EFFECTIVE DATE

Section 251(c) of Pub. L. 97–34, as amended by Pub. L. 99–514, § 2, Oct. 22, 1986, 100 Stat. 2095, provided that:

''(1) OPTIONS TO WHICH SECTION APPLIES.—

''(A) IN GENERAL.—Except as provided in subparagraph (B), the amendments made by this section [enacting this section and amending sections 421, 425 [now 424], and 6039 of this title] shall apply with respect to options granted on or after January 1, 1976, and exercised on or after January 1, 1981, or outstanding on such date.

''(B) ELECTION AND DESIGNATION OF OPTIONS.—In the case of an option granted before January 1, 1981, the amendments made by this section shall apply only if the corporation granting such option elects (in the manner and at the time prescribed by the Secretary of the Treasury or his delegate) to have the amendments made by this section apply to such option. The aggregate fair market value (determined at the time the option is granted) of the stock for which any employee was granted options (under all plans of his employer corporation and its parent and subsidiary corporations) to which the amendments made by this section apply by reason of this subparagraph shall not exceed $50,000 per calendar year ans shall not exceed $200,000 in the aggregate.

''(2) CHANGES IN TERMS OF OPTIONS.—In the case of an option granted on or after January 1, 1976, and outstanding on the date of the enactment of this Act [Aug. 13, 1981], paragraph (1) of section 425(h) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954] shall not apply to any change in the terms of such option (or the terms of the plan under which granted, including shareholder approval) made within 1 year after such date of enactment to permit such option to qualify as a incentive stock option.''

SAVINGS PROVISION

For provisions that nothing in amendment by Pub. L. 101–508 be construed to affect treatment of certain transactions occurring, property acquired, or items of income, loss, deduction, or credit taken into account prior to Nov. 5, 1990, for purposes of determining liability for tax for periods ending after Nov. 5, 1990, see section 11821(b) of Pub. L. 101–508, set out as a note under section 45K of this title.

TREATMENT OF OPTIONS AS INCENTIVE STOCK OPTIONS

Section 1003(d)(1)(B) of Pub. L. 100–647 provided that: ''In the case of an option granted after December 31, 1986, and on or before the date of the enactment of this Act [Nov. 10, 1988], such option shall not be treated as an incentive stock option if the terms of such option are amended before the date 90 days after such date of enactment to provide that such option will not be treated as an incentive stock option.''

PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§ 1101–1147 and 1171–1177] or title XVIII [§§ 1800–1899A] of Pub. L. 99–514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99–514, as amended, set out as a note under section 401 of this title.

[§ 422A. Renumbered § 422]

§ 423. Employee stock purchase plans

(a) General rule

Section 421(a) shall apply with respect to the transfer of a share of stock to an individual pursuant to his exercise of an option granted after December 31, 1963, under an employee stock purchase plan (as defined in subsection (b)) if—

(1) no disposition of such share is made by him within 2 years after the date of the granting of the option nor within 1 year after the transfer of such share to him; and

(2) at all times during the period beginning with the date of the granting of the option and ending on the day 3 months before the date of such exercise, he is an employee of the corporation granting such option, a parent or subsidiary corporation of such corporation, or a corporation or a parent or subsidiary corporation of such corporation issuing or assuming a stock option in a transaction to which section 424(a) applies.

(b) Employee stock purchase plan

For purposes of this part, the term ''employee stock purchase plan'' means a plan which meets the following requirements:

(1) the plan provides that options are to be granted only to employees of the employer corporation or of its parent or subsidiary corporation to purchase stock in any such corporation;

(2) such plan is approved by the stockholders of the granting corporation within 12 months before or after the date such plan is adopted;

(3) under the terms of the plan, no employee can be granted an option if such employee, immediately after the option is granted, owns stock possessing 5 percent or more of the total combined voting power or value of all classes of stock of the employer corporation or of its parent or subsidiary corporation. For purposes of this paragraph, the rules of section 424(d) shall apply in determining the stock ownership of an individual, and stock which the employee may purchase under outstanding options shall be treated as stock owned by the employee;

(4) under the terms of the plan, options are to be granted to all employees of any corporation whose employees are granted any of such options by reason of their employment by such corporation, except that there may be excluded—

(A) employees who have been employed less than 2 years,

(B) employees whose customary employment is 20 hours or less per week,

(C) employees whose customary employment is for not more than 5 months in any calendar year, and

(D) highly compensated employees (within the meaning of section 414(q));

(5) under the terms of the plan, all employees granted such options shall have the same rights and privileges, except that the amount of stock which may be purchased by any employee under such option may bear a uniform relationship to the total compensation, or the basic or regular rate of compensation, of employees, and the plan may provide that no employee may purchase more than a maximum amount of stock fixed under the plan;

(6) under the terms of the plan, the option price is not less than the lesser of—

(A) an amount equal to 85 percent of the fair market value of the stock at the time such option is granted, or

(B) an amount which under the terms of the option may not be less than 85 percent of

the fair market value of the stock at the time such option is exercised;

