CHECKPOINT LEARNING

CPE NETWORK TAX REPORT

JUNE 2024

VOLUME 37, ISSUE 5

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• Experts Forum



EXECUTIVE SUMMARY

PART 1. CURRENT DEVELOPMENTS

The tax landscape is ever changing with new court cases, IRS actions, and sometimes, legislation. Practitioners need to be cognizant of changes to properly advise clients. This material covers some changes since last month. [Running time: 36:30]

Learning Objective:

Upon completion of this segment, the user should be able to understand a variety of current tax issues including: (1) identifying phishing and smishing; (2) determining how to report phishing or smishing to the IRS; and (3) assess fake charities.

PART 2. INDIVIDUAL TAXATION

Stock Incentive Plans: Part II17

Incentive stock options are one means of compensating employees. They are particularly popular with start up organizations who may not be flush with cash at the beginning. There are several different types of stock incentive plans, most of which are intended to retain key employees. In this second part of the discussion, Mike Giangrande focuses on AMT, ESPPs, RSUs, RSAs, W-2 reporting, and 83(b) and 80(i) elections. [Running time: 56:56]

Learning Objective:

Upon completion of this segment, the user should be able to discuss: (1) AMT adjustments and incentive stock plans, (2) income and limits on incentive stock options, (3) income recognition on dispositions of stock awards and purchases; (4) differences between RSUs and RSAs; and (5) the purpose of a Section 83 (b) election

ABOUT THE SPEAKERS

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Mike Giangrande, JD, LLM, is a California licensed attorney and has been a tax practitioner for 25 years. He is licensed to practice before the United States Tax Court, has a B.S. in Accounting, an L.L.M. in Tax from Chapman University, and a J.D. from Whittier Law School with a certificate of concentration in business law. Mike has spent time as an adjunct professor of law and has served as a member of the Orange County Assessment Appeals Board.

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EXPERT ANALYSIS AND COMMENTARY

PART 1. CURRENT DEVELOPMENTS

Experts' Forum

Experts' Forum is a popular feature in which we review recent developments in taxation. This month Ian Redpath looks at the IRS' Dirty Dozen list. From phishing and smishing to bogus and fraudulent offshore schemes, he reviews the list of common tax scams considered the worst of the worst by the IRS. He also briefly reviews the new draft Form 1099-DA for digital assets for 2025.

Let's join Ian.

Mr. Redpath

Hi everybody, welcome to the program. This is the segment where we go over a number of different things that have happened with the IRS, Congress, the courts, whatever the case may be, such a dynamic field, tax, and lots of changes. But let's start right off with a segment that generally you viewers have said that you enjoy and we can cue up the music and here we go, the 2024 version of the Dirty Dozen. We can make light of it in some respects, but there are a number of tax frauds. Some of these keep continuing on the Dirty Dozen. Last year, the year before, you heard me talking about them because they keep reappearing, which means the frauds are continuing.

Now, one of the things we can start right off with is, what do you do if you have a client who has been defrauded, or what can a taxpayer do? Again, the IRS says to report an abusive tax scheme or to report a problem with a tax preparer, not you, but maybe you have a new client that's come in, you should use the online Form 14242, called Report Suspected Abusive Tax Promotions or Preparers. It's online. You can mail or fax the completed form, a PDF of it, and any supporting materials to the IRS Lead Development Center in the Office of Promoter Investigations. The address is Stop MS5040, 24000 Avila Road, Laguna Niguel, California 92677 -3405 and the fax number 877 -477 -9135. You can also submit information to the IRS whistleblower office and potentially, depending on what you've reported, you may be eligible for a monetary reward.

A. Dirty Dozen

Let's start right off with the dirty dozen. The IRS beginning at the end of March, each week they would issue, or sometimes a couple a week, they would issue these dirty dozen tax fraud schemes, the most popular schemes from last year, from 2023, that we need to be aware of in 2024.

1. IR 2024-84

Let's start off with IR 2024 -84 phishing and smishing scams designed to steal sensitive information. And we should point out that the IRS and the security summit partners in dealing with the states, et cetera, have warned individuals and businesses that they have to stay vigilant against these attacks, these attempts to trick the recipient into clicking a suspicious link, filling out personal and financial information, or downloading malware onto a computer. The IRS says that there's just a barrage of email and text scams targeting taxpayers. One of the things that I think is a good idea is to take the dirty dozen and let your clients be aware of it.

Here's what the IRS is seeing out there. Highlight these things so that they can be aware of them. The role of the dirty dozen is, not just to alert us as tax professionals, but to allow us to alert our clients as to things that they should be aware of. In tax, there's a wide array of scams, and they target tax professionals, they target payroll providers, human resource departments, and some of these are more in the nature of spear phishing, which we're going to talk about as another one of the dirty dozen. But tax professionals, payroll providers, human resource departments are one of the favorite targets of email and text scams because they have a lot of personal and sensitive information.

We'll talk later about the new client scam, which a lot of accountants get, especially during tax season. So these are things that you really need to be aware of. . . . You should have policies and procedures to deal with it. What happens

when a, perhaps a staff person, because they've done their research, receives something that appears to be from a payroll provider, and is asking for certain information? Or, what happens when your client receives something that appears to be from you, or appears to be from their payroll provider, or maybe you're doing both, asking for certain information about various of their employees? It's a great way to get information should someone answer it. In addition, you can click and the next thing you know there's been malware added to the computers or to your computer system. You have to be very, very careful of this, and what they're going to use it for, obviously, is nefarious reasons. Phishing, that's email sent claiming to be from the IRS, and they mirror the IRS website. They look like they come from the IRS.

One that I'm aware of, my client brought this to my attention when it asked for their social security number. It looked like the IRS website to begin with, but then as you went through, it clearly was not the IRS's website to a trained eye, but to an untrained eye it did. But what they had done is they had...right at the bottom, where it said to put in their social security number, it said, the IRS will never ask you for your social security number over email. So they didn't quite mirror the site that great. But nonetheless, the client brought it to my attention, fortunately. And I said, yes, I'm glad you didn't fill in anything further. But often again, they'll get information. They'll ask, we have a refund due you. You need to put in this information. That's what this one was. You have a refund due. You need to provide us this information. And, of course, they wanted social security number, banking information to get the refund.

Then, smishing, that's a text or smartphone SMS message where again, they use language and usually something like, your account has now been put on hold, or we have detected unusual or suspicious activity, and then it has a link to solutions. Now you're going to see the same thing on emails, so the phishing and smishing can be the same. So the solution, the link to restore your account, and again, that is not taking you where you think it's going to take you. Never click on unsolicited communication claiming to be from the IRS. They can load malware onto your computer. That's a great way for hackers to load ransomware. This is something that you really need to be careful of. And remember your whole need now to have ... a plan to protect client data. How to deal with these types of things should all be in that plan that your office has adopted. And so, again, they appear to come from legitimate sources, but we know that they're not. Now another thing that's happened is they come from, an organization, a trusted organization, or a family friend to target individuals or tax preparers. Again, verify the information as to who they come from if they start asking for that type of information. Again, the inspector general and the IRS, what should you do if you get an email claiming to be from the IRS that contains a request for personal information. Don't reply. Don't open any attachments. Don't click on any links. Send the full email header or forward the email to phishing@irs.gov. Don't forward screenshots or scanned images of the email, because that removes the information, a lot of the metadata that they need. Then, delete the original email. For texts, pretty much the same thing. Don't reply. Again, don't open any attachments or links. Report the message to 7726. Include the caller ID, the message body in the email. Again, you can send to phishing @irs.gov, and delete the text.

2. IR 2024-85

Number two, IR 2024 -85, unscrupulous and aggressive promoters of the ERC. We've talked about this in a number of programs and all of the things going on, but again, you don't hear this much anymore as the IRS became very aggressive. There is still a moratorium on processing of new claims. Now, if you have a legitimate claim for a client, you should send it in. It's not going to get processed, but at least it'll be in the queue for processing. Congress and the IRS have talked about moving up the statute of limitations from its current 2025 deadline. If that's the case, you want to make sure that you're in the queue already. But that goes back to September 14, 2023. Now, the IRS's compliance efforts, they claim have topped more than \$1 billion in questionable claims. The IRS continues to urge people to look at, if you have something suspicious, look at the IRS withdrawal program, the voluntary compliance program was discontinued as of March 22nd. The withdrawal program is the only way that you can go. Now the IRS has also received over 250 million in withdrawals since they started the withdrawal program. What happens if you haven't cashed the check? What happens if you have cashed the check?

Well, you can do the withdrawal if you haven't cashed a check or had it deposited in your account. However, if you have, you're going to have to return the funds and ask for relief from penalties. You have to go through pretty much the old process. Now, the rule under the voluntary compliance, the 20%, no penalties and interest, that is gone.

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However, the IRS mentioned that they may consider bringing it back, but the way they're talking about bringing it back at having to pay back the full amount, not the 80%.

Some of the signs that an ERC claim can be incorrect. Now, I've had many, many accountants send me requests to review something, documents they've gotten, or questions as to how to handle these things. So they're going on, clients are getting caught into it. I had a client, or an individual, who came to me and said, guess what? I got a million something dollars. And I said, ERC? He goes, yes, he goes, I called one of those things on the radio and the guy, they've got, I'm getting a million dollars. Well, have you talked to your accountant yet? And I said, did they amend your payroll, or your income tax returns? Well, no, they did this payroll tax. I said, you've got an issue, go talk to your accountant. I haven't talked to him since, I don't know what he did, but it just sounded fishy.

I had another one where the accountant said, hey, we told them they weren't entitled to it. They called one of those companies, the ERC (Employee Retention Credit) mills. They went ahead and filed. They got them a check for \$750,000. We've checked it over and over again. They don't qualify. What do we do? Well, fortunately, they would be able to be subject to the withdrawal because they actually had a physical check and had not cashed it.

