

Section 162(m) Transition Relief May Be Expiring for 2010 Performance-Based Compensation

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In 2008, the IRS issued a ruling limiting the deductibility of certain incentive compensation under Section 162(m) of the Internal Revenue Code.

The IRS ruling applies to any incentive compensation plan permitting payment to be made or providing for accelerated vesting without regard to actual performance upon the occurrence of one of the following events: a covered employee's involuntary termination, good reason termination or retirement. Reversing its earlier position on the matter, the IRS ruled that an incentive compensation plan providing for payment or vesting upon such an event fails to provide for deductible "performance-based compensation" under Section 162(m) – even if the event does not occur and the employee is paid or vests based on the satisfaction of the relevant performance goals.

The IRS provided transition relief allowing employers to delay amending their existing incentive compensation plans if either: (1) the incentive compensation performance period began on or before January 1, 2009; or (2) the incentive compensation is payable pursuant to an employment contract as in effect on February 21, 2008 (without regard to future renewals or extensions, including renewals or extensions that occur automatically).

For many employers, this transition relief is expiring.

To preserve a deduction under Section 162(m), publicly held corporations should ensure that their incentive compensation plans do not include any of the features described above if:

- Amounts are payable for performance periods beginning on or before January 1, 2010; or
- Amounts are payable under employment agreements that were renewed or extended after February 21, 2008.

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