



AMERICAN BENEFITS COUNCIL

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TALKING POINTS: WAYS AND MEANS PROVISION ON OFFSHORE NONQUALIFIED DEFERRED COMPENSATION

The Energy and Tax Extenders Act of 2008 (H.R. 6049), as approved by the Ways and Means Committee on May 15, would require that amounts deferred under nonqualified deferred compensation plans maintained by certain foreign entities be included in income when there is no substantial risk of forfeiture with respect to the compensation (i.e., upon vesting). The provision would apply in addition to Code section 409A and longstanding general tax principles.

Although the provision is apparently targeted at hedge fund managers operating in offshore tax havens, its scope is much broader and it likely would apply in many instances where a U.S. taxpayer works overseas for a U.S. multinational. Moreover, the provision inexplicably treats performance-based compensation and various types of equity compensation as nonqualified deferred compensation -- even where such compensation is not considered nonqualified deferred compensation under section 409A -- and would apply an interest charge and 20 percent penalty to performance-based compensation.

This provision should be rejected for the following reasons:

- **It is extremely broad and would apply to non-abusive compensation practices.** The provision could apply to various types of compensation paid by a foreign company -- including a foreign subsidiary of a U.S. multinational -- to U.S. taxpayers working outside the U.S. In many instances, compensation paid to U.S. taxpayers working in a foreign country must be paid by an entity established in that country in order to satisfy local laws and regulations.
- **It targets equity compensation.** The provision's expanded definition of nonqualified deferred compensation would apply to stock appreciation rights (SARs) issued at fair market value and restricted stock units (RSUs) that pay out upon (or shortly after) vesting, both of which are exempt from section 409A. It is not clear what policy rationale is served by effectively outlawing these non-abusive forms of equity compensation in companies/countries subject to the provision.

- **It targets performance-based compensation.** The proposal would apply to performance-based programs that are exempt from section 409A because any bonus is paid shortly after the performance conditions are satisfied. Moreover, the proposal would impose an interest charge and a 20 percent penalty on amounts that are not reasonably determinable at the time of vesting, including where a performance bonus is not determinable because it is dependent upon the satisfaction of pre-established, objective performance criteria. It is not clear what policy rationale is served by effectively outlawing pay-for-performance programs in companies/countries subject to the provision.
- **It would create great uncertainty and would be virtually impossible to administer.** To determine whether the provision applies, a company would need to (among other things) determine whether:
 - internationally mobile U.S. taxpayers are paid by a foreign company,
 - any such compensation is deferred compensation under the very broad definition in the provision, and
 - substantially all of the income of the foreign company paying the compensation is subject to a comprehensive tax treaty and, if not, whether the IRS might eventually determine that the country otherwise has a "comprehensive income tax."
- **It is retroactive.** Apparently to force more revenue into the 10-year budget window, the provision would apply even to amounts deferred for services performed before 2009 to the extent the amounts are not otherwise included in income before 2018.