

LUSE GORMAN POMERENK & SCHICK

A PROFESSIONAL CORPORATION
ATTORNEYS AT LAW

5335 WISCONSIN AVENUE, N.W., SUITE 780 ■ WASHINGTON, D.C. 20015 ■ 202.274.2000 T ■ 202.362.2902 F ■ WWW.LUSELAW.COM

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NEW IRS REPORTING RULES FOR INCENTIVE STOCK OPTIONS

The Internal Revenue Service (the “IRS”) has adopted final reporting rules (the “Final Rules”) that will require employers to file a new form with the IRS, Form 3921, to report information regarding exercises of incentive stock options (“ISOs”). The requirement to file Form 3921 with the IRS will be effective with respect to ISOs exercised on or after January 1, 2010 and the new Form 3921 must be filed by January 31 of the following year. The IRS presently requires employers to provide information statements to employees who exercised ISOs during the prior calendar year. The Final Rules also changed employers’ reporting obligations for employee stock purchase plans (“ESPPs”) (not to be confused with employee stock ownership plans (“ESOPs”), which are not subject to these rules). These rules do not apply to nonqualified stock options, restricted stock or restricted stock units. ***Therefore, by January 31, 2010, employers are only required to provide information statements to employees who exercised ISOs during 2009.***

The Final Rules are intended to give employees more accurate information to enable them to calculate their tax obligations upon the disposition of shares acquired upon the exercise of an ISO. The information statement to be given to employees for 2009 ISO exercises must include the following:

- (a) Employer’s name, address and employer identification number (“EIN”);
- (b) Issuer’s name, address and EIN (if different from the employer; for example, the bank is the employer and the holding company is the issuer);
- (c) Name, address and Social Security Number (“SSN”) of the person to whom the shares of stock were transferred pursuant to the ISO exercise (but for privacy reasons, the SSN can be limited to the last four digits);
- (d) ISO grant date;
- (e) Exercise price per share;
- (f) Exercise date;

(g) Fair market value of a share of stock on the ISO exercise date; and

(h) Number of shares transferred pursuant to the ISO exercise.

The Final Rules do not require that this information include a statement that the shares issued were acquired upon the exercise of an ISO (but we recommend that such a statement be included). There is no particular form for providing this information, so the employer can type the information up on a plain sheet of paper or on letterhead. The statement can be given in person or mailed to the employee’s last known address, but these statements are ***not*** filed with the IRS. The statements can be sent by email only if the employee has properly consented to such means of delivery (*i.e.*, the individual affirmatively consents in a manner that demonstrates that the individual can access the same electronic format in which the notice is furnished). Under the Final Rules, information statements are generally not required to be given to non-resident aliens.

Failure to provide the notice may result in a penalty of \$50 for each information statement that is not timely furnished or that contains incomplete or inaccurate information, up to a maximum of \$100,000 per calendar year. Note that the information statement is in addition to other reporting requirements that arise upon the “disqualifying disposition” of stock acquired upon the exercise of an ISO. Specifically, upon a disqualifying disposition, the difference between the exercise price and the fair market value of the stock must be included as “other compensation” on Form W-2. If the employee does not make a “disqualifying disposition,” then W-2 reporting is not required.

Please contact any of the attorneys below if you need help with preparing the information statements that must be given to employees by January 31, 2010, with respect to 2009 ISO exercises, or if you have any executive compensation or employee benefits questions.

Beverly J. White ■ (202) 274-2005

Norma Sharara ■ (202) 274-2035

Max Seltzer ■ (202) 274-2038