

## Executive Compensation Alert:

### 162(m) and Treatment of Dividends and Dividend Equivalents-IRS Clarifies

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Earlier this summer, the Internal Revenue Service issued Revenue Ruling 2012-19 to clarify the treatment of dividends and dividend equivalents on equity that qualifies as performance-based compensation under Section 162(m) of the Internal Revenue Code of 1986, as amended (the “Code”). A copy of the ruling can be found here: <http://www.irs.gov/pub/irs-drop/rr-12-19.pdf>.

#### Background

Section 162(m) of the Code provides that a publicly held corporation may not deduct certain remuneration to any covered employee to the extent that the total remuneration for the taxable year exceeds \$1,000,000. A covered employee is typically the corporation’s chief executive officer and the other four most highly compensated officers.

However, the \$1 million deduction limit does not apply to “qualified performance-based compensation.” A corporation may deduct remuneration to a covered employee that is payable solely on account of the attainment of one or more pre-established objective performance goals.

#### Revenue Ruling

Revenue Ruling 2012-19 clarifies that if dividends and dividend equivalents are issued with respect to restricted stock and restricted stock units (“RSUs”) that qualify as performance-based compensation, such dividends must independently qualify as performance based compensation or otherwise be contingent upon achievement of the performance goals applicable to the restricted stock or RSUs.

The Revenue Ruling provides that dividends and dividend equivalents are “grants of compensation that are separate and apart” from the performance-based restricted stock and RSU grants on which they are issued. Since the IRS views the dividends and dividend equivalents as separate compensation, the dividends or their equivalents must either independently qualify as performance-based compensation or vest and become payable only upon the achievement of the performance goals applicable to the restricted stock or RSUs on which such dividends are paid.

**For more information, you may contact any attorney in the Executive Compensation and Employee Benefits Group at Fenwick & West LLP.**

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