

Section 4960: Who, When and How Much

1

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Properly identifying covered employees, the existence of deferred compensation arrangements, and ensuring that compensation is properly measured for relevant reporting periods.

2

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- **Section 4960: Basic Overview**

- Imposes a 21% tax (the corporate tax rate) that:
 - is effective for tax years beginning after December 31, 2017,
 - is payable by the exempt employer, on the sum of
 - 4960(a)(1) - employment **remuneration** paid by an applicable tax-exempt organization (ATEO) to a **covered employee** over \$1 million, and
 - 4960(a)(2) **excess parachute payments** paid, to a **covered employee**.
- ATEO includes colleges and universities that are exempt under Section 501(a) as well as those exempt under Section 115(1).

Section 4960: Who, When, and How Much?

- **Who is a “covered employee”?**

- A covered employee includes:
 - the five highest compensated employees of the institution for the taxable year; AND
 - any covered employee for any preceding taxable year beginning after December 31, 2016
 - The number of “covered employees” is subject to continuous expansion.
 - Includes former employees of the institution.
 - Includes deceased employees, if payments are made to families of death of covered employees
 - NOT just officers

Section 4960: Who, When, and How Much?

- **Example:**
 - In 2018, A, B, C, D, and E are the five highest compensated employees (and have been since 2017).
 - In 2019, F, G, H, I, and J are the five highest compensated employees.
 - For 2019, all ten employees are “covered employees.”
- **Example 2: Same facts as Example above but in 2021.**
 - In 2021 F and G are no longer in top paid group, replaced by L and M
 - F terminates voluntarily in 2021. His section 457(f) plan vested normally in 2021 and is paid in a lump sum in 2022
 - G is now part-time
 - A – M are all counted as covered employees.
 - Need to test F’s 457(f) payment for 4960 purposes

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- **How Much? Identifying 4960(a)(1) Remuneration.**
 - **Remuneration includes:**
 - wages (as defined in section 3401(a)),
 - ineligible deferred compensation plan distributions under Section 457(f)
 - Taxable fringe benefits
- **Note: Remuneration includes compensation paid by “related organizations.”**

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