So some of the common flags--too many quarters being claimed, government orders that don't qualify as a shutdown of the business or where the business voluntarily closed, too many employees and wrong calculations, supply chain issues. Those are difficult ones because the supply chain disruption itself is not enough, even though it was caused by COVID, was it caused by a...governmental closing. The business claiming the ERC for too many tax periods. The business didn't pay wages or didn't exist during the eligibility period. I saw one of those myself. They got an ERC, they didn't exist. They weren't even there during that time. So they started after [that period]. A promoter says, you have nothing to lose. Well, you have a lot to lose, potentially, in this case. The biggest thing you have to lose is the fees you paid the promoter. So you have to go now and chase the promoter. We have a large judgment against a former OIC (offer In Compromise) mill. Well, the founders went to prison and the company's gone belly up. So, what are you going to do?

3. IR 2024-87

Number three, IR 2024 -87, scammers attempting to sell or offer help in setting up an online account. The scammers are contacting taxpayers. They're offering to help them set up an online IRS account. They come across as a legitimate business. The IRS online account is a valuable tool, but it does not need a third party. You may help a client, but these are just scams. Third parties aren't offering them any more advice than they would get if they just contacted the IRS directly. Again, you should tell your clients, be wary.

4. IR 2024-91

Then IR 2024-91 is number four. The IRS is settling for pennies on the dollar. Okay, well, OIC (offers in compromise) mills, they're still there, they're still advertising. It's really a very valuable program. I've used it many times for clients with a lot of success, but people are being sold a bill of goods. I was sitting on a plane and a woman asked me what I did and I told her. She goes, can I ask you a question? She said, I contacted XYZ, a company about an offer in compromise, and it's been over two years, and every time I call, I get somebody else on the phone. The person just asks me the same questions, and they can't really tell me what the status is. They say it's pending. I said, there's a problem here.

I had another one where they told the people, we will compromise. It's going to be \$14,000, it was an odd amount, \$14,000 something, and that will cover your tax, penalties, interest, and our fee. Well, that's interesting because they hadn't filed tax returns in over 10 years. So what tax liability were they compromising? I said, did they get your information to file a new return? To file your back returns? Did they get anything from you? No, that was the first call over the phone. They told us that this is what it was going to cost when we told them we hadn't filed our returns. So again, a lot of problems. They're still going on.

5. IR 2024-89

Number five is IR 2024 -89. A lot of problems going on out there with unscrupulous promoters for fuel tax. Fuel tax is only available for off-highway business and farming use. Most taxpayers aren't entitled to it, yet the IRS has seen

an increased number of fictitious claims for fuel tax on Form 4136. Again, they are in general not legitimate claims. The average person is not entitled to it, even though these promoters seem to act like you are just for driving.

6. IR 2024-92

Number six is IR 2024 -92, fake charities. It's unfortunate, but every time there's a natural disaster, a lot of charities pop up, but a lot of people who are raising money are not legitimate charities. They're either looking to get sensitive information, financial information, or just simply to get money or some combination thereof. So again, . . . if your client contacts you first, look under the TEOS, the Tax Exempt Organization Search to make sure it's a legitimate charity. If they aren't listed, you can call the IRS. If they're not, if they have no information, then you might want to tell the client, find another charity to give to. So again, don't give in to pressure, exercise caution with donations, always verify the legitimacy and avoid sharing too much data. Because they'll try to ask people for more and more information. Let your client be aware of that.

7. IR 2024-96

Number seven is IR 2024 -96. This is not you, but during tax season, ghost preparers pop up. They may take an office in a mall just during tax season. I know of one that they were contacting people and they would come to your house and prepare your taxes basically at your kitchen table. I questioned that. Now, one of the things that they tend to do is, ghost preparers and they're called that because they don't have a PTIN number, not sign the return. So no PTIN, not sign the return. Often they will steal refunds and or charge a significant amount of money. So clients should be aware of that. A couple of things to watch out for, shady fees, sometimes providing false income information. If they say they've got to deposit the refund into their bank account, theirs rather than yours, using the wrong bank account numbers, all of those things are red flags.

8. IR 2024-98

Number eight is IR 2024 -98, bad tax information on social media. Tell your clients not to pay attention to TikTok or other social media. There's two major schemes that they're seeing. Common documents like W -2s misuse, or using obscure forms like Form 8944, which involves a technical e -file. It's not used by taxpayers, it's used by tax professionals.

Social media, it's not all information that is a scam, but it's almost always bad information. Two recent schemes that the IRS found online. The one on social media encourages people to use tax software, manually fill in the W -2 wage and state tax statement, include false income information, false withholding information, to get a large refund. File it electronically in hopes that you can get the large refund. The IRS has said sometimes these are as much as five figures due to the large amount of withholding that was claimed. Two others similar; fraudulent Form 7202s, the credit for sick leave and family leave for certain self-employed people, and fraudulent Schedule H's, household employment. It encourages people to invent fictional household employees, file the...Schedule H to claim a refund based upon false sick and family leave paid.

And, then Form 8944, again, another example that the IRS says they see, wildly inaccurate claims about the form, including it's use by taxpayers to get a refund. Even if the taxpayer has a balance due, this is not the form. It's just false information. So two types of forms.

9. IR 2024-100

Number nine is IR 2024 -100. This is spear phishing. What's the difference between phishing and spear phishing? Spear phishing is targeted. When I talked about it earlier, I mentioned that we'd talk about this, but spear phishing...the targets, specific targeting, for example, a staff person trying to get into the computer system or trying to get the theft of client data or some form of identity. They target individuals, organizations, businesses. So how to avoid it? Don't click on suspicious links. Call a potential client to confirm. Send only password protected or encrypted documents through email, protect email accounts with strong passwords and two -factor authentication, and then again, use security software products with anti -phishing tools. The biggest one now is the new client scam. That spear phishing attempt. Cyber criminals impersonated a new or potential client to get the tax preparers to respond to their emails. The scammer sends a malicious attachment that can compromise, again, your computer system and attack sensitive

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information. Be very careful of the new client scheme. Warning signs about the new client-- poorly constructed sentences, unusual word choices. Sometimes you'll say, this doesn't sound like it was written by someone who has much of the knowledge of the English language or Spanish language, if it's in Spanish. Be aware that by gaining access to a hacked email account, they can locate genuine email from a previous victim's email account and send it to their tax professional. So again, if it's coming from a client's email that you recognize, but all of a sudden, it doesn't sound right, the language doesn't sound right. The spelling and grammar are wrong. That should give you a little bit of a cause not to jump in and respond. Contact them directly to find out if this is legitimate.

10. IR 2024-104

All right, number 10 is IR 2024 -104, schemes aimed at high income taxpayers. Improper art donations. So what's happening here? Promoter comes, promoter says look what we're going to do is we're going to buy this art at a significantly discounted price hold it for a year, then donate it, then get the write off of the full fair market value, but the full fair market value is significantly inflated to get a much higher deduction. And so that's kind of the scheme that's being used. And remember that the appraisals have to be legitimate. If it looks too good to be true, it probably is.

Now the next thing, charitable remainder annuity trust. First, the IRS has said that they want to make these reportable transactions under those rules, but their use of charitable remainder trusts has come under some scrutiny because even though the trusts are legitimate trusts, the person donates assets to a charity and draws an annual income for life for a specific period, the charity then gets whatever is remaining. However, what's been happening is that appreciated property has been transferred to the CRAT (Charitable Remainder Annuity Trust). Taxpayer wrongfully claims the transfer of the assets to the CRAT, giving it a step up in a basis as if they had sold it to the trust. So now it's a step up in basis. The CRAT then sells the property and doesn't recognize any gain because it's claiming a step up in basis. The CRAT uses the proceeds then to purchase a single premium immediate annuity. The beneficiary reports his income only the small portion of the annuity, so again, through misapplication of the law, the beneficiary treats the remaining payment as excluded, being a return of investment and there's no tax. That isn't a correct use, it is a misuse of a CRAT.

Monetized installment sales--another example, in these examples, taxpayers seek to defer the recognition of gain on appreciated property, organize an abusive tax shelter through selling them monetized installments. So again, an intermediary purchases the appreciated property from the seller in exchange for an installment note, which typically provides for payment of interest only. Principal is being paid somewhere at the end of the term, down the road. The seller gets the lion's share of the proceeds, but then delays the recognition on the sale until the final payment, often a lot of years later.

11 and 12.IR 2024-105

Then numbers 11 and 12, [are in] IR 2024 -105, bogus tax strategies and fraudulent offshore schemes... Syndicated conservation easements continue to be an area of scrutiny because they have been abused so often. Microcaptive insurance arrangements where you are insuring offshore, you are insuring really for, you don't have a genuine risk. You can't match the business needs. It's implausible sometimes, some of the risks. Duplication of other coverages and the premiums are often excessive, reflecting non-arms-length. So again, the owners elect to be taxed on the captive investment income only. The scheme, while it looks like real insurance, it's really not. You're insuring at very high premiums, often things that are duplicate or they're implausible risks. The circus comes to town and the circus animals get loose and they come and destroy your business property. Okay. It could happen. This is an area, again, when you say you're going to be taxed on investment income only creates a real problem.

Another one is the schemes involving international elements like the Maltese retirement arrangements. And in this one promoters lure the US person to place their assets offshore saying they're out of reach of the IRS and the FATCA that these Maltese retirement arrangements are misusing the Maltese treaty to claim that they're actually retirement or pension funds.

Then, of course, digital assets. We know that digital assets are a huge problem for reporting. Something that the IRS has been going after for a significant period of time. So that winds up our dirty dozen.

B. Draft Form 1099-DA

One thing, though, kind of following up on the dirty dozen is the IRS has now released the draft form 2025 Form 1099 DA for digital asset reporting. And so, this is the first hit at the Form 1099 -DA. There's questions in there that mirror the questions on the 1040, and by the way, the S corps and partnerships 1065, 1120S. There's also information requested on wash sales under Section 1091. So there's a new box, or a box, it's all new, box 11D, which is to be checked if the sale is not recorded on a distributed ledger. Now why is that there? It's necessary because often digital asset addresses or transaction IDs cannot be provided because the transaction occurred in an internal recordkeeping system. So you can't provide a digital asset address or transaction ID. So again, something to look at and to review at your leisure.

SUPPLEMENTAL MATERIALS

Experts' Forum

By Ian J. Redpath, JD, LLM

A. Dirty Dozen

The IRS urges individuals to report those who promote abusive tax practices and tax preparers who intentionally file incorrect returns. To report an abusive tax scheme or a tax return preparer, use the online Form 14242 – Report Suspected Abusive Tax Promotions or Preparers, or mail or fax a completed Form 14242 and any supporting material to the IRS Lead Development Center in the Office of Promoter Investigations.

