



AMERICAN BENEFITS COUNCIL

April 2, 2019

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Internal Revenue Service
CC:PA:LPD:PR (Notice 2019-09)
Room 5203
P.O. Box 7604
Ben Franklin Station
Washington, DC 20044

Re: Comments on Interim Guidance under Section 4960 (Notice 2019-09)

Dear Sir/Madam:

The American Benefits Council (“the Council”) appreciates the opportunity to submit comments on Notice 2019-09, which provides interim guidance on the excise tax imposed on excess compensation paid by tax-exempt organizations under new Internal Revenue Code Section 4960.¹ As discussed below, **we are writing to ask the Treasury Department and the Internal Revenue Service (IRS) to clarify that an applicable tax-exempt organization (ATEO) will not be subject to the excise tax imposed by Section 4960 with respect to officers who serve in a solely volunteer capacity with the organization.** For the reasons described below, an adverse position on this issue (1) is inconsistent with the statute and (2) would very likely result in the termination of some ATEOs that do so much to benefit the public and the causes they support.

The Council advocates for employers dedicated to the achievement of best-in-class solutions that protect and encourage the health and financial well-being of workers, retirees and families. Council members include over 220 of the world's largest corporations as well as organizations serving employers of all sizes. Collectively, our members directly sponsor or administer health and retirement benefits for virtually all Americans covered by employer-sponsored plans.

¹ Unless indicated otherwise, all references to “section” herein refer to sections of the Internal Revenue Code.

SUMMARY

As described in more detail below, the Council offers the following recommendations for approaches that the Treasury Department and IRS should take in providing clarification that an ATEO or related organization will not be subject to the excise tax imposed by Section 4960 with respect to ATEO officers who serve in a solely volunteer capacity:

- **Volunteers are not employees.** We ask that, consistent with the statute, the Treasury Department and IRS clarify that individuals who serve as officers of an ATEO and do not receive any compensation, directly or indirectly, for their volunteer services are not considered employees of the ATEO for purposes of Section 4960.
- **Alternative 1: Covered employee status is determined based only on ATEO compensation.** If the Treasury Department and IRS choose not to clarify that a volunteer officer of an ATEO is not considered an employee of the ATEO, then, we urge the Treasury Department and IRS to provide, based on the statute, that the determination of an ATEO's covered employees is made without regard to any remuneration received by an ATEO's employee from a related entity with respect to services the individual performs for a related entity.
- **Alternative 2: Excise tax is based only on compensation for services to ATEO.** In the event that the Treasury Department and the IRS issue guidance providing that unpaid, volunteer officers of an ATEO are considered "employees" of the ATEO for purposes of Section 4960 and that any remuneration paid to such volunteers by a related entity is counted for purposes of determining whether they are "covered employees" of the ATEO, then we would urge the Treasury Department and IRS to establish an anti-abuse rule that would only take into account remuneration paid for services to the ATEO.

TAX-EXEMPT ORGANIZATIONS SERVED BY VOLUNTEER OFFICERS

The Council's members are concerned about the manner in which Section 4960 will be applied to the following situation in particular. As the Treasury Department and IRS are aware,² a number of tax-exempt organizations have officers who are volunteers and are not paid, directly or indirectly, for their services to the organization. A common example of this is one in which a for-profit corporation has established a private foundation. It is not unusual for the for-profit entity – in addition to funding the private foundation – to ask talented employees of the for-profit entity to serve as officers of the foundation in a volunteer capacity.

² See EXEMPT ORGANIZATIONS: COMPENSATION OF OFFICERS, <https://www.irs.gov/charities-non-profits/exempt-organizations-compensation-of-officers> (last visited March 21, 2019) ("Many exempt organizations have officers who are volunteers and not paid for their services.")

These volunteer officers are often highly accomplished and successful individuals, including mid- and upper-level managers and executives of the for-profit entity.³ The private foundation benefits significantly from the insight, knowledge and perspectives that these individuals bring to their roles as officers. In addition, the individuals typically continue to perform their employment duties with respect to the for-profit entity and do not receive additional compensation from the for-profit entity as a result of their part-time volunteer service to the private foundation.

In some situations, these individuals may serve as officers of the private foundation for many years. But in other situations, the for-profit entity may ask its employees to serve on a more temporary basis, such as a one-year or two-year period, after which the employee is expected to return to solely performing his or her role with the for-profit entity. For large for-profit entities in particular, including some of the Council's members, this rotational approach may be used to allow more employees the opportunity to contribute their talents to the private foundation. A rotational approach also offers greater flexibility to all parties involved based on the strategic, leadership, or management needs of the private foundation, the business needs of the for-profit entity and the capacity of the individual to serve in a volunteer position in addition to his or her responsibilities to the for-profit entity.

ADVERSE CONSEQUENCES OF APPLYING SECTION 4960 TO ATEOs WITH RESPECT TO VOLUNTEER OFFICERS

As described below, the Council believes that the excise tax imposed by Section 4960 is best interpreted as *not* applying to an ATEO with respect to an officer who is serving solely in a volunteer capacity. Although the language of Notice 2019-09 suggests that the Treasury Department and IRS may already share this view, our members are nevertheless concerned that any additional guidance issued by the Treasury Department and IRS under Section 4960 address the remaining lack of clarity on this point and, more importantly, not adopt a contrary view.

The potential guidance that concerns the Council's members is any guidance under which (1) a volunteer officer would be treated as an employee of the ATEO and (2) the volunteer officer's remuneration received from a related entity (for services performed for the related entity) would be required to be taken into account for purposes of both determining covered employee status and calculating the excise tax. It is not uncommon for individuals who serve as volunteer officers of an ATEO to be highly paid by a related for-profit entity for their continuing services to the for-profit entity. Any guidance that operates as described above would be very problematic if the volunteer

³ Such individuals may or may not be "covered employees" for purposes of Section 162(m) with respect to the for-profit entity in cases where the for-profit entity is a publicly held corporation.

officers are paid more than \$1 million a year by the for-profit entity for their services to the for-profit entity.

The adverse consequences of such guidance are best illustrated using the above example in which a for-profit entity asks its employees to serve as volunteer officers of its private foundation on a temporary or rotational basis. If the Treasury Department and IRS issue guidance that applies Section 4960 in the manner described in the preceding paragraph, then in many cases the private foundation's covered employees for a taxable year would consist largely or entirely of its volunteer officers. As a result, any of these individuals earning over \$1 million for their services to the for-profit entity will cause the for-profit employer to owe excise tax under Section 4960.

The prospect of facing an excise tax liability with respect to up to five volunteers is daunting. But that is just the beginning. The statute treats any individual who was ever a covered employee (beginning in 2017 or later) as forever continuing to be a covered employee. Within a matter of years, a for-profit entity that uses a rotational approach to encourage its employees to serve as volunteer officers of its private foundation could find itself with dozens of employees with respect to whom the for-profit entity is liable for an ever-increasing amount of tax under Section 4960.

These consequences are exacerbated even more for a for-profit entity that encourages mid-career employees to serve as volunteer officers of its foundation, because those individuals may continue in their employment with the for-profit entity for many years after they become a covered employee with respect to the foundation. At some point in the not-too-distant future, any charitable inclinations or other benefits the for-profit entity and the public enjoy from the private foundation will be largely overshadowed by this new tax burden. As a result, some of our members have indicated that, in the event that the Treasury and IRS issue guidance that would produce this result, their for-profit entity would likely terminate its private foundation and attempt to provide charitable giving in a different, less effective and less efficient manner.

Although we understand the policy reasons behind Congress enacting Section 4960 and we support measures aimed at thwarting abusive compensation schemes, we do not believe that Congress intended for Section 4960 to be interpreted in a manner that becomes so burdensome in the situation described above that for-profit entities would view terminating their private foundation as the only viable path forward. And, as discussed below, we believe that such an interpretation is contrary to the statute.

REQUEST FOR GUIDANCE THAT AVOIDS SEVERE ADVERSE IMPLICATIONS FOR CERTAIN ATEOS WITH VOLUNTEER OFFICERS

As noted above, the Council does not believe that the statute requires the application of Section 4960 in a manner that will produce the very adverse result described above for ATEOs that have volunteer officers who are also employed by a related entity. In this regard, we have the following recommendations for approaches that the Treasury Department and IRS could take in providing the clarification needed to avoid the harm described above in a manner that is entirely consistent with the statute.

1. Clarify that unpaid, volunteer officers are not considered “employees” of the ATEO.

The most straightforward approach that we recommend for purposes of avoiding severe harm to ATEOs with volunteer officers is to clarify that individuals who serve as officers of an ATEO and do not receive any compensation, directly or indirectly, for their volunteer services are not considered employees of the ATEO for purposes of Section 4960.

Section 4960(c)(2) defines “covered employee” in part as “any *employee* (including any former employee) of an applicable tax-exempt organization” (emphasis added). Thus, by definition, an individual cannot be a covered employee of an ATEO unless that individual is first established to be an employee of the ATEO. Section 4960, however, does not provide a definition of “employee.”

In Notice 2019-09, the IRS provides that “only an ATEO’s common law employees (including officers) can be one of an ATEO’s five highest-compensated employees.” The phrase “including officers” indicates that the officers being referred to are a subset of the ATEO’s common law employees. In other words, the notice suggests that an officer of an ATEO could not meet the definition of covered employee unless the officer is also a common law employee of the ATEO (as opposed to an unpaid volunteer or an independent contractor). The Council strongly supports this result.

Yet because Notice 2019-09 is not entirely clear on this point, questions have been raised as to the relevance, if any, of the definition of “employee” in other sections of the Code, such as sections 3401 and 3121, for purposes of Section 4960. Sections 3401(c) and 3121(d), which define employee for purposes of chapter 24 (Collection of Income Tax at Source on Wages) and chapter 21 (Federal Insurance Contributions Act), respectively, provide in part that the term employee means an “officer of a corporation.” Treasury regulations, however, provide that:

Generally, an officer of a corporation is an employee of the corporation.
However, *an officer of a corporation who as such ... performs only minor services and*

*who neither receives nor is entitled to receive, directly or indirectly, any remuneration is not considered to be an employee of the corporation.*⁴ [Emphasis added.]

These authorities tell us a few things. First, without sections 3401(c) and 3121(d), volunteer officers would not be employees. Otherwise, sections 3401(c) and 3121(d) would serve no purpose. This, in turn, tells us that the general rule under the Code is that volunteer officers are not employees, except to the extent that they are specifically treated as employees by a Code provision, like sections 3401(c) and 3121(d). But because neither Section 3401(c) nor Section 3121(d) applies for purposes of Section 4960, the conclusion is inescapable that volunteer officers are not employees for purposes of Section 4960. The inapplicability of the definition of “employee” in Section 3401(c) in particular is especially apparent because Congress specifically cross-referenced the definition of “wages” in Section 3401(a) for purposes of defining the term “remuneration” in Section 4960(c)(3), yet Congress did not include a similar cross-reference to Section 3401(c) for purposes of defining who constitutes an “employee” under Section 4960. Had Congress intended for the definition of “employee” in either sections 3401(c) or 3121(d) to apply for purposes of Section 4960, Congress would have provided for such a result.

Second, even if an argument could be made that Treasury and the IRS have the authority to treat volunteer officers as employees for purposes of Section 4960, which we do not believe is the case, the Treasury Department and IRS clearly have the authority *not* to do so, especially since they exercised that authority even in the context of multiple statutory provisions that treat officers as employees.⁵ At a minimum, Treasury and the IRS should exercise that same authority under Section 4960 in situations like those described above with respect to part-time temporary volunteer officers.

2. Clarify that an ATEO’s covered employees are determined without regard to remuneration received by an employee from a related organization.

If the Treasury Department and IRS choose not to clarify that a volunteer officer of an ATEO is not considered an employee of the ATEO, then, in the alternative, we urge the Treasury Department and IRS to provide that the determination of an ATEO’s covered employees is made without regard to any remuneration received by an ATEO’s employee from a related entity with respect to services the individual performs for a related entity.

⁴ Treas. Reg. Section 31.3401(c)-1(f); *see also* Treas. Reg. Section 31.3121(d)-1(b) (providing nearly identical language). In addition, the IRS generally recites the language of this regulation in its webpage regarding the compensation of officers of exempt organizations. EXEMPT ORGANIZATIONS: COMPENSATION OF OFFICERS, *supra* note 2.

⁵ *See* Treas. Reg. Section 31.3401(c)-1(f); Treas. Reg. Section 31.3121(d)-1(b); Treas. Reg. Section 31.3306(i)-1(e).

Section 4960(c)(2)(A) provides that an individual is a covered employee of an ATEO if the individual “is one of the 5 highest compensated employees of the organization for the taxable year.” The statute is silent with respect to how an ATEO should identify its five highest compensated employees. Notice 2019-09 provides that the five highest compensated employees should be determined based on remuneration paid, which is the same standard used for purposes of computing the excise tax. In other words, “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 ... for services performed as an employee of such related organization.”⁶

We encourage the Treasury Department and IRS to reconsider the position taken in the notice. If Congress had intended for all remuneration, as described in Section 4960(c)(3)-(4), to be taken into account for purposes of determining which employees are the five highest-compensated employees of an ATEO, Congress clearly could have provided for that result by using the term “remuneration” in the definition of covered employee. But Congress did not do so and instead used the term “compensation.” There is no statutory basis to conclude that “compensation” from a related entity should be attributed to an ATEO for purposes of determining an ATEO’s covered employees, especially in light of the statutory provision adopting this position with respect to remuneration, but not compensation. We therefore request that the Treasury Department and IRS interpret Section 4960(c)(2)(A) as simply requiring the identification of the five employees to whom the ATEO pays the most compensation. Under this approach, a volunteer officer of the ATEO who is unpaid would be excluded from the ATEO’s list of covered employees.

3. Establish an anti-abuse rule under which remuneration received by a covered employee from a related entity is not included to the extent that such remuneration is paid for services the covered employee performs for a related entity.

In the event that the Treasury Department and the IRS issue guidance providing that unpaid, volunteer officers of an ATEO are considered “employees” of the ATEO for purposes of Section 4960 and that any remuneration paid to such volunteers by a related entity is counted for purposes of determining whether they are “covered employees” of the ATEO, then we would urge the Treasury Department and IRS to establish an anti-abuse rule that would provide a path forward for the parties involved in a non-abusive situation such as the one we described above.

Section 4960(c)(4)(A) provides, “Remuneration of a covered employee by an [ATEO] shall include any remuneration paid with respect to employment of such employee by

⁶ Section I(C) of Notice 2019-09.

any related person or governmental entity.” It is not clear from this provision whether remuneration includes (1) any remuneration paid by any related person or governmental entity *with respect to the employee’s employment by the ATEO*, or (2) any remuneration paid by a related person or governmental entity *with respect to the employee’s employment by the related person or governmental entity*. In light of this ambiguity in the statutory language and the authority provided to the Secretary of the Treasury to prescribe regulations to prevent abusive situations, we believe that it would be appropriate for the Treasury Department and IRS to incorporate an anti-abuse rule into the determination of a covered employee’s remuneration.

The Council recommends that such an anti-abuse rule should provide that any remuneration paid to an employee of an ATEO by a related entity will not be included for purposes of calculating the excise tax under Section 4960 to the extent that such remuneration is paid solely for services performed by the individual as an employee of the related entity and there is no evidence that the arrangement is intended to avoid the excise tax. Such a rule would effectively distinguish between abusive and non-abusive situations, thus protecting non-abusive ATEOs from the inappropriately adverse consequences described above.

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We ask the Treasury Department and IRS to use one of the approaches recommended above in order to avoid an inappropriate extension of Section 4960 to ATEOs with volunteer officers that would produce counterproductive results that are not consistent with the statute.

Thank you for your consideration of our comments. If you would find it helpful to discuss any of these matters with us, please contact me at 202-289-6700 or ldudley@abcstaff.org.

Sincerely,

A handwritten signature in cursive script that reads "Lynn D. Dudley".

Lynn D. Dudley
Senior Vice President, Global Retirement & Compensation Policy