates used in determining the state housing credit ceiling under §42(h) and the private activity bond volume cap under §146.

4. Revenue procedure under §143 regarding average area purchase price.

5. Revenue ruling under §6621 regarding the applicable interest rates for overpayments and underpayments of tax for the period April through June 2019.

   • PUBLISHED 03/11/19 in IRB 2019-11 as REV. RUL. 2019-05.

6. Revenue ruling setting forth the terminal charge and the standard industry fare level (SIFL) cents-per-mile rates for the first half of 2020 for use in valuing personal flights on employer-provided aircraft.

7. Notice setting forth updates for the corporate bond yield curve for plan years beginning in March 2020, the 24-month average segment rates, the funding segment rates applicable for March 2020, the spot segment rates for February 2020 that are used for determining minimum present values, and the 30-year Treasury rates.

8. Revenue procedure providing the annual update to the List of Automatic Changes for taxpayer changes in method of accounting.

**APRIL 2020**

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of §§42, 382, 1274, 1288, and 7520.

2. Guidance providing the calendar year inflation adjustment factor and reference prices for the renewable electricity production credit under §45.

3. Revenue procedure providing a current list of countries and the dates those countries are subject to the §911(d)(4) waiver and guidance to individuals who fail to meet the eligibility requirements of §911(d)(1) because of adverse conditions in a foreign country.
4. Notice setting forth updates for the corporate bond yield curve for plan years beginning in April 2020, the 24-month average segment rates, the funding segment rates applicable for April 2020, the spot segment rates for March 2020 that are used for determining minimum present values, and the 30-year Treasury rates.

MAY 2020

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of §§42, 382, 1274, 1288, and 7520.

2. Guidance providing the inflation adjustment factor to be used in determining the enhanced oil recovery credit under §43 for tax years beginning in the calendar year.

3. Revenue procedure providing guidance for use of the national and area median gross income figures by issuers of qualified mortgage bonds and mortgage credit certificates in determining the housing cost/income ratio under §143.

4. Revenue procedure under §223 regarding the inflation adjusted items for 2021.


6. Notice regarding marginal production rates under §613A for oil and gas well depletion.

7. Notice setting forth updates for the corporate bond yield curve for plan years beginning in May 2020, the 24-month average segment rates, the funding segment rates applicable for May 2020, the spot segment rates for April 2020 that are used for determining minimum present values, and the 30-year Treasury rates.

JUNE 2020

1. Revenue ruling setting forth tables of the adjusted applicable federal rates for the current month for purposes of §§42, 382, 1274, 1288, and 7520.

2. Notice setting forth the §45K(d)(2)(C) reference price for the nonconventional source production credit.

3. Notice setting the inflation adjustment factor for the credit for carbon dioxide (CO₂) sequestration under §45Q for calendar year 2019.
4. Revenue ruling under §6621 regarding the applicable interest rates for overpayments and underpayments of tax for the period July through September 2019.

5. Notice setting forth updates for the corporate bond yield curve for plan years beginning in June 2020, the 24-month average segment rates, the funding segment rates applicable for June 2020, the spot segment rates for May 2020 that are used for determining minimum present values, and the 30-year Treasury rates.