Mail:

Internal Revenue Service Lead Development Center Stop MS5040 24000 Avila Road Laguna Niguel, California 92677 3405

Fax: 877-477-9135

This can also be submitted to the IRS Whistleblower Office. The person might be eligible for a monetary award.

1. IR-2024-84, March 28, 2024 - phishing and smishing scams designed to steal sensitive taxpayer information

The Internal Revenue Service today kicked off the annual Dirty Dozen list with a warning for taxpayers to be aware of evolving schemes. Taxpayers continue to be bombarded by email and text scams. Fraudsters and identity thieves attempt to trick the recipient into clicking a suspicious link, filling out personal and financial information or downloading a malware file onto their computer. "Scammers are relentless in their attempts to obtain sensitive financial and personal information, and impersonating the IRS remains a favorite tactic," said IRS Commissioner Danny Werfel. "People can be anxious to get the latest information about their refund or other tax issues, so scammers frequently try using the IRS as a way to trick people. The IRS urges people to be extra cautious about unsolicited messages and avoid clicking any links in an unsolicited email or text if they are uncertain."

Phish or smish: Don't take the bait

Tax professionals, payroll providers and human resource departments remain favorite targets of email and text scams since they have sensitive personal and financial information. These messages arrive in the form of unsolicited texts or emails to lure unsuspecting victims to provide valuable personal and financial information that can lead to identity theft. There are two main types:

- **Phishing:** An email sent by fraudsters claiming to come from the IRS. The email lures the victims into the scam with a variety of ruses such as enticing victims with a phony tax refund or threatening them with false legal or criminal charges for tax fraud.
- Smishing: A text or smartphone SMS message where scammers often use alarming language such as, "Your account has now been put on hold," or "Unusual Activity Report," with a bogus "Solutions" link to restore the recipient's account. Unexpected tax refunds are another potential lure for scam artists.

Never click on any unsolicited communication claiming to be from the IRS as it may surreptitiously load malware. It may also be a way for malicious hackers to load ransomware that keeps the legitimate user from accessing their system and files. In some cases, phishing emails may appear to come from a legitimate sender or organization that has had their email account credentials stolen. Setting up two-factor or multi-factor authentication with their email provider can reduce the risk of individuals having their email account compromised. Another common way is posing as a trusted organization, friend or family member remains a common way to target individuals and tax preparers for various scams. Individuals should verify the identity of the sender by using another communication method, for instance, calling a number they independently know to be accurate, not the number provided in the email or text.

Supplemental Materials CPE Network® Tax Report

Report all unsolicited email - including the full email headers - claiming to be from the IRS or an IRS-related function to phishing@irs.gov. If someone experienced any monetary losses due to an IRS-related scam incident, they should report it to the Treasury Inspector General for Tax Administration (TIGTA), the Federal Trade Commission and the Internet Crime Complaint Center (IC3).

The IRS recommends that if a taxpayer receives an **email** claiming to be from the IRS that contains a request for personal information, taxes associated with a large investment, inheritance, lottery or similar information:

- Don't reply.
- Don't open any attachments. They can contain malicious code that may infect the computer or mobile phone.
- Don't click on any links. If a taxpayer inadvertently clicked on links in a suspicious email or website and entered confidential information, visit the IRS' identity protection page.
- Send the full email headers or forward the email as-is to phishing@irs.gov. Don't forward screenshots or scanned images of emails because this removes valuable information.
- Delete the original email.

If a taxpayer receives a similar text, the IRS recommends:

- Don't reply.
- Don't open any attachments. They can contain malicious code that may infect the computer or mobile phone.
- Don't click on any links. If a taxpayer clicked on links in a suspicious SMS and entered confidential information, they should visit Identity Theft Central.
- Report the message to 7726 (SPAM).
- Include both the Caller ID and the message body in an email and send to phishing@irs.gov. Copy the Caller ID from the message by pressing and holding on the body of the text message, then select Copy, paste into the email. If the taxpayer is unable to copy the Caller ID or message body, forward a screenshot of the message.
- Delete the original text.

The Report phishing and online scams page at IRS.gov provides complete details. The Federal Communications Commission's Smartphone Security Checker is a useful tool against mobile security threats.

2. IR-2024-85, March 29, 2024: unscrupulous and aggressive promoters of questionable claims for the Employee Retention Credit (ERC).

Since the IRS announced a moratorium on processing new claims filed after Sept. 14, 2023, the ERC claims have topped more than \$1 billion so far since last fall as work continues on a number of efforts to counter questionable claims. The IRS remains concerned that some ineligible businesses are being encouraged by marketers to submit an incorrect ERC claim; people should contact a trusted tax professional first to avoid potential IRS compliance action in the future. Promoters pushed more applicants into the program, frequently by taking a percentage of the payout.

The IRS is continuing to accept and process requests to withdraw an employer's full ERC claim under a special withdrawal process. The IRS has already received more than \$250 million in withdrawals as the agency continues intensifying audits and criminal investigation work in this area. This option allows certain employers that filed an ERC claim but have not yet received a refund to withdraw their submission and avoid future repayment, interest and penalties. Employers that submitted an ERC claim that have not yet been paid can withdraw their claim and avoid the possibility of getting a refund for which they're ineligible. They can also withdraw their claim if they've received a check but have not yet deposited or cashed it. Claims that are withdrawn will be treated as if they were never filed. The IRS will not impose penalties or interest.

Recently, the IRS highlighted special warning signs that an ERC claim may be questionable to help small businesses that may need to resolve incorrect claims. Among them are:

- **Too many quarters being claimed.** Some promoters have urged employers to claim the ERC for all quarters that the credit was available. Qualifying for all quarters is uncommon and this could be a sign of an incorrect claim.
 - o **Government orders that don't qualify.** Some promoters have falsely told employers they can claim the ERC if any government order was in place in their area, even if their operations weren't affected or if they chose to suspend their business operations voluntarily.
 - Too many employees and wrong calculations. Employers should be cautious about claiming the ERC for all wages paid to every employee on their payroll. The law changed throughout 2020 and 2021. There are dollar limits and varying credit amounts, and employers need to meet certain rules for wages to be considered qualified wages, depending on the tax period.
- **Business citing supply chain issues.** Qualifying for the ERC based on a supply chain disruption is very uncommon. A supply chain disruption by itself doesn't qualify an employer for the ERC.
- Business claiming the ERC for too much of a tax period. It's uncommon for an employer to qualify for the ERC for the entire calendar quarter if their business operations were fully or partially suspended due to a government order during a portion of a calendar quarter.
- **Business didn't pay wages or didn't exist during eligibility period.** Employers can only claim the ERC for tax periods when they paid wages to employees.
- **Promoter says there's nothing to lose.** Businesses should be on high alert with any ERC promoter who urged them to claim the ERC because they "have nothing to lose." Businesses that incorrectly claim the ERC risk repayment requirements, penalties, interest, audit and potential expenses of hiring someone to help resolve the incorrect claim.

3. IR-2024-87: Scammers attempting to sell or offer help setting up an Online Account on IRS.gov.

An IRS Online Account allows taxpayers access to the information about their tax account. They can log in and get the latest on their payment history, current balance, see copies of select IRS notices and more. It is a useful and easy to use tool that scammers target. While they may make it seem like a complicated task needing their assistance, taxpayers can and should establish their own Online Account through IRS.gov. Scammers often ask for the taxpayer's personal information including address, Social Security number or Individual Taxpayer Identification number (ITIN) and photo identification. They can sell the information or use the sensitive details to file fraudulent tax returns, obtain loans and open credit accounts.

The only place individuals should go to create an IRS Online Account is IRS.gov. People should not use third-party assistance, other than the approved IRS authentication process through IRS.gov, to create their own IRS Online Account.

4. IR-2024-91: Offer in compromise (OIC) "mills"

As in past years, companies running OIC mills continue heavily advertising their promises to settle taxpayer debt at steep discounts for "pennies on the dollar." Many taxpayers do not meet the technical requirements for the tax resolution program, often leaving them facing excessive fees from the promoters for information they could have easily obtained for free by using the IRS's Offer in Compromise Pre-Qualifier tool.

Taxpayers, however, should be cautious of OIC mills, which make exaggerated claims through radio and TV ads about settling tax debts inexpensively. In reality, these mills often charge excessive fees, and taxpayers end up paying for a service they could have obtained directly from the IRS. Taxpayers may also qualify for the first time penalty abatement program.

5. IR-2024-89: Improper Fuel Tax Credits claims

The Fuel Tax Credit is available only for off-highway business and farming use and not for most taxpayers. The IRS continues to see instances where unscrupulous promoters or return preparers mislead taxpayers about fuel use and

create fictitious documents or receipts for fuel. Falsely claiming the Fuel Tax Credit is a fraudulent practice with severe consequences, including civil and criminal penalties.

6. IR-2024-92: Fake Charities

In natural disasters and other tragic events, it's common for compassionate individuals to donate money to help the victims. Unfortunately, scammers often use fake charities as a cover to not only obtain money but also gather sensitive personal and financial information that can be exploited for tax-related identity fraud. People should remember it's important to never feel pressured to give donations immediately. They should do some research and only donate to clearly established charities that help victims." Fake charities have become a concern. These deceitful organizations are created by scammers who take advantage of people's generosity. They solicit money and personal information to victimize individuals through identity theft.

Individuals intending to donate can utilize the Tax-Exempt Organization Search (TEOS) tool on IRS.gov to ensure legitimacy.

7. IR-2024-96: unscrupulous tax preparers

A common problem seen annually during tax season, "ghost preparers" pop up to encourage taxpayers to take advantage of tax credits and benefits for which they don't qualify. These preparers can charge a large percentage fee of the refund or even steal the entire tax refund. After the tax return is prepared, these "ghost preparers" can simply disappear, leaving well-meaning taxpayers to deal with the consequences. A ghost preparer is someone who doesn't sign tax returns they prepare. These unethical tax return preparers should be avoided, especially if they refuse to sign a complete paper tax return or digital form when filing electronically.

