



Alert

Employee Benefits & Executive Compensation
Client Service Group

To: Our Clients and Friends

July 7, 2011

IRS Issues Guidance On Health Plan Excise Tax Returns, Code Section 162(m)

On June 24, 2011, the Internal Revenue Service ("IRS") finalized rules on automatic extensions for Form 8928 Excise Tax Returns for employer-sponsored health plans and also released guidance on performance-based compensation plans of public companies. Highlights follow.

Filing Extensions for Health Plan Excise Tax Returns

An employer or group health plan is required to file an excise tax return on [Form 8928](#) if certain plan failures occur. Such failures include but are not limited to: the failure to satisfy COBRA continuation requirements; the failure to comply with HIPAA portability rules; and the failure to make comparable contributions to employees' health savings accounts. The final regulations regarding excise tax return extensions mirror the prior proposed regulations. Under the new regulations, the IRS will automatically grant a six-month extension if the employer or group health plan:

- files [Form 7004](#), "Application for Automatic Extension of Time to File Certain Business Income Tax, Information, and Other Returns" before the due date of the tax return; and
- remits payment of the estimated tax on or before the date prescribed for payment.

Note, however, that this automatic filing extension does not extend the due date for payment of the applicable excise tax. The estimated tax still must be paid by the applicable due date of the Form 8928 without extension.

Clarifications on Qualified Performance-Based Compensation under Section 162(m)

Under Section 162(m) of the Internal Revenue Code ("Code"), public corporations may not take a federal income tax deduction for payment of certain employee compensation in excess of \$1,000,000. The limitation does not include "qualified performance-based compensation" as described in the regulations.

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The IRS published new proposed regulations regarding “qualified performance-based compensation” exempt from the 162(m) deduction limitation. These regulations clarified that a plan under which stock options or stock appreciation rights are granted must specify the maximum number of shares that may be granted during a specified time period on a per-employee basis. Stating an aggregate maximum number of shares without providing a specific per-employee limitation will disqualify the compensation from being exempt. Similarly, the description of compensation payable under a performance goal that is provided to shareholders must specify the maximum number of shares which may be granted to each individual employee during a specified time period and also the exercise price of those options. These clarifications are effective immediately. While most stock option and stock appreciation rights plans likely already comply with this requirement, employers should review their existing plans to ensure that they incorporate the per-employee limit as described above.

The regulations also clarified a transition rule for privately held companies that then become publicly held corporations. For these transitioning companies, the deduction limit does not apply to compensation paid under a plan that existed when the corporation was not publicly held. This relief applies until the occurrence of the earliest of the following specified events listed in the existing regulations:

- the expiration of the plan or agreement
- the material modification of the plan or agreement
- the issuance of all employer stock and other compensation that has been allocated under the plan
- the first meeting of shareholders at which directors are to be elected that occurs after the close of the third calendar year in which an IPO occurs or, in the case of a privately held corporation that becomes publicly held without an IPO, the first calendar year following the calendar year in which the corporation becomes publicly held

This transition relief applies to any compensation received pursuant to the exercise of a stock option or stock appreciation right, or the substantial vesting of restricted property, granted under an existing plan if the grant occurs on or before the earliest of these four specified events. According to the new proposed regulations, compensation payable under a restricted stock unit arrangement or a phantom stock arrangement must actually be paid, rather than simply granted, before the occurrence of the earliest specified event to be eligible for the transition relief. The clarifications pertaining to the transition rules for privately held companies that then become publicly held corporations are proposed to apply to taxable years ending on or after the date final regulations are published.

If you have any questions regarding anything discussed in this Alert, the attorneys and other professionals of the Employee Benefits and Executive Compensation group of Bryan Cave LLP are available to answer your questions.

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