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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Parts 1 and 602

[TD 9144]

RIN 1545-BA75

Statutory Options; Correction

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Correcting amendment.

SUMMARY: This document corrects final regulations (TD 9144) that were published in the **Federal Register** on Tuesday, August 3, 2004 (69 FR 46401).

The document contains final regulations relating to statutory options. These final regulations affect certain taxpayers who participate in the transfer of stock pursuant to the exercise of incentive stock options and the exercise of options granted pursuant to an employee stock purchase plan (statutory options).

DATES: This document is effective on August 3, 2004.

FOR FURTHER INFORMATION CONTACT: Erinn Madden, (202) 622-6030 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

The final regulations (TD 9144) that is the subject of this correction are under sections 421, 422, and 424 of the Internal Revenue Code.

Need for Correction

As published, the final regulations (TD 9144) contains errors that may prove to be misleading and are in need of clarification.

List of Subjects

26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

26 CFR Part 602

Reporting and recordkeeping requirements.

Correction of Publication

Accordingly, 26 CFR Parts 1 and 602 are is corrected by making the following correcting amendment:

PART 1 – INCOME TAXES

Paragraph 1. The authority citation for part 1 and continues to read in part as follows:

Authority: 26 USC 7805 * * *

§1.421-1 [Corrected]

1. Section 1.421-1(g), fifth sentence, the language “See §1.422-1(b)(3) Example 3.” is removed and the language “See §1.422-1(b)(3) Example 2.” is added in its place.
2. Section 1.421-1(j)(2), third sentence, the language “For statutory options granted after June 9, 2003, and before the earlier of January 1, 2006, or the first regularly scheduled stockholders meeting on the granting corporation occurring 6 month after August 3, 2004, taxpayers may rely on either the REG-122917-02 or this

section.” is removed and the language “For statutory options granted after June 9, 2003, and before the earlier of January 1, 2006, or the first regularly scheduled stockholders meeting of the granting corporation occurring at least 6 months after August 3, 2004, taxpayers may rely on either the REG-122917-02 or this section.” is added in its place.

§1.421-2 [Corrected]

3. Section 1.421-2(f)(2), second sentence, the language “For statutory options granted after June 9, 2003, and before the earlier of January 1, 2006, or the first regularly scheduled stockholders meeting of the granting corporation occurring 6 months after August 3, 2004, taxpayers may rely on either the REG-122917-02 or this section.” is removed and the language “For statutory options granted after June 9, 2003, and before the earlier of January 1, 2006, or the first regularly scheduled stockholders meeting of the granting corporation at least 6 months after August 3, 2004, taxpayers may rely on either the REG-122917-02 or section.” is added in its place.

§1.422-1 [Corrected]

4. Section 1.422-1(b)(3), Example 2, fourth sentence, the language “Additionally, at the time of the disposition, section 422 and §1.422-1(a) no longer apply, and thus, section 83(a) is used to measure the consequences of the disposition.” is removed and the language “Additionally, at the time of the disposition, section 422 and §1.422-1a) no longer apply, and thus, section 83(a) is used to measure the consequences of the disposition and the holding period for capital gain purposes begin on the vesting date, six months after exercise.” is added in its place.

§1.422-5 [Corrected]

5. Section 1.422-5(e), tenth sentence, the language “Under the rules of paragraph (b)(3) of this section, A has sold all 60 of the non-section-1036 shares and 15 of the 40 section-1036 shares.” is removed and the language “Under the rules of paragraph (b)(2) and (b)(3) of this section, A has sold all 60 of the non-section-1036 shares and 15 of the 40 section-1036 shares.” is added in its place.

6. Section 1.422-5(f)(2), third sentence, the language “For statutory options granted after June 9, 2003, and before the earlier of January 1, 2006, or the first regularly scheduled stockholders meeting of the granting corporation occurring 6 months after August 3, 2004, taxpayers may rely on either the REG-122917-02 or this section.” is removed and the language “For statutory options granted after June 9, 2003, and before the earlier of January 1, 2006, or the first regularly scheduled stockholders meeting of the granting corporation occurring at least 6 months after August 3, 2004, taxpayers may rely on either the REG-122917-02 or this section.” is added in its place.