8. IR-2024-98: bad tax information on social media

Social media can routinely circulate inaccurate or misleading tax information, where people on TikTok and other social media platforms share wildly inaccurate tax advice. Some involve urging people to misuse common tax documents like Form W-2, or more obscure ones like Form 8944 involving a technical e-file form not commonly used by taxpayers. Both schemes encourage people to submit false, inaccurate information in hopes of getting a refund.

"Social media is an easy way for scammers and others to try encouraging people to pursue some really bad ideas, and that includes ways to magically increase your tax refund," said IRS Commissioner Danny Werfel. But people should be careful with who they're following on social media for tax advice. Unlike hacks to fix a leaky kitchen sink or creative makeup tips, people shouldn't rely on made-up ways on social media to patch up their tax return and boost their refund."

The IRS warns taxpayers to be wary of trusting internet advice, whether it's a fraudulent tactic promoted by scammers or it's a patently false tax-related scheme trending across popular social media platforms. While some producers of misleading content are driven by criminal profit motive, others are simply trying to gain attention and clicks. They will post anything, no matter how wrong or outlandish, if it garners more attention.

9. IR-2024-100: email spearfishing aimed at tax professionals and businesses

The IRS and the Security Summit partners urge tax pros and businesses to watch out for a surge in a particular type of spear fishing known as "new client" scams, where identity thieves pose as potential clients using fake emails. Through spear phishing emails, cybercriminals impersonate real taxpayers seeking help with their taxes, using fake emails to get sensitive data or gain access to a tax professional's client information from their computer systems. While these can peak around tax season, they remain a year-round threat. Criminals accessing tax preparer credentials, or their client's tax-related information, can affect multiple victims.

While phishing refers to emails or text messages designed to steal personal information directly, or by clicking on an embedded link or attachment, spear fishing is more targeted. Spear phishing is a type of phishing that targets specific individuals, organizations or businesses, typically using malicious emails. A successful spear phishing attack can lead to the theft of client data and the identity theft of the tax preparer. This could potentially enable the attacker to file fraudulent returns.

The "new client" scam, which involves spear phishing attempts, continues to be a concern for the IRS and its Security Summit partners. Cybercriminals impersonate new, potential clients to trick tax preparers into responding to their emails.

10. IR-2024-104: Schemes aimed at high income taxpayers

These can take many different forms, ranging from inflated art donation deductions to aggressive charitable remainder annuity trusts and detailed shelters that maneuver to delay paying gains on property.

Improper art donation deductions

There are ways for taxpayers to properly claim donations of art. But some unscrupulous promoters use direct solicitation to promise values of art that are too good to be true. These promoters encourage taxpayers to buy various types of art, often at a "discounted" price. This price may also include additional services from the promoter, such as storage, shipping and arranging the appraisal and donation of the art. The promotor promises the art is worth significantly more than the purchase price. These schemes are designed to encourage purchasers to donate the art after waiting at least one year and to claim a tax deduction for an inflated fair market value, which is substantially more than they paid for the artwork. Promoters may suggest taxpayers donate art annually and allow them to buy a quantity of art that guarantees a specific deductible amount. Promoters may even arrange for certain charities to take the donations.

Charitable remainder annuity trust

Charitable remainder trusts (CRAT) are irrevocable trusts that let persons donate assets to charity and draw annual income for life or for a specific time period. A CRAT pays a specific dollar amount each year. Unfortunately, these trusts are sometimes misused to eliminate capital gain. Here's how it works. The appreciated property is transferred to a CRAT. Taxpayers wrongly claim the transfer of the appreciated assets to the CRAT, which gives those assets a step-up in basis to fair market value as if they had been sold to the trust. The CRAT then sells the property but does not recognize gain due to the claimed step-up in basis. The CRAT then uses the proceeds to purchase a single premium immediate annuity (SPIA). The beneficiary then reports, as income, only a small portion of the annuity received from the SPIA. Through a misapplication of the law relating to CRATs, the beneficiary treats the remaining payment as an excluded portion representing a return of investment for which no tax is due. Taxpayers who seek to achieve this inaccurate result do so by misapplying the rules.

Monetized installment sales

In these frequently shady deals, promoters look for taxpayers seeking to defer the recognition of gain upon the sale of appreciated property and then organize an abusive shelter through selling them monetized installment sales. These transactions occur when an intermediary purchases appreciated property from a seller in exchange for an installment note, which typically provides for payments of interest only, with principal being paid at the end of the term. In these arrangements, the seller gets the lion's share of the proceeds but improperly delays the gain recognition on the appreciated property until the final payment on the installment note, often slated for many years later.

11 and 12. IR-2024-105: Bogus tax strategies and fraudulent offshore schemes

Various fraudulent schemes threatening taxpayers can take different forms, including exploitative agreements related to syndicated conservation easements and micro-captive insurance arrangements. These schemes may also have an international aspect, such as concealing money and digital assets in foreign accounts or using foreign captive insurance and Maltese foreign individual retirement accounts.

Digital assets

A digital asset is a digital representation of value that is recorded on a cryptographically secured, distributed ledger or any similar technology. Common digital assets include:

- Convertible virtual currency and cryptocurrency.
- Stablecoins.
- Non-fungible tokens (NFTs).

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Unscrupulous promoters often recommend digital assets as being untraceable and undiscoverable by the IRS. However, the truth is that the IRS can identify and track anonymous transactions of digital assets around the globe.

For federal tax purposes, digital assets are treated as property. General tax principles applicable to property transactions apply to transactions using digital assets.

B. 2025 Draft Form 1099-DA

The IRS released a draft of the 2025 Form 1099-DA. This is the information return for reporting digital asset transactions that will be furnished by brokers, reflecting proposed regulations issued last year. Common examples of digital assets to be reported include cryptocurrencies, stablecoins, and non-fungible tokens. Form 1099-DA asks for various information about the type and amounts of digital assets transacted, as well as the addresses and Taxpayer Identification Number of parties involved. Taxpayers are expected to report when they acquired the asset, when it was sold or disposed, and cost basis. The form also includes a question on the "amount of nondeductible loss in a wash sale transaction involving digital assets that are also stock or securities for tax purposes."

GROUP STUDY MATERIALS

A. Discussion Problems

- 1. You received a text message, allegedly from the IRS, telling you there has been suspicious activity on your Tax Pro Account and the account has been frozen. To solve the issues you are directed to a link provided in the text.
- 2. Your client, Arthur, comes into the office and says he received an email from a group that offered to help him establish an IRS On-Line Account. They told him all the benefits once it is established but they needed some information such as his complete name, address, SSN, banking information and more. They are charging a fee for this. He told them he needs to gather the information and they are calling back in the morning. Arthur wonders if he should get one.
- 3. Anita, a longtime client of the office, comes in and tells you she has been approached by a charity that is raising money to assist the victims of a recent hurricane. The call seemed legitimate and professional. They said they had been doing this nationwide for over 10 years and that I had given about a year ago for another hurricane. They indicated the contributions are fully deductible and 98% of all funds go directly to the victims. She tells you she wants to donate a significant sum and how much do you think she should give for tax purposes?

Required:

Discuss the issues fairly presented in the above independent situations based on the material provided.

B. Suggested Answers to Discussion Problems

1. This is an example of spear smishing and a common fraud scheme. It is aimed at obtaining valuable information from the tax professional and also the ability to gain access to some confidential client information. Do not click on the link and do not provide any information. Report this to the IRS.

- 2. While the IRS On-Line Account is good for taxpayers, it is easy to set up and the IRS provides easy to use instructions. Additionally, you can assist if they need it. This is most likely a fraud scheme to obtain information for identity theft.
- 3. Fake charities are a significant problem and often used by fraudsters to obtain important information from a person, usually for identity theft reasons. You can check out the charity on the TEOS system to see if it is a valid charity.

PART 2. INDIVIDUAL TAXATION

Stock Incentive Plans: Part II

We complete our discussion from last month on stock incentive plans. Stock incentive plans have proven to be a difficult subject for many tax professionals to understand and/or track for their clients. From AMT issues to available elections there are a variety of concerns when it comes to stock incentive plans.

Let's join Mike to further our discussion on the types of plans, and the elections and reporting that are available.

Mr. Giangrande

Let's move on to the alternative minimum tax issues. This point is very important here. Incentive stock options are the only type of incentive stock plan that requires an AMT adjustment. After this discussion, we can ignore AMT. Non-qualified options don't have AMT issues. Employee stock purchase plans, restricted stock units, restricted stock awards, none of them have AMT issues. Only incentive stock options have an AMT adjustment. The adjustment is made on line 2i of Form 6251, our AMT form, and we can use our Form 3921 for a super easy calculation. [Let's look at] the formula. When we exercise, this is on the exercise of incentive stock options. Your client gets a Form 3921 in hand. That means they exercise incentive stock options during the year. Take that 3921, take box four, subtract out box three, multiply it by box five, and whatever that comes up with, that's your AMT adjustment. Slap it on the 6251 line 1i, and there you've made your AMT adjustment. It's that simple.

One sort of comment here though, practice pointer towards top of page eight, if your client does sell that stock in the same year, they exercise it and they sell it in the same year, so they're essentially going to have a non-qualifying disposition, there is no AMT adjustment required. Why is there no AMT adjustment required? Well, because what your client's going to end up with is a non-qualifying disposition. They sold within the same year and you're going to have ordinary income showing up on the W-2 anyway. So an AMT adjustment is just quite simply not necessary. So you don't make that AMT adjustment.

What you do want to do though is, when you do have to make that AMT adjustment, now your stock is going to have a different regular and AMT basis. Your 1099-B, your client, they're not tracking that. You have to track that. You're now going to have a different AMT basis and you want to add that AMT basis to that stock, so that when they do sell the stock, you're not sort of, if you are an AMT situation not paying too much AMT, add that AMT basis there.

Example with Joshua real quick. Joshua was granted an incentive stock option by his employer on September 1, 2022, for 5,000 shares with an exercise price of \$32 per share on July 12, 2023, he exercised the option for all 5,000 shares when the fair market value when the fair market value of the stock was \$39 per share. And so we look at Josh's 3921 once again. Grant date was September 1, of 2022. Exercise date was July 12, 2023. Exercise price \$32 per share in box three. Fair market value on the exercise date is \$39 per share and he had 5,000 shares. So now let's go through our calculation.

