

## **IRS PROPOSES REGULATIONS ON SUBSTANTIAL RISK OF FORFEITURE**

Jun 11, 2012

The IRS has released proposed regulations under Section 83 of the Internal Revenue Code to refine the concept of what constitutes a substantial risk of forfeiture for the purpose of narrowing the scope of the concept.

The proposed regulations are in response to case law, tracing back as far as 1986, which the IRS claims has created confusion over the appropriate elements of what may constitute a substantial risk of forfeiture.

In the proposed regulations, the IRS clarifies that a substantial risk of forfeiture may be established only through (1) a service condition or (2) a condition related to the purpose of the transfer, such as a performance condition relating to the services provided by a service provider. In addition, the proposed regulations further clarify that in determining whether a substantial forfeiture exists based on a condition is related to the purpose of the transfer, both the likelihood that the forfeiture event will occur and the likelihood that the forfeiture will be enforced must be considered.

The IRS emphasizes in the proposed regulations that transfer restrictions do not create a substantial risk of forfeiture, such as lock-up agreements or restrictions related to insider trading. However, the IRS acknowledges that the statutory exception related to potential short-swing profits liability under Section 16(b) of the Securities Exchange Act does delay taxation under Section 83.

The IRS appears to be laying the groundwork for the anticipated issuance of new regulations under Section 457 of the Internal Revenue Code, which incorporates the same concept of a substantial risk of forfeiture. While we are not aware of any statements by IRS officials to that effect, it is one possible explanation why the IRS did not address an issue from 1986 until now.

The proposed regulations, if finalized, will apply to transfers of property occurring on and after January 1, 2013.

## MEET THE TEAM



**Richard L. Arenburg**

Atlanta

[richard.arenburg@bclplaw.com](mailto:richard.arenburg@bclplaw.com)

+1 404 572 6765