§1.424-1 [Corrected]

7. Section 1.424-1(a)(3)(ii), first sentence, the language “A distribution (excluding an ordinary dividend or a stock split or stock dividend described in §1.424-1(e)(v)) or change in the terms or number of outstanding shares of such corporation; and” is removed and the language “A distribution (excluding an ordinary dividend or a stock split or stock dividend described in §1.424-1(e)(4)(v)) or change in the terms or number of outstanding shares of such corporation; and” is added in its place.

8. Section 1.424-1(a)(10), Example 8, sixth sentence, the language “Based on these facts, a new option to purchase 200 shares of Y at an option price of \$25 per share could be granted to E in complete substitution of E’s old option.” is removed and

the language “Based on these facts, and new option to purchase 200 shares of Y at an option price of \$25 per share could be granted to E in complete substitution of E’s old option. In the alternative, it would also be permissible in connection with the spin off, to grant E a new option to purchase 100 shares of Y, at an option price of \$25 per share, and E retains an option to purchase 100 shares of X under the old option, with the option price adjusted to \$25. However, because X is no longer a related corporation with respect to Y, E must exercise the option for 100 shares of X within three months from the date of the spin off for the option to be treated as a statutory option. See §1.421-1(h).” is added in its place.

9. Section 1.424-1(a)(10), paragraph (iii) of Example 9, third sentence, the language “Because the amendment of the plan to allow options on a different stock is considered the adoption of a new plan under §1.422-2(b)(2)(iii), the stockholders of X must approve the plan within 12 months before or after the date of the amendment of the plan.” is removed and the language “Because the amendment of the plan to allow options on a different stock is considered the adoption of a new plan under §1.422-2(b)(2)(iii), the stockholders of Y must approve the plan within 12 months before or after the date of the amendment of the plan.” is added in its place.

10. Section 1.424-1(a)(10), paragraph (iii) of Example 9, fourth sentence, the language “If the stockholders of X timely approve the plan, the future grants to acquire Y stock will be incentive stock options (assuming the other requirements of §1.422-2 have been met).” is removed and the language “If the stockholders of Y timely approve the plan, the future grants to acquire Y stock will be incentive stock options (assuming the other requirements of §1.422-2 have been met).” is added in its place.

11. Section 1.424-1(c)(4)(vi), the last sentence is removed.

12. Section 1.424-1(c)(4)(viii), second sentence, the language “Thus, for example, if the terms of an option are inadvertently changed on March 1 to extend the exercise period and the change is removed on November, then if the option is not exercised prior to November 1, the option is not considered modified under this paragraph (e).” is removed and the language “Thus for example, if the terms of an option are inadvertently changed on March 1 to extend the exercise period and the change is removed on November 1, then if the option is not exercised prior to November 1, the option is not considered modified under this paragraph (e).” is added in its place.

13. Section 1.424-1(g)(2), third sentence, the language “For statutory options granted after June 9, 2003, and before the earlier of January 1, 2006, or the first regularly scheduled stockholders meeting of the granting corporation occurring 6 months after August 3, 2004, taxpayers may rely on either the REG-122917-02 or this section.” is removed and the language “For statutory options granted after June 9, 2003, and before the earlier of January 1, 2006, or the first regularly scheduled stockholders meeting of the granting corporation occurring at least 6 months after August 3, 2004, taxpayers may rely on either the REG-122917-02 or this section.” is added in its place.

§1.6039-1 [Corrected]

14. Section 1.6039-1(g)(2), second sentence, the language “For statutory options transferred after June 9, 2003, and before the earlier of January 1, 2006, or the first regularly scheduled stockholders meeting of the granting corporation occurring 6 months after August 3, 2004, taxpayers may rely on either REG-122917-02 or

this section.” is removed and the language “For statutory options transferred after June 9, 2003, and before the earlier of January 1, 2006, or the first regularly scheduled stockholders meeting of the granting corporation occurring at least 6 months after August 3, 2004, taxpayers may rely on either REG-122917-02 or this section.” is added in its place.

PART 602-- OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 2. The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

§602.101 [Corrected]

15. Section 602.101(b) is amended by adding the entry “1.422-1 1545-0820” to the table in numerical order.

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