It's the same calculation, but now I'm doing it in example form. We're going to take box four, \$39 a share, subtract out box three, \$32 per share, gives the \$7 difference. And that's going to be our AMT adjustment multiplied by our 5,000 shares exercised. We have a \$35,000 AMT adjustment. And Joshua must increase now his AMT basis in those shares by \$7 per share.

Quick discussion on AMT credits. So an alternative minimum tax credit is claimed on Form 8801 and it is essentially claimed in taxable years when the taxpayer's NOLA is not subject to AMT and is really a refund of AMT paid in a prior year. It's a way to sort of try to equalize over a period of time our client's tax. And so when it comes to AMT credits, AMT is caused by two types of adjustments, deferral item adjustments and exclusion item adjustments. Deferral items are simply timing difference items. They don't cause permanent regular and AMT differences. And so when we are stuck in an alternative tax scenario, because of deferral items, we can claim an AMT credit later on.

Exclusion items are permanent differences between regular tax and AMT tax. You're never going to claim an AMT credit based on those items. We've got the list of the exclusion items there. This is going to be certain itemized deductions, certain tax-exempt income, depletion, qualified business stock exclusion under section 1202, the standard deduction. So exclusion items are found on the Form 6251, on lines 2a, b, c, d, g, and h. Those are our permanent difference items. And like I said, the AMT credit is only allowed for AMT caused by the deferral items, not the exclusion items.

Let's move on to sort of the last part I want to cover under ISOs. Taxpayers are subject to a \$100,000 annual limit on the aggregate fair market value of incentive stock options that are exercisable during the calendar year. Any incentive stock options that are exercisable during the year in excess of \$100,000 are classified automatically as non-qualified stock options.

I have an example of how that works. What this means for you is when you have a client who says, I have incentive stock options, you may be dealing with both incentive stock option rules and non-qualifying stock option rules. You're going to deal with the non-qualifying stock option rules on any shares that are in excess of this \$100,000 annual exercisable limit. Let's look at the example on how this works.

On January 1, 2021, Valentina's company granted her the right to purchase 30,000 shares of stock through an incentive stock option plan with a grant price of \$20 per share. The options vest, otherwise known as becoming exercisable, over a four-year period. Valentina began exercising her options on January 1, 2022. She determines that the annual \$100,000 exercise limit has been exceeded as follows.

I suppose I probably didn't need that sentence. It says, Valentina began exercising her options on January 1, 2022. We're looking at exercisable, not what was actually exercised. . . . So if we look at our vesting date, she has 7,500 shares vest on January 1 each year in 2022, 2023, 2024, and 2025.

Her grant price per share is \$20 per share, which means her total grant price is \$150,000 each year, which is \$50,000 over our limit on what is exercisable during each of those years as they vest. And so what we end up with is, she ends up with 2,500 shares over the exercisable limit. And those 2,500 shares per year are treated as non-qualifying stock options and then she has \$5,000 of ISOs each year. So even though your client like I said says, I've got incentive stock options, you may be dealing with both the ISO and the non-qualifying stock option rules at the same time on the same, let's call them options.

With that, let's move on to non-qualified stock options. In the realm of a non-qualified stock option, income is recognized on stock when the stock has met two components, (a) has a readily ascertainable fair market value and (b) is not subject to a substantial risk of forfeiture. This is the basic rule under section 83(a).

Just to kind of give you a background, section 83(a) really covers the income recognition when you receive something of value in exchange for your services. If you do work for me and instead of me paying you in cash, I give you the keys to a beat up old used car. I know that's a weird example, but I gave you the keys to a beat up used car because you did some part-time work for me during tax season. Hypothetically, you have a thing. Now you've received a car with a readily ascertainable fair market value, right? You can Blue Book it if you want, however you want to come up with a fair market value. And it's not subject to a substantial risk of forfeiture. I signed over the pink slip to you, it's yours. And on that date, you now have income recognition. Well, that applies to non-qualified stock options, RSUs, RSAs, really all of our non-statutory options, as well as the receipt of anything else in exchange for your services. That's not cash or cash equivalent. That's the same treatment, actually, that we see with cryptocurrencies. Someone pays you in crypto. The day you actually get it, if you can determine that fair market value for that crypto, and it's yours, the transfer to your account. You meet the two requirements of Section 83(a), and you pick up income, ordinary income, in the day you receive it, based on the fair market value of that thing, that crypto. And that's sort of how Section 83(a) works. Well, this is how non-qualified stock options are taxed. Because the timing of income recognition, like I said, is governed by Section 83.

Now in practice, non -qualified options typically require an employee to actually exercise a previously granted option, where the exercise date is the date that the stock is no longer subject to a substantial risk of forfeiture. If I go back to my definition, readily ascertainable value not subject to a substantial risk of forfeiture, what that means is, when the

stock is granted to you, when the option is granted, you don't have it. It's forfeited if you don't meet the vesting requirements. So, and then you meet the vesting requirements and then you actually pay for the stock. Now you've met the two requirements under section 83(a). That's why non-qualified stock options typically do not have income recognition on their grant date, but they do have income recognition on their exercise date. Because as soon as you've purchased those shares, they now have a readily ascertainable fair market value, and they're no longer subject to a substantial risk of forfeiture. Because remember with the ISOs, you had no tax on the grant, no tax on the exercise, but you had tax when you sold it. Non-qualified options, there's no tax on the grant, they are taxable when you exercise, when you purchase them, because the two requirements of section 83(a) are met.

When income is recognized on a non-qualified stock option, it is taxed as ordinary income and it is subject to Social Security and Medicare. Now, what is the ordinary income that we must recognize when we exercise our incentive stock options? It is the exercise price paid minus the fair market value of the stock on the exercise date. If you really kind of have the ISOs that we talked about down, say, OK, I totally understand these, you'll notice that this is the same calculation as the AMT adjustment for ISOs. Exercise price minus fair market value of the stock on the exercise date, and then, obviously, multiplied by the number of shares, it is the same calculation. The slight bummer of it for you when it comes to the non-qualified stock options, is that you're not going to get a Form 3921. That doesn't exist for non-qualified options. You can get a Form 3921 when you exercise incentive stock options, but the stock that is a non-qualified option or treated as a non-qualified option because you're over that \$100,000 limit we talked about a few minutes ago, you're not going to get a Form 3921. So you're going to have to get this information independently from a form. Now, the ordinary income is going to be reported on an employee's W-2.

It can be on a 1099-NEC if the person is not an employee. And then they'd obviously pay self-employment tax because, like I said, the ordinary income here is subject to Social Security and Medicare. Now, unlike incentive stock options, there is no AMT adjustment when you exercise the non-qualified options. Why is that? Well, because you're already recognizing ordinary income on the day you exercise. And like I said also, it's my hard rule, right? Only ISOs have AMT issues. There is no AMT with any of the other type of options. And I said it before, it's worth repeating here though, that for a non-qualified stock option, the ordinary income is calculated exactly the same way as you would the AMT adjustment for incentive stock options. But you do not receive any IRS form. There is no Form 3921. There is no type of IRS form at all when you exercise a non-qualified stock option.

Now, what happens when we dispose of our non-qualified stock options? So in addition to the ordinary income that's recognized on our W-2 or a 1099-NEC if you're not an employee, the sale of stock acquired by a non-qualifying stock option is treated as capital gain, calculated simply by the fair market value on the exercise, subtracting the fair market value on the exercise date from the sale proceeds. Can be treated as long-term or short-term depending on how long you owned the stock. One year or less, short term, greater than one year, long term.

Let's go through the example... for the disposition of a non-qualified stock option. And you do have the calculation there, as well, right? Sale proceeds minus fair market value because of our capital gain. So here on January 30, 2021, Fiona's employer, granted her 5,000 shares of stock through a non-qualified stock option with an exercise price of \$12 per share. On January 5, 2022, she exercised her option to purchase the 5,000 shares at the fair market value on the exercise date of \$27 per share. And then on April 15, 2023, Fiona sold 1,200 of those shares for \$24 per share. So Fiona's ordinary income is calculated by taking the fair market value per share on the exercise date. We're going to subtract it from that, the exercise price paid, and that equals our ordinary income of \$15 per share multiplied by the 5,000 shares, gives her \$75,000 of ordinary income, which will show up on her W-2.

Now, when Fiona sold her shares for \$24, that represented a \$3 loss per share, right? Because they were worth \$27 when she exercised her options and paid ordinary income, right, on that spread between what she paid and the \$27, but now she sells them for \$24. Now I have to subtract out the fair market value on exercise, which is a \$27 a share, gives her a \$3 capital loss, multiplied by 1,200 shares that she actually sold, she didn't sell 5,000, and she ends up with a \$3,600 long-term capital loss.

Now, let's talk about the 1099-B in the case of a non-qualified stock option. And what this means, because you've got a W-2 adjustment for non-qualified options, the basis shown, I guess I should rephrase that. Let me just start that over. The basis shown on a 1099-B for a non-qualified option is going to be whatever the taxpayer paid, the exercise

price paid per share. That's the same as it is with an incentive stock option. What shows up on the 1099-B for basis is what the taxpayer paid for the shares, the exercise price. And because you're always going to have ordinary income reported on a W-2, for the exercise of a non-qualified option, that means that you will always be required to make a basis adjustment from what is shown on the 1099-B. Clients sell stock acquired through a non-qualified option, your client's going to get a 1099-B, you will have a basis adjustment you must make on the Form 8939 because your client did recognize ordinary income when they exercised their options. Unless for some reason, they exercised the option when the stock had its fair market value the same as their exercise price. In that case though, your client probably isn't exercising the options. They aren't going to bother because they're getting no benefit from it. So really, for all intents and purposes, you're always going to have a basis adjustment. . . .

