SIMPSON THACHER

MEMORANDUM

IRS Adopts New Form for U.S. Persons with Foreign-Source Deferred Compensation, Retirement Benefits or Equity Based-Awards and Other Specified Non-U.S. Financial Assets

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As a result of the implementation of anti-tax evasion provisions of the Foreign Account Tax Compliance Act ("FATCA"), U.S. persons with certain types of foreign compensation arrangements or other foreign assets may be required to include a new tax form with their federal tax returns for tax years beginning after March 18, 2010. This Form 8938, Statement of Specified Foreign Financial Assets,[1] is required to be filed by U.S. taxpayers holding minimum amounts of "foreign financial assets." The term "foreign financial assets" is defined broadly to include many arrangements not commonly considered "assets," including, among other things, deferred compensation or retirement arrangements, stock options, restricted stock units and profits interests, as well as stock and derivative securities. In addition, domestic "financial assets" may trigger the reporting requirement if payment is guaranteed by a non-U.S. entity.

A brief summary of this filing requirement is set forth below. We encourage employers with these types of non-U.S. arrangements to remind their employees and partners to discuss this filing requirement with their tax professionals, as failure to comply may result in penalties to the taxpayer.

AFFECTED INDIVIDUALS AND MINIMUM ASSET VALUE THRESHOLDS

For purposes of FATCA reporting, individuals who are U.S. citizens, U.S. resident aliens, and certain other limited categories of non-resident aliens, who file a U.S. tax return are specified as individuals required to report their "foreign financial assets" (described more fully below) on Form 8938 if such assets meet certain thresholds.

For married U.S. residents filing joint tax returns, the aggregate asset value must be more than $100,000 on the last day of a given tax year or more than $150,000 on any day during a given tax year in order to trigger a Form 8938 filing for such year. The thresholds increase to $400,000 and $600,000, respectively, for married U.S. taxpayers filing joint tax returns and living abroad.

For unmarried U.S. residents and married U.S. residents filing separate tax returns, the aggregate asset value must be more than $50,000 on the last day of a given tax year or more

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1 This form, together with the instructions for completing it, can be found at http://www.irs.gov/pub/irs-pdf/f8938.pdf and http://www.irs.gov/pub/irs-pdf/i8938.pdf.

than $75,000 on any day during a given tax year in order to trigger a Form 8938 filing for such year. The thresholds increase to $200,000 and $300,000, respectively, for those living abroad. The instructions to Form 8938 indicate that an individual satisfies the test for "living abroad" if such individual is a U.S. citizen who either (i) has been a bona fide resident of a foreign country for an uninterrupted period that includes an entire tax year, or (ii) is present in a foreign country at least 330 full days during any period of 12 consecutive months that ends in the tax year being reported.

TYPES OF ARRANGEMENTS COVERED

"Foreign financial assets" include (i) stock or securities issued by someone other than a U.S. entity, (ii) any interest in a foreign entity, and (iii) any financial instrument or contract that has an issuer or counterparty that is not a U.S. entity. Therefore, individuals who are U.S. taxpayers and participate in equity-based award programs and retirement and deferred compensation arrangements of non-U.S. entities are now subject to this new reporting requirement, subject to the minimum asset value thresholds described above.

Some of these affected arrangements include:

- Restricted stock or other equity units, stock or unit options, capital or profits interests in partnerships or limited liability companies, phantom stock or other equity-based awards or derivative securities where the applicable equity security is that of a non-U.S. entity;

- Unfunded deferred compensation arrangements (including supplemental retirement plans and guarantees) for which any non-U.S. entity has the obligation to make payments to participants;

- Funded non-U.S. retirement plans; and

- Any amounts held in foreign financial institutions.[2]

The instructions to Form 8938 provide specific rules for valuing deferred compensation accounts and funded retirement benefits, while generally providing that assets such as equity-based awards are to be valued at "fair market value" as of the end of the applicable tax year. No official guidance has been provided as yet with regard to how vesting conditions that may be applicable to compensatory arrangements may affect valuation. However, the IRS has unofficially indicated that, with respect to unvested stock options, for example, a prudent

[2] The instructions to Form 8938 indicate that a foreign financial institution is any financial institution that is not a U.S. entity and satisfies one or more of the following: (i) it accepts deposits in the ordinary course of a banking or similar business, (ii) it holds financial assets for the account of others as a substantial part of its business, or (iii) it is engaged primarily in the business of investing, reinvesting or trading in securities, partnership interests, commodities or any interest in the foregoing. A foreign financial institution also includes investment vehicles such as foreign mutual funds, hedge funds and private equity funds.

position for the taxpayer would be to report such options as foreign financial assets on Form 8938 and treat them as having a zero dollar value.

POTENTIAL PENALTIES

Failure to file a complete and correct Form 8938 with a tax return may result in a penalty of $10,000, with a maximum additional penalty of $50,000 for a continuing failure to file after the IRS notifies the subject individual of a filing deficiency.

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For more information about this new filing requirement, please contact a member of the Firm's Executive Compensation and Employee Benefits Practice Group.

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