(7) under the terms of the plan, such option cannot be exercised after the expiration of—

(A) 5 years from the date such option is granted if, under the terms of such plan, the option price is to be not less than 85 percent of the fair market value of such stock at the time of the exercise of the option, or

(B) 27 months from the date such option is granted, if the option price is not determinable in the manner described in subparagraph (A)

(8) under the terms of the plan, no employee may be granted an option which permits his rights to purchase stock under all such plans of his employer corporation and its parent and subsidiary corporations to accrue at a rate which exceeds $25,000 of fair market value of such stock (determined at the time such option is granted) for each calendar year in which such option is outstanding at any time. For purposes of this paragraph—

(A) the right to purchase stock under an option accrues when the option (or any portion thereof) first becomes exercisable during the calendar year;

(B) the right to purchase stock under an option accrues at the rate provided in the option, but in no case may such rate exceed $25,000 of fair market value of such stock (determined at the time such option is granted) for any one calendar year; and

(C) a right to purchase stock which has accrued under one option granted pursuant to the plan may not be carried over to any other option; and

(9) under the terms of the plan, such option is not transferable by such individual otherwise than by will or the laws of descent and distribution, and is exercisable, during his lifetime, only by him.

For purposes of paragraphs (3) to (9), inclusive, where additional terms are contained in an offering made under a plan, such additional terms shall, with respect to options exercised under such offering, be treated as a part of the terms of such plan.

(c) Special rule where option price is between 85 percent and 100 percent of value of stock

If the option price of a share of stock acquired by an individual pursuant to a transfer to which subsection (a) applies was less than 100 percent of the fair market value of such share at the time such option was granted, then, in the event of any disposition of such share by him which meets the holding period requirements of subsection (a), or in the event of his death (whenever occurring) while owning such share, there shall be included as compensation (and not as gain upon the sale or exchange of a capital asset) in his gross income, for the taxable year in which falls the date of such disposition or for the taxable year closing with his death, whichever applies, an amount equal to the lesser of—

(1) the excess of the fair market value of the share at the time of such disposition or death over the amount paid for the share under the option, or

(2) the excess of the fair market value of the share at the time the option was granted over the option price.

If the option price is not fixed or determinable at the time the option is granted, then for purposes of this subsection, the option price shall be determined as if the option were exercised at such time. In the case of the disposition of such share by the individual, the basis of the share in his hands at the time of such disposition shall be increased by an amount equal to the amount so includible in his gross income. No amount shall be required to be deducted and withheld under chapter 24 with respect to any amount treated as compensation under this subsection.

(Added Pub. L. 88–272, title II, §221(a), Feb. 26, 1964, 78 Stat. 67; amended Pub. L. 94–455, title XIV, §1402(b)(1)(E), (2), Oct. 4, 1976, 90 Stat. 1732; Pub. L. 98–369, div. A, title X, §1001(b)(5), (e), July 18, 1984, 98 Stat. 1011, 1012; Pub. L. 99–514, title XI, §1114(b)(13), Oct. 22, 1986, 100 Stat. 2451; Pub. L. 101–508, title XI, §11801(c)(9)(D), (E), Nov. 5, 1990, 104 Stat. 1388–525; Pub. L. 108–357, title II, §251(c), Oct. 22, 2004, 118 Stat. 1459.)

AMENDMENTS

2004—Subsec. (c). Pub. L. 108–357 inserted at end of concluding provisions ''No amount shall be required to be deducted and withheld under chapter 24 with respect to any amount treated as compensation under this subsection.''

1990—Subsec. (a). Pub. L. 101–508, §11801(c)(9)(D)(i), struck out ''(other than a restricted stock option granted pursuant to a plan described in section 424(c)(3)(B))'' after ''December 31, 1963''.

Subsec. (a)(2). Pub. L. 101–508, §11801(c)(9)(D)(ii), substituted ''424(a)'' for ''425(a)''.

Subsec. (b)(3). Pub. L. 101–508, §11801(c)(9)(E), substituted ''424(d)'' for ''425(d)''.

1986—Subsec. (b)(4)(D). Pub. L. 99–514 substituted ''highly compensated employees (within the meaning of section 414(q))'' for ''officers, persons whose principal duties consist of supervising the work of other employees, or highly compensated employees''.

1984—Subsec. (a)(1). Pub. L. 98–369 substituted ''6 months'' for ''1 year'', applicable to property acquired after June 22, 1984, and before Jan. 1, 1988. See Effective Date of 1984 Amendment note below.

1976—Subsec. (a)(1). Pub. L. 94–455, §1402(b)(2), provided that ''9 months'' would be changed to ''1 year''.

Pub. L. 94–455, §1402(b)(1)(E), provided that ''6 months'' would be changed to ''9 months'' for taxable years beginning in 1977.

EFFECTIVE DATE OF 2004 AMENDMENT

Amendment by Pub. L. 108–357 applicable to stock acquired pursuant to options exercised after Oct. 22, 2004, see section 251(d) of Pub. L. 108–357, set out as a note under section 421 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by Pub. L. 99–514 applicable to years beginning after Dec. 31, 1986, see section 1114(c)(1) of Pub. L. 99–514, set out as a note under section 414 of this title.