The example here on the 1099-B is on page [31], and let's walk through that. The facts are the same as the previous example, and now we're going to look at Fiona's 1099-B when she sells the stock. So she sold 1,200 of those shares on April 15, 2023. She bought them on January 1, 2022. So she's going to end up with \$28,800 proceeds, which is her . . . 1,200 shares that she sold multiplied by her \$24 sale price per share. The cost base is shown as 14,400, which again is her 1,200 shares that she sold multiplied by the \$12 per share exercise price gives her a capital gain, a long-term capital gain as shown on her 1099-B of \$14,400. But we know from our previous example's calculation, that she actually has a \$3,600 long-term capital loss. Don't report the basis as shown in the 1099-B. Then if we move down to the Form 8949 there, you see we make the basis adjustment the same way. Column F, use the code B for boy, subtract out 18,000 from her gain, from her taxable gain, gets us to the \$3,600 long-term capital loss. That's how our non-qualified options are going to work. I have for you, oops, let me go back a page.

What I have for you . . . is a sort of a quick hit comparison chart of our non-qualified options and our incentive stock options. If you like charts and like to see the comparison of those two types.

Let's move on to employee stock purchase plans. Employee stock purchase plans, in my mind, are probably the most difficult of all of these from a tax reporting standpoint. And the reason for that is very simple. Both a qualifying and a non-qualifying disposition of stock acquired through an employee stock purchase plan can give rise to ordinary income, and therefore, will always have a basis adjustment on 1099-B. Now, only ISOs and ESPPs are defined as, "statutory stock options," because they each are given a special provision in the code for them. That's what makes them statutory stock options. And these are the only two that require the issuance of a tax form at the end of the year.

We've already talked about the ISOs. In the year you exercise your ISO, you're going to get a Form 3921.... So in the year you purchase your employer stock, you're going to get a Form 3922, very similar form, slightly different information, but very similar. And so when your client comes to you, let's say you get a new client, in early February comes to you and says, Yes, I've got stock options. I don't know what kind I have. And here's all my documents. And they hand you as part of those documents a Form 3921. You know, you have incentive stock options. If it's a Form 3922, you have an employee stock purchase plan. So you can see that right away when you see those forms. Now, the key differences, though, between an ISO and ESPP is that an incentive stock option is a form of equity compensation, where an employee stock purchase plan is really an elective program that allows employees to purchase company stock at a discount. I think almost all of the ones I see are 15% discounts. I think most are between five and 15%. That's what you see there. So if the stock's worth \$100, you have the right to purchase it at say \$85. Now, employees usually elect a percentage of wages to set aside to purchase their company shares at the end of what's called an offering period. Employees have post-tax deductions taken out of their paycheck, right? It's not a pre-tax deduction, post-tax, and that money gets accumulated. At the end of the offering period, whatever money is set aside, that money is used to purchase the employer stock. With an employee stock purchase plan, there is no income recognition on the grant date and there is no income recognition on the exercise date. The date our client simply purchases the shares.

Let's look at an example here of how this works with Jackson. Jackson's employer offers an employee stock purchase plan. Under the terms of the plan, any funds set aside from the employee's wages during the offering period are used to purchase company stock at a 15% discount based on the stock's fair market value on the grant date, which is also the first date of the offering period under the terms of this plan. The fair market value of the employer stock at the

beginning of the current offering period is \$100 per share. During the current offering period, Jackson set aside \$9,000 from his paycheck through the ESPP. Now the offering period can be a calendar quarter, half a year, it could be a year. It can be any period of time. After applying the 15 % discount rate, Jackson's exercise price per share is \$85, which is \$100 per share multiplied by our 15% discount rate. So Jackson ends up receiving 105.88 shares at the end of the offering period. \$9,000 he set aside divided by \$85 a share, 105.88. Even if Jackson does not hold the shares at all and sells them right away, he has received an immediate 15% gain. Because he bought the shares at a 15% discount, sells them right away, he makes 15% on his money instantly. So ESPPs, if there's a nice discount rate, can be a good thing.

So just like with the ISOs and the Form 3921 in the realm of an ESPP, the employer must issue the Form 3922 by January 31st of the following year, the employee purchases the stock through an ESPP. Let's say you've got an employer whose offering period is every calendar quarter, and your client participates. Every calendar quarter they get more stock. Well, they're going to get four Forms 3922. Every time a block of stock is purchased as I said earlier with the Form 3921, sometimes an employer gives you the one form, but has different line items for each block of stock. That might happen here as well with the Form 3922. But for each block of stock, you're going to get the same information. You're going to get Form 3922 contains the grant date, the exercise date, the fair market value of the shares on the grant date, the fair market value of the shares on the exercise price paid per share, the number of shares transferred to the employee, the date legal title to the stock is transferred to the employee, and the exercise price paid per share determined as if the purchase options exercised on the grant date. All that information is information you're going to need.

Now let's talk about disposition of employee stock purchase plan stock. Just like ISOs, the tax treatment depends on whether the disposition was a qualifying disposition or a non-qualifying disposition. It's the same test, right? Sale of stock acquired through an employee stock purchase plan is defined as a qualifying disposition if the sale takes place greater than two years after the grant date, and greater than one year after the exercise date, same as it is with ISOs, same timing period. If the time requirements are not met, then the sale is therefore by definition a non-qualifying, otherwise known as a disqualifying disposition. Pretty simple there.

This is where ESPPs can get in my mind to be some of the more difficult. So, I do think they're the most difficult in terms of tracking this stuff.

... This is a qualifying disposition. Sorry, I should back up and say that. Remember, with an ISO in a qualifying disposition, there is no ordinary income. You are only going to have long-term capital gain on stock that you acquire through an ISO. With an ESPP in a qualifying disposition, you're still going to have ordinary income recognition that will be reported on the employee's W-2, and will therefore, require a basis adjustment on the Form 8949. In a qualifying disposition of stock acquired through an ESPP, ordinary income is the lesser of the sale price minus the discounted purchase price, but it cannot be less than zero, or the fair market value of the stock at the grant date multiplied by the discount percentage offered. If you look . . . , I have...those two items set aside in a formula format there for you. And what I have is you show it lesser of A or B and then you go through each of those two calculations. Now let's go through an example of this.

This is Danica. On January 5, 2022, Danica was granted the right to purchase stock from her employer at a 15% discount through an employee stock purchase plan. The stock had a fair market value at the grant date of \$60 per share. On August 14, 2022, Danica exercised her purchase option, the end of her offering period, for 1,250 shares when the fair market value of the stock was \$62 per share. Danica paid \$52.70 per share, which is a \$62 fair market value on the exercise/purchase date reduced by the 15% discount. And so now we have our Form 3922. You'll notice the Form 3922 looks very similar to a Form 3921. Slightly different information though. Box one, we have our grant date. Box two, we have our exercise date. Box three, we have our fair market value on the grant date. Box four, we have our fair market value on the exercise date. Box five, we have our exercise price paid per share. Box six, number of shares transferred. Box seven, we have the date legal title has actually transferred. And then if we look at box eight, we have the exercise price paid per share determined as if the option was exercised on the date shown in box one, which is the grant date. And so if she had gotten a 15% discount on the fair market value at the grant date, she would have only paid \$51 per share. So now on January 10, 2024, Danica sold the 1,250 shares that she purchased

on August 14, 2022 for \$65 per share and because the January 10, 2024 disposition of the shares was made more than one year after the exercise date and more than two years after the grant date, Danica's sale is a qualifying disposition.

Notice now so the first step in the ESPP is let's calculate her overall gain. And then we'll move on to segregating that overall gain between the ordinary income component and the capital gain component. So she sold the stock for \$65 a share. From that, we subtract out her exercise price paid per share, \$52.70. And you see these in the box Form 3922 box five. She has total gain per share of \$12.30 multiplied by the 1,250 shares, her total gain is \$15,375.

Let's move on to the second part of the example. And now we've got to take our total gain of \$15,375 and break that up between our ordinary income component and our capital gain component. And so our ordinary income component, and this is the formula. . . , is we take the lesser of her sale proceeds, which is, and now I'm doing this on a total number now, not just per share. For sale proceeds of \$81,250, subtract out her discounted purchase price of \$65,875 gives us the ordinary income of \$15,375. If you'll notice, that is the full amount of the gain. But her ordinary income is the lesser of two items. So it's the lesser of that or the fair market value on grant multiplied by her discount of 15%, which gives us \$11,250. And so we see when we do that calculation, that lesser of A or B, her ordinary income ends up being \$11,250. Looking at the capital gain component now. Now we take her total gain. Now I'm back to showing this per share. Her total gain per share was \$12.30, which we saw in the first part of the example. Subtract out her ordinary income recognition, which turned out to be \$9 a share, leaving the remainder of \$4,125 as her capital gain component.

You could have done that otherwise by simply taking the total gain, subtracting the ordinary income that you figured out before, but I wanted to sort of do the long form on the example there. And that's how you calculate that. And so even on a qualifying disposition, like I said, at the top of the ESPP discussion, even a qualifying disposition is going to have an ordinary income component that is going to hit your client's W-2 and will, therefore, require a basis adjustment.

When you've got a non-qualifying disposition, the entire spread between the fair market value on the exercise date and the exercise price paid is taxed as ordinary income, and then, the remainder is taxed as capital gain. Let's walk through that example. Here the facts are the same as the previous example, except that Danica sold her stock on October 30, 2023. So she's not met the two-year holding period, and therefore, she has a non-qualifying disposition. And now I've reproduced the same exact Form 3922 as the prior example, same one, just kind of putting it in one place for you to make it easy. Now we say, let's look at the tax effects here. Sale proceeds per share were \$65 a share. We subtract out what she paid, \$52.70 a piece. Total gain, so her total gain doesn't change, right? Right, 15,375. What's going to change is going to be the ordinary income and the capital gain component. Now we have to move on to that part of the example. So same total gain, \$15,375. And so now we look at the ordinary income. We're going to take the fair market value of the stock on the exercise date, subtract out her exercise price paid, gives us our ordinary income component of \$9.30 a share for a total of \$11,625. And the reason for that is, like I said, that you see on the screen there, the entire spread between the fair market value on the exercise and the exercise price is taxed as ordinary income. And that leaves us with a smaller amount of capital gain.

So if we compare the last example ..., and the one that went [on to the next page], what we see is in both a qualifying and a non-qualifying disposition, we have an ordinary income component. But by waiting it out and selling the stock when you have a qualifying disposition, you're increasing the capital gain component, minimizing the ordinary income component.

