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President Biden's FY 2024 budget proposes many changes affecting employers and employees

Summary

- *President Biden released an FY 2024 budget calling for $3 trillion in deficit reduction over the next 10 years.*
- *The budget proposes reducing some employer credits, such as the Workforce Opportunity Tax Credit (WOTC), while making some others permanent.*
- *The budget addresses some issues that employers have been asking about, such as simplifying tax compliance for on-demand pay arrangements.*

President Biden's FY2024 budget and its accompanying "Green Book" propose changes of interest to employers and employees. For example, the proposals would make permanent some employer and employee credits while reducing others, such as the work opportunity tax credit (WOTC). In addition, the budget reproposes, from prior budgets, specific tax rules for on-demand pay arrangements and other tax changes that may be of interest to employers.

High-income taxpayers

Medicare: The budget proposes prolonging the Medicare Trust Fund through provisions that include increasing the Medicare tax rate on earned and unearned income above $400,000 from 3.8% to 5%, similarly increasing the Net Investment Income Tax (NIIT) rate to 5% for those above that income threshold, and expanding the tax to include business income, as well as income from investments, wages, and self-employment (effective for tax years beginning after December 31, 2022).

Retirement arrangements: The budget proposes requiring high-income taxpayers who have over $10 million in tax-favored retirement arrangements to distribute a minimum of 50% of that excess in the following calendar year. It would also prohibit Roth conversions by high-income taxpayers (effective for tax years beginning after December 31, 2023). In addition, an IRA could not hold an interest in a domestic international sales corporation (DISC) or foreign sales corporation (FSC) (acquired or held after December 31, 2023) that receives a payment from an entity owned by the IRA owner.

Employer tax credits

Work opportunity tax credit (WOTC): The budget proposes to eliminate the 25% WOTC credit for employers on the qualified wages of eligible individuals who work 120 to 400 hours in their first year of service. Instead, a WOTC of 40% of qualified wages would only be available for individuals who work at least 400 hours in their first year (effective for individuals hired after December 31, 2023).

Tax compliance

"Failed" nonqualified deferred compensation plans: The budget would require employers with "failed" nonqualified deferred compensation (NQDC) arrangements to withhold the 20% additional tax and additional interest tax that must be included in an employee's income when the NQDC arrangement does not meet certain requirements under IRC Section 409A (effective after December 31, 2023).

COVID paid leave and employee retention tax credits: The budget would give the IRS more time to assess erroneous (1) paid leave tax credits under the Families First Coronavirus Response Act of 2020 (FFCRA) and (2) employee retention tax credits, extending the limitations period for all calendar quarters to the five-year period provided for certain calendar quarters under ARPA. The ARPA extension of the limitations period applies only for the second and third quarters of 2021 for the paid leave tax credit and the third and fourth quarters (the fourth quarter ERTC was later repealed) of 2021 for the ERTC (effective on the date of enactment). The proposal would expand this extension to include FFCRA and ERC credits for all quarters. Thus, the limitation period for assessment (but not for filing a claim) would be extended to five years after the later of (1) the filing date of the original return that includes the calendar quarter for which the paid leave credit or ERTC is determined, or (2) "the April 15 date on which the return is treated as filed."

Control of the payment of wage: In response to a recent court decision, the budget would clarify the phrase "control of the payment of wages" to make it consistent with the Administration's understanding of the original legislative history and congressional intent (effective after December 31, 2023).

Tax administration

Fixed indemnity health policies: The budget would amend IRC Section 105(b) to not exclude from gross income a fixed payment to an employee under a fixed indemnity arrangement (if made without regard to the actual cost) and would treat the payment as wages subject to FICA and FUTA taxes. Payments for the specific amount of the medical expense would be excluded from gross income (effective for tax years beginning after December 31, 2023).

Funding post-retirement medical and life insurance benefits: The budget would require post-retirement benefits to be funded over the longer of (1) the working lives of the covered employees on a level basis, or (2) 10 years, unless the employer commits to maintaining those benefits over at least 10 years (effective for tax years beginning after December 31, 2023).

On-demand pay arrangements: The budget would define an on-demand pay arrangement as one that allows employees to withdraw earned wages before their regularly scheduled pay dates and would treat the payroll period for on-demand pay arrangements as a weekly payroll period. The proposal would also amend IRC Sections 3102, 3111, and 3301 to clarify that on-demand pay arrangements are not loans for those federal employment tax purposes (effective for calendar years and quarters beginning after December 31, 2023).

Ernst & Young LLP insights

Those proposals that would increase taxes on high-income taxpayers and lower the WOTC could face challenges in the House while those pertaining to tax compliance might have a better chance of becoming part of a broader tax package.

The budget's commentary about on-demand pay arrangements is virtually identical to the text from last year's budget, but it remains instructive of the IRS's position and the lack of clarity under current law.

Contact us for more information

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