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**National Association of Federally-Insured Credit Unions**

August 7, 2020

Internal Revenue Service  
P.O. Box 7604  
Ben Franklin Station  
Washington, D.C. 20224

**RE: Tax on Excess Tax-Exempt Organization Executive Compensation (IRS  
REG-122345-18)**

Dear Sir or Madam:

On behalf of the National Association of Federally-Insured Credit Unions (NAFCU), I am writing in response to the Internal Revenue Service's (IRS) notice of proposed rulemaking regarding an excise tax on excess executive compensation for tax-exempt organizations. NAFCU advocates for all federally-insured not-for-profit credit unions that, in turn, serve nearly 121 million consumers with personal and small business financial service products. The *Tax Cuts and Jobs Act* (TCJA) added section 4960 to the Internal Revenue Code (IRC) whereby applicable tax-exempt organizations (ATEO) must pay an excise tax on excess remuneration. Credit unions and certain credit union service organizations are ATEOs and subject to the proposed rule. NAFCU asks the IRS to not include fringe benefits in excess of excludable amounts in the definition of excess remuneration. In addition, NAFCU again urges the IRS to grandfather certain nonqualified deferred compensation plans to assist credit unions with attracting and retaining talent.

**The Definition of Remuneration Should Exclude Taxable Fringe Benefits in Excess of the Amount that is Excludable**

NAFCU asks the IRS to exclude taxable fringe benefits over and above the amount that is excludable from gross income. Under the proposal, the definition of remuneration has the definition found in IRC section 3401(a). Section 3401(a) defines remuneration as regular employee wages; however, the definition also includes benefits paid to or on behalf of an employee over an above any excludable amount. Many employers provide benefits to employees not only to attract them to a job but to supplement salaries. For example, employers regularly offer reimbursement of childcare expenses and other fringe benefits to employees. Certain fringe benefits, excludable from gross income under the IRC, have caps on the amount that may be excluded from gross income. The IRS should adopt a definition of remuneration that does not include excess fringe benefit amounts and instead only include regular employee wages.

Fringe benefits are not the type of excess remuneration that the proposal aims to tax and excluding these benefits will assist in attracting and retaining talent. The proposal charges an excise tax on remuneration over \$1,000,000 and includes things like parachute payments. Certainly, the intent

was not to tax a covered employee on paid parking and reimbursement of childcare expenses. Excluding fringe benefits will have a positive impact on a credit union's ability to attract and retain key talent. According to NAFCU's 2019 *Federal Reserve Study*, attracting and retaining skilled staff and management is one of the top challenges anticipated by credit unions over the next three years. Moreover, this challenge continues to be a concern year-over-year as credit unions face competitive pressures from others in the financial services industry.

### **The IRS Should Grandfather Certain Employee Remuneration Contracts Executed on or Before November 2, 2017**

The proposal allows for a grandfathering effect on certain compensation, including nonqualified deferred compensation that vests prior to the first day of the first taxable year of the ATEO beginning after December 31, 2017. These nonqualified deferred compensation plans are not considered remuneration; however, all earnings that accrue or vest after the effective date are treated as remuneration. NAFCU reiterates its call for the IRS to evaluate its authority to provide for the grandfathering of certain employee remuneration contracts, including nonqualified deferred compensation plans, executed on or before November 2, 2017.

Employee remuneration in the form of a deferred compensation plan helps attract talented executives with community-focused leadership skills to credit unions. Permitting the grandfathering of nonqualified deferred compensation plans assists credit unions in overcoming strategic challenges in hiring executives. In addition, assessing an excise tax on certain compensation plans increases credit union expenditures. As not-for-profit, member-owned financial institutions, credit unions provide benefits to their members and communities. Additional expenditures deplete resources that could otherwise help credit unions serve their members and communities. Member-owners receive benefits in the form of dividends, therefore additional taxes imposed on credit unions means less money in the pockets of members and in the communities in which they live and work.

This outcome is at odds with the underlying reason for the excise tax, which is Congress' belief that excessive compensation diverts resources from the purpose of the tax-exempt entity. The proposal references a House Report which argues that tax-exempt organizations enjoy a tax subsidy because contributions to the ATEO are generally deductible, ATEOs are subject to using their resources for specific purposes, and that excessive compensation, including excessive severance packages, to senior executives diverts resources from the purpose of the ATEO.<sup>1</sup> However, this report and the legislative history of the TCJA fail to consider the vast differences between credit unions and their for-profit counterparts. It is important to note that credit unions are unique, member-focused and owned, cooperatives that provide necessary capital and financial services to their communities, including underserved areas. Moreover, credit unions may be tax exempt organizations, but they still pay many taxes and fees, including payroll and property taxes. In addition, credit unions do not receive contributions like a typical tax-exempt organization.

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<sup>1</sup> H.Rep. 115-409, 115<sup>th</sup> Cong., 1<sup>st</sup> Sess. 333 (Nov. 13, 2017).

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Due to these differences, NAFCU asks that the IRS provide for the grandfathering of certain employee remuneration contracts executed on or before November 2, 2017. Alternatively, NAFCU asks the IRS to support congressional efforts to introduce a technical corrections bill that would adopt this change. Congress has indicated its intention to work on a technical corrections bill to fix errors and unanticipated complications such as this inappropriate excise tax on certain credit union employee remuneration contracts.

## **Conclusion**

NAFCU appreciates the opportunity to share its members' views on this matter. NAFCU asks the IRS to not include fringe benefits in excess of excludable amounts in the definition of excess remuneration. In addition, NAFCU again urges the IRS to grandfather certain nonqualified deferred compensation plans. Should you have any questions or require additional information, please do not hesitate to contact me at (703) 842-2249 or [kschafer@nafc.org](mailto:kschafer@nafc.org).

Sincerely,



Kaley Schafer  
Senior Regulatory Affairs Counsel