Now let's move on to the ESPP and the basis adjustments on the Form 1099-B. Because just like the incentive stock options and the non-qualified stock options, the basis that you're going to get on the Form 1099-B is going to be equal to the exercise price actually paid for the shares. Whatever shows up on the W-2 as an ordinary income will not show up on the 1099-B. You need to make a basis adjustment when you report the sale of the stock on the Form 8949, which ultimately, obviously flows up to the schedule D. You see that on my second bullet point here. I know I've said it multiple times, bears repeating as many times as I can. . . , both qualifying and non-qualifying dispositions of stock acquired through an employee stock purchase plan can give rise to ordinary income reportable on the employee's W-2.

So a basis adjustment is always required. There would be only one exception to that, and that would be where you have stock purchased with no discount. If the stock is purchased with no discount, there would be no ordinary income and you would only have capital gain. I think that would be a pretty rare scenario.

Let's look at the example for the 1099-B. So the facts are the same as the previous example, Danica sold her stock at a non-qualifying disposition. I mean, really, how you get to the end result is going to be the same because you're going to have ordinary income component on both. So I'm using the non-qualifying disposition as my example here. And so in this situation, Danica's 1099-B is going to show us the 1,250 shares she sold on October 30, 2023. She acquired the stock on August 14, 2022. Her proceeds of \$65 a share are \$81,250. Her cost basis is what she paid for the shares, her exercise price, which shows the total gain of \$15,375, we saw that in our previous example, the total gain, \$15,375. But in our example, both examples, qualifying and non-qualifying, where there's an ordinary income component, and the non-qualifying disposition, our ordinary income component, if you remember, was \$11,625. Once again, on the Form 8949, we see that as an adjustment here. Column F, B as in boy is the code. And we reduce the gain by the \$11,625, that she had picked up on her W-2.

Let's move on away from ESPPs and on to restricted stock units (RSUs). After ESPPs, boy, restricted stock units sure seem really easy at this point. Now, when it comes to restricted stock units, . . . RSUs, there is no income recognition on the grant date. RSUs, they're unlike ISOs, non-qualifying stock options or ESPPs. RSUs typically are not purchased by the employee. I think I've seen a client before have to purchase them, but I can't remember. The vast, vast majority, I'll tell you that I see the employee does not have to pay anything for an RSU. It is simply a form of compensation. They're automatically received by the employee through a vesting schedule. So the date the stock is granted, there is no income recognition. The reason there is no income recognition is very similar to the non -qualified stock options, if you remember. And we're looking at section 83(a). There may be a readily determinable fair market value on the grant date. The first part of section 83(a), but our client does not have a non-forfeitable right. They haven't actually received the stock yet. It hasn't come to them yet. They've only been granted the options. Ordinary income though is recognized as an RSU vests. Because once you meet the vesting schedule in an RSU, as soon as shares vest, they're transferred to your client's brokerage account from the employer. And at that point, you have a readily determinable fair market value and you have a non-forfeitable right. It's totally vested. So you must recognize the fair market value of that asset on the date vested. Hey, that's the very definition of section 83(a).

Like non-qualified options, income recognition is governed by section 83, where the vesting date is the date the stock is no longer subject to a substantial risk of forfeiture. And because RSUs are taxed as ordinary income, when they vest, that fair market value investing is reported on our clients W-2 or 1099-NEC if they're vested in someone who's not an employee. And the income is subject to Social Security and Medicare tax.

When we dispose of RSUs, in addition to the ordinary income that we've recognized in our W-2, the sale of stock acquired through an RSU is capital gain. Calculated very simply, what's the fair market value on the vesting date? Subtract that from the sale proceeds, and it can either be short term or long term, depending on how long we've held the stock. If we held the stock for one year or less, short term; greater than one year, long term. It's the identical calculation to non-qualifying options just substitute quote the exercise date from the vesting date. Because our client doesn't actually exercise the RSUs, they simply vest and they get them automatically.

... I want to mention something--practice pointer. ... It's very common in the RSU area for your client to not actually receive into their brokerage account the number of vested units they received. That's because the vast, vast, vast majority of clients will use what they call cashless vesting, otherwise called cashless exercise. Sometimes it's called sell to cover. And so when your client gets, say, 100 shares of vesting, maybe they're only getting 60 sent into their account. The other 40 are being sort of sold right away or just not given to them and are held back by the employer to cover the withholding, both the federal and state income tax withholding, as well as Social Security and Medicare tax withholding on the vesting, so that your client isn't having to come out of pocket with other funds to pay for the rest of that. So it's referred to as a cashless vest. And in that respect, I have found that sometimes RSUs can be a little difficult to track for your client. Your client says, well, I had X amount of shares vested, and then you go and you try to track that dollar amount over to their brokerage account, and you're not going to see that dollar amount. You're going to see some other amount of shares because of that cashless vest, the way that works.

Let's talk about the 1099-B for RSUs, the basis shown on 1099-B is the fair market value of the shares on the vesting date. So if you have basis shown on a 1099-B for RSUs, then that basis should be accurate, and you can just report what shows up on the 1099-B because what shows up with 1099-B has already showed up on the W-2 as ordinary income. . . . The sale of RSUs are treated as a non-covered transaction, which means that basis doesn't have to be reported to the IRS, which means it might not show up on a 1099-B. If you get an RSU, and you don't have basis that shows up on the 1099-B, then you are going to have to go track down how much ordinary income was reported on the W-2. Then you're going to have to make that basis adjustment on the 8949. But if you get our RSU shares that are sold and you do see basis reported on that 1099-B, it's going to be accurate. You can just report what's on the 1099-B.

So similar to RSUs, RSAs are a form of equity compensation that often do not have to be separately purchased by the employee, but there are plans out there that do require them to be purchased. I think I've seen RSAs that clients have to purchase much more often than I've ever seen in an RSU. But RSAs, maybe your client has to purchase them, maybe not. The big difference between RSUs and RSAs is that with an RSU, the employee doesn't actually receive the stock upfront. They don't receive the stock until the end of their vesting period for that stock. And then as the stock vests, I say it's 20 shares a year, every year they get 20 shares into their account. And that's when they get the stock.

RSAs are sort of flipped. They're sort of backwards. With a restricted stock award, the employee is given the stock upfront on the grant date, but if they don't meet some condition, some vesting condition, then they either have to forfeit the stock, give it back, or if they did have to purchase the RSA, then the employer will purchase it back from them, you know, whatever, whatever terms are agreed upon in the RSA grant if the vesting conditions are not met. So RSAs, you don't get stock upfront, you get stock at the end. RSAs, you get the stock upfront, but if you don't meet the vesting schedule, you have to give it up or it is bought back by the employer, but you do get it upfront. Why that matters for us, as you'll see when we get to the §83(b) election, §83(b) election is not available for RSUs, but it is available for RSAs. And that's a big difference, I think, between these two. There I am. See, I get ahead of myself in my discussion. Because stock is received by the employee on the grant of an RSA, the section §83(b) election is available. It's not available for RSUs. And we'll talk about that later.

RSAs. So even though the stock is received on the grant date, the employee doesn't actually have any income recognition because why? Even though they received the stock, it is still subject to a substantial risk of forfeiture. They don't meet the vesting conditions, they're going to lose the stock. It's going to be sold back or it's going to be just given up altogether. So you still with an RSA, even though you're getting the stock upfront, you do not have any income recognition on the grant date. But then once the vesting conditions are met, the employee does recognize ordinary income, which is equal to whatever the fair market value is at the end of the vesting period, right? Not at the beginning, because once you meet the two requirements of section 83(a), no longer subject to a substantial risk of forfeiture, and you have readily determined fair market value, it's on that date that the fair market value and the ordinary income is determined.

Let's talk about W-2 reporting when it comes to all of these incentive stock plans. I have a chart for the W-2 reporting for all of these. And so for example, if I look at the ISOs, on this chart, what is the date the stock is actually received by the employee? With ISOs, we see it's when the ISO is exercised. Same thing with non-qualified. ESPP is the date the employee purchases the stock. RSU is the date actually received at the end of the vesting period. RSA is the beginning of the vesting period. Phantom stock and stock appreciation rights, they never actually receive any stock. And then what I've got here is rows, for which of these are, which of these types of stock incentive plans are subject to Social Security and Medicare tax. What is the disclosure that you're going to see on a W-2? I will tell you, non-qualified stock options require a code of V as Victor in box 12 of the W-2. The rest of them, you may see some kind of disclosure in box 14, and I've got common codes. Whatever shows up in box 14 is just a disclosure item. It's not required to be shown on W-2. If it is, though, I've shown some of the common items.

Let's talk about those two elections, §83(b) and §83(i). Section §83(b) allows the employee to elect to include the fair market values of their stock in ordinary income on the grant date, which is going to be an earlier date than the stock would ordinarily be subject to income recognition.

Think about the example we just went over with Lee with RSAs and how that works. It would work the same for any of the type of incentive stock plans for which an §83(b) election is allowed. And just if I'm looking at my chart, §83(b) elections are allowed for ISOs, non-qualified options, and RSAs. They are not allowed for ESPPs. They're not allowed for RSAs. So ISOs, non-qualified options, and RSAs. Quick hit chart on which ones are allowed in the §83(b) election. So the whole point of the §83(b) election is to try to minimize the income recognized, the ordinary income recognition, by electing to be taxed in the stock when it has a much lower value. Now, I've got a list of all the risks.

What is the risk of an §83(b) election? Well, one, it's an irrevocable election. You cannot unwind it, which means, let's say you elect to be taxed on ordinary income today. Think about my example with Lee. It picks up ordinary income, but then he's fired or he leaves the company before he meets his vesting conditions. He doesn't get that money back. He doesn't get a deduction. He just, he simply picked up income that he never had to pick up. And that's a risk of an §83(b) election. Also, if the stock drops in value. Doesn't matter. I mean, you're going to have basis in that stock from what you had purchased it for or what you recognize as ordinary income earlier, I should say, but you don't get anything back. You've lost something by picking up income earlier. And because you're electing to be taxed on the grant date, you haven't actually received anything yet. You don't have anything you can sell yet, which means you've got to come out of pocket with some other money in order to pay the tax liability generated by an §83(b) election. Go back to the example with Lee on the RSAs and think about those risks in terms of that example.

