Tax reform presents pension plan and deferred compensation planning opportunities

Background
President Trump and the Republican majority in Congress have issued varying tax reform legislative proposals. If enacted, the legislation is expected to reduce corporate tax rates significantly. This creates opportunities to accelerate the timing of the deduction for compensation and benefits expenses into a taxable year with a higher tax rate. Potential changes to taxation of foreign income also creates greater focus on methods of accounting for foreign pension expenses.

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Legislative
• Reduction to corporate tax rates
• Acceleration of tax deductions
• Delaying income inclusion
• Earnings and profits planning (E&P)
• Use of foreign tax credits
• Changes to Internal Revenue Code (IRC) §199 deduction

Strategy
• US pension funding
• Non-US pension funding and reserves
• Health and welfare:
  • Incurred but not reported (IBNR) costs
  • Voluntary employee benefits association (VEBA) trusts
  • Deferred compensation programs
  • Bonus accruals

Regulatory

Compensation and benefits tax planning

Governance
Industry and enterprise

Financial impact

Building a better working world
Opportunity

Compensation and benefits programs represent significant expenses to taxpayers. Methods and strategies surrounding the funding of compensation and benefits programs, and the timing of the deduction of these expenses, are key components of overall tax reform planning activities. In many cases, tax benefits can be identified without requiring additional funding to benefit plans or changing the benefits provided under the plans.

Ernst & Young LLP has an experienced team of tax technical and actuarial professionals that can review your compensation and benefits programs to find opportunities to accelerate or identify missed deductions. And, if applicable, we can assist with applying for a change in accounting methods through filing a Form 3115 with the Internal Revenue Service.

<table>
<thead>
<tr>
<th>Characteristics</th>
<th>Potential opportunity</th>
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<tbody>
<tr>
<td>US parent sponsoring foreign defined benefit pension plans</td>
<td>International tax planning through deductions for foreign pension plan expenses: Make election under IRC §404A to claim a tax deduction (or in the case of a foreign subsidiary, an adjustment to E&amp;P) for actual cash contributions made to trusteed foreign pension plans or for the additions to the reserve for unfunded pension plans</td>
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<tr>
<td>Sponsor of retirement plans taking an IRC §199 production deduction</td>
<td>Exclusion of pre-IRC §199 enactment costs: Increase the IRC §199 deduction while still available by actuarially determining the costs associated with defined benefit pension and/or retiree health and welfare plans that relate to pre-IRC §199 enactment periods, and consider whether these amounts can be apportioned away from Qualified Production Activities Income</td>
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<td>Sponsor of US qualified defined benefit pension plan</td>
<td>Acceleration of deductions for qualified pension plans: Increase pension contribution up to the IRC §404(o) deductible limit; deduction may be accelerated to prior taxable year for contributions made on account of that year (e.g., reported on the Form 5500 for that plan year) prior to the corporate tax filing date, plus extensions</td>
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<td>Sponsor of retiree medical plan</td>
<td>Acceleration of retiree medical expense deductions: Pre-fund benefits under a VEBA to accelerate deductions, subject to IRC §419A limitations</td>
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<td>Self-insured active or retiree medical plan sponsors</td>
<td>Acceleration of deductions for IBNR claims: Apply for a method change to accelerate deduction to the period when the services are rendered</td>
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<td>Sponsors of NQDC arrangements</td>
<td>Acceleration of nonqualified deferred compensation (NQDC) deductions: Consider accelerating deduction for NQDC “short-term deferrals” by accelerating vesting and payments in accordance with IRC §409A</td>
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<tr>
<td>Sponsor of restricted stock</td>
<td>Accelerated vesting of restricted stock: Consider opportunities to accelerate deductions by expediting the vesting of restricted stock grant where no IRC §83(b) election was made</td>
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<td>Bonus accruals</td>
<td>Bonus deduction acceleration: A bonus pool or accrual of minimum payment may allow payments to be fixed and deductible by the end of the tax year regardless of employee “last day” requirements or other typical discretion to reduce payments to individuals; if paid within 2.5 months after the end of the tax year, this could accelerate deductions for taxpayers on accrual method, while delaying employee income inclusion until the year in which the bonus is paid</td>
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