EFFECTIVE DATE OF 1984 AMENDMENT

Amendment by Pub. L. 98–369 applicable to property acquired after June 22, 1984, and before Jan. 1, 1988, see section 1001(e) of Pub. L. 98–369, set out as a note under section 166 of this title.

EFFECTIVE DATE OF 1976 AMENDMENT

Section 1402(b)(1) of Pub. L. 94–455 provided that the amendment made by that section is effective with respect to taxable years beginning in 1977.

Section 1402(b)(2) of Pub. L. 94–455 provided that the amendment made by that section is effective with respect to taxable years beginning after Dec. 31, 1977.

EFFECTIVE DATE

Section applicable to taxable years ending after Dec. 31, 1963, see section 221(e) of Pub. L. 88–272, set out as an Effective Date of 1964 Amendment note under section 421 of this title.

REGULATIONS

Secretary of the Treasury or his delegate to issue before Feb. 1, 1988, final regulations to carry out amendments made by section 1114 of Pub. L. 99–514, see section 1141 of Pub. L. 99–514, set out as a note under section 401 of this title.

SAVINGS PROVISION

For provisions that nothing in amendment by Pub. L. 101–508 be construed to affect treatment of certain transactions occurring, property acquired, or items of income, loss, deduction, or credit taken into account prior to Nov. 5, 1990, for purposes of determining liability for tax for periods ending after Nov. 5, 1990, see section 11821(b) of Pub. L. 101–508, set out as a note under section 45K of this title.

PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§ 1101–1147 and 1171–1177] or title XVIII [§§ 1800–1899A] of Pub. L. 99–514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99–514, as amended, set out as a note under section 401 of this title.

§ 424. Definitions and special rules

(a) Corporate reorganizations, liquidations, etc.

For purposes of this part, the term ''issuing or assuming a stock option in a transaction to which section 424(a) applies'' means a substitution of a new option for the old option, or an assumption of the old option, by an employer corporation, or a parent or subsidiary of such corporation, by reason of a corporate merger, consolidation, acquisition of property or stock, separation, reorganization, or liquidation, if—

(1) the excess of the aggregate fair market value of the shares subject to the option immediately after the substitution or assumption over the aggregate option price of such shares is not more than the excess of the aggregate fair market value of all shares subject to the option immediately before such substitution or assumption over the aggregate option price of such shares, and

(2) the new option or the assumption of the old option does not give the employee additional benefits which he did not have under the old option.

For purposes of this subsection, the parent-subsidiary relationship shall be determined at the time of any such transaction under this subsection.

(b) Acquisition of new stock

For purposes of this part, if stock is received by an individual in a distribution to which section 305, 354, 355, 356, or 1036 (or so much of section 1031 as relates to section 1036) applies, and such distribution was made with respect to stock transferred to him upon his exercise of the option, such stock shall be considered as having been transferred to him on his exercise of such option. A similar rule shall be applied in the case of a series of such distributions.

(c) Disposition

(1) In general

Except as provided in paragraphs (2), (3), and (4), for purposes of this part, the term ''disposition'' includes a sale, exchange, gift, or a transfer of legal title, but does not include—

(A) a transfer from a decedent to an estate or a transfer by request or inheritance;

(B) an exchange to which section 354, 355, 356, or 1036 (or so much of section 1031 as relates to section 1036) applies; or

(C) a mere pledge or hypothecation.

(2) Joint tenancy

The acquisition of a share of stock in the name of the employee and another jointly with the right of survivorship or a subsequent transfer of a share of stock into such joint ownership shall not be deemed a disposition, but a termination of such joint tenancy (except to the extent such employee acquires ownership of such stock) shall be treated as a disposition by him occurring at the time such joint tenancy is terminated.

(3) Special rule where incentive stock is acquired through use of other statutory option stock

(A) Nonrecognition sections not to apply

If—

(i) there is a transfer of statutory option stock in connection with the exercise of any incentive stock option, and

(ii) the applicable holding period requirements (under section 422(a)(1) or 423(a)(1)) are not met before such transfer,

then no section referred to in subparagraph (B) of paragraph (1) shall apply to such transfer.

(B) Statutory option stock

For purpose of subparagraph (A), the term ''statutory option stock'' means any stock acquired through the exercise of an incentive stock option or an option granted under an employee stock purchase plan.

(4) Transfers between spouses or incident to divorce

In the case of any transfer described in subsection (a) of section 1041—

(A) such transfer shall not be treated as a disposition for purposes of this part, and

(B) the same tax treatment under this part with respect to the transferred property shall apply to the transferee as would have applied to the transferor.

(d) Attribution of stock ownership

For purposes of this part, in applying the percentage limitations of sections 422(b)(6) and 423(b)(3)—

(1) the individual with respect to whom such limitation is being determined shall be considered as owning the stock owned, directly or indirectly, by or for his brothers and sisters