The timing of an §83(b) election. The election must be filed with the IRS within 30 days of the grant. And because of that, it's really rare for me to have a client who comes to me and asks me to file it. What's much more common is...when the employee is given their grant, they're given all of their grant documents from their employer to sign. Typically, one of those things is an §83(b) election, because the employer will tell them, an §83(b) election is available here, and here's why you should make the election. Most people will make it if it's available to them. And so it is typically signed and filed then and there with the IRS by the employer. You can only revoke it with IRS consent.

I will say when it comes to the §83(b) election, I think it's before 2016, you had to also attach a copy of the §83(b) election to the tax return for the year it was made. You don't have to do that starting in 2016. And so for us, I'll tell you that's one of the areas where I'll ask a client, did you make an §83(b) election if they're a new client? They don't know or they don't remember, and they've got to dig. Sometimes they have to dig back to documents that are a decade old. And sometimes they don't keep them. And it can be very difficult to figure out whether they even made an §83(b) election. You sort of have to put them on the scavenger hunt with their employer, sometimes a former employer, to go figure out if an §83(b) election was filed. Or, you're going to have to get a power of attorney and call the IRS and figure that whole thing out.

A couple of miscellaneous issues with the §83(b) election. I already said that with the election. If you do have a client who asks you to make an election and you say, how do I make an §83(b) election? Rev.Proc. 2012-29 has a sample election in it. I know it's an old Rev. Proc., but that's the latest sample election the IRS has published. Pretty simple. Just grab that and copy. It actually has a sample. You can just copy that into a Word document and just fill in the blank lines.

Moving on to §83(i) election, it's called a qualified equity grant. This came about with the Tax Cuts and Jobs Act in 2018. With an §83(b) election, we're electing to be taxed sooner than we have to be. With an 83(i) election, we're electing to be taxed later than we have to be. And where this becomes a good election is when you've got an employer who is not publicly traded, right? How do you determine a fair market value? Maybe you get your stock and you're supposed to be taxed on it today, but you can't turn around and sell it because the company's not being sold on an exchange. So what are you supposed to do? So §83(i) allows you to wait until a later date to have income recognition ordinary income recognition. It only applies to private corporations that do not have stock readily available on an established securities market and have a written plan under which at least 80% of all employees are granted stock options or RSUs. If the election is made by the employee, then ordinary income is recognized, and therefore W-2 inclusion, on the earliest of the dates that start on the bullet points . . . ,. The date the qualified stock becomes transferable, the date the employee first becomes an excluded employee, the first date on which the stock of the corporation does become readily tradable on an exchange, so you become a public company. The date that is five

years after the first date, the rights of the employee and the stock are transferable or are not subject to a substantial risk of forfeiture. So the $\S83(i)$ election can essentially push out your ordinary income recognition as far as five years at the max. Or the date the employee revokes the election. We've got a list of ineligible employees. Also . . . , which employees are not eligible to make the election? 1% owners of the business, anybody who's been the chief executive or chief financial officer, and then there's a few other excluded employees who are not allowed to make the $\S83(i)$ election.

SUPPLEMENTAL MATERIALS

Incentive Stock Options: Part II

A. ALTERNATIVE MINIMUM TAX

Incentive stock options (ISOs) are the only type of stock incentive plan that requires an AMT adjustment. The amount by which the fair market value (on the exercise date) of shares acquired through an ISO exceeds the exercise price paid for those shares constitutes a preference item for AMT purposes and must be reported on line 2i of Form 6251, Alternative Minimum Tax – Individuals. (IRC §56(b)(3))

Taxpayers must receive Form 3921, Exercise of an Incentive Stock Option Under Section 422(b), by January 31 of the year after they exercise an incentive stock option. Using the Form 3921, the AMT adjustment is:

FMV of shares on Exercise price paid Number of shares

exercise date - per share × exercised = AMT adjustment

(Form 3921, box 4) (Form 3921, box 3) (Form 3921, box 5)

Practice Pointer

No AMT adjustments are required for shares of stock that are sold in the same year they are exercised in an ISO.

AMT basis of shares acquired through an ISO

Taxpayers must increase their AMT basis in any stock acquired by exercising an ISO by the amount of the AMT adjustment.

Example AMT basis

Joshua was granted an incentive stock option by his employer on September 1, 2022, for 5,000 shares with an exercise price of \$32 per shares. On July 12, 2023, he exercised the option for all 5,000 shares when the fair market value of the stock was \$39 per share.

Joshua received the following Form 3921 by January 31, 2024:

	☐ CORRE	ECTED (if checked)		_
TRANSFEROR'S name, street address, city or town, state or province, country, and ZIP or foreign postal code		1 Date option granted	OMB No. 1545-2129	Evereine of on
Employer		0/4/0000	Form 3921	Exercise of an Incentive Stock
One First Street		9/1/2022 2 Date option exercised	101111 0921	Option Under
Anaheim, CA 92801			(D. O. I. I. O. I. I.	Section 422(b)
		7/12/2023	(Rev. October 2017)	
TRANSFEROR'S TIN	EMPLOYEE'S TIN	3 Exercise price per share	4 Fair market value per sha	re Copy B
12-3456789	987-65-4321	100	on exercise date	For Employee
EMPLOYEE'S name		\$ 32.00	\$ 39	.00 This is important tax
Joshua Employee		5 No. of shares transferred		information and is being furnished to the
Street address (including apt. no.)		5,000 6 If other than TRANSFEROR,	name address and TIN of	IRS. If you are required to file a return, a
123 Main Street		corporation whose stock is b		negligence penalty or
City or town, state or province, country	and ZIP or foreign postal code			other sanction may be imposed on you if this
Anaheim, CA 92801	,			item is required to be reported and the IRS
Account number (see instructions)		1		determines that it has
				not been reported.
Form 3921 (Rev. October 2017) (keep for your records) www.irs.gov/Form392		www.irs.gov/Form3921	Department of the Treasu	ury - Internal Revenue Service
	Example AN	AT basis (Continued)		
Joshua's AMT adjustn	nent is:			
			\$ 39.00	
FMV	FMV of shares of exercise date (Form 3921			
Exercise price paid per share (Form 3		Form 3921, box 3)	<u>- 32.00</u>	
AMT adjustment per shares			7.00	
Number of shares exercised (Form 3921, box 5)		orm 3921, box 5)	× 5,000	
AMT	AMT adjustment (Form 6251, line 2i)		\$35,000	
Joshua must increase his AMT basis by the amount of his AMT adjustment (\$7 per share).				

AMT credits

Taxpayers who must pay the alternative minimum tax due to the exercise of incentive stock options can file Form 8801, Credit for Prior Year Minimum Tax — Individuals, Estates and Trusts, in subsequent years and claim an AMT credit. The AMT credit is claimed in taxable years when the taxpayer is not subject to AMT and is essentially a refund of alternative minimum taxes paid in prior years.

Alternative minimum taxes are caused by two types of adjustments and preference items:

- Deferral items; and
- Exclusion items.

Deferral items generally don't cause a permanent difference between regular taxable income and alternative minimum taxable income over time. Examples include regular versus AMT depreciation and the adjustment for the exercise of incentive stock options, among others.

Exclusion items include:

• Certain itemized deductions (including any investment interest expense reported on Schedule E);

- Certain tax-exempt interest;
- Depletion;
- The qualified small business stock exclusion under IRC §1202;
- The standard deduction; and
- Any other adjustments related to exclusion items (such as taxable refunds reported on Schedule 1).

Exclusion items can be found on Form 6251 on lines 2a, 2b, 2c, 2d, 2g, and 2h.

The minimum tax credit is only allowed for alternative minimum taxes caused by deferral items — it is not allowed for alternative minimum taxes caused by exclusion items.

\$100,000 ANNUAL ISO LIMIT

Taxpayers are subject to a \$100,000 annual limit on the aggregate fair market value of incentive stock options *exercisable* for the first time during the calendar year. (IRC §422(d)) If the \$100,000 limit is exceeded during the year, then the remaining exercisable options during the year are treated as nonqualified stock options (NQSOs).

Example of \$100,00 limit

On January 1, 2021, Valentina's company granted her the right to purchase 30,000 shares of its stock through an incentive stock option plan with a grant price of \$20 per share.

The options vest (aka become exercisable) over a four-year period. Valentina began exercising her options on January 1, 2022. She determines if the annual \$100,000 exercise limit has been exceeded as follows:

Vest date	Shares vested	Grant price per shares	Total grant price	Value over \$100k limit	Shares exercised over limit ¹	ISO shares granted
1/1/22	7,500	\$20	\$150,000	\$50,000	2,500	5,000
1/1/23	7,500	\$20	\$150,000	\$50,000	2,500	5,000
1/1/24	7,500	\$20	\$150,000	\$50,000	2,500	5,000
1/1/25	7,500	\$20	\$150,000	\$50,000	2,500	5,000
Totals	30,000				10,000	20,000
¹ Treated a	as NOSO sha	res				•

Valentina exceeded the \$100,000 limit by \$50,000 each year (or 2,500 shares). As such, 2,500 shares per year are treated as nonqualified stock options.

NONQUALIFIED STOCK OPTIONS (NQSOS) (AKA NONSTATUTORY STOCK OPTIONS)

An employee does not recognize income when a nonqualified stock option is granted (the grant date) unless the stock has:

- A readily ascertainable fair market value when granted; and
- The stock is not subject to a substantial risk of forfeiture. (IRC §83(a))

Comment

IRC §83 governs the tax rules for property transferred in connection with the performance of services. In its simplest form, IRC §83(a) provides that if an employee receives something of value (other than cash or a cash equivalent) in exchange for their services (the work they perform as an employee), then they must recognize ordinary income equal to the fair market value of the property they received.

For example, if an employer pays an employee one share of stock valued at \$1,000 instead of paying the employee \$1,000 cash (or cash equivalent), then the employee must recognize \$1,000 of ordinary income, which is reportable on the employee's W-2. In our emerging cryptocurrency world, this is also the required treatment when employees are paid in cryptocurrency instead of real currency.

In practice, nonqualified stock options typically require an employee to exercise a previously granted option. The exercise date becomes the date that the stock has a readily ascertainable value and is no longer subject to a substantial risk of forfeiture, and the option is therefore taxed on the exercise date.

An employee recognizes ordinary income in the year in which a nonqualified stock option is exercised. (IRC §83(a)) