
IRS Revenue Ruling under Internal Revenue Code Section 162(m) Upholds Private Letter Ruling but Grants Transition Relief

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On February 21, 2008, the Internal Revenue Service ("IRS") issued a revenue ruling upholding the position it had taken in a private letter ruling released on January 25, 2008 relating to the "performance-based" compensation exception to the \$1 million cap on deductible compensation under Section 162(m) of the Internal Revenue Code of 1986, as amended (the "Code"). Under this revenue ruling, compensation would not be considered "performance-based" for purposes of Section 162(m) of the Code if the plan or agreement under which the compensation is paid provides that the compensation will be paid without regard to whether the performance goal is attained in either of the following situations: (i) the employee's employment is involuntarily terminated by the employer without cause or the employee terminates his or her employment for good reason, or (ii) the employee retires. This holding differs from the position taken by the IRS in two earlier private letter rulings. While a private letter ruling applies only to the taxpayer who requested that ruling, a revenue ruling has general applicability. In recognition of the fact that many employers have designed their plans and agreements in light of the position taken by the IRS in the earlier private letter rulings, the new revenue ruling contains broad transition relief (described on the last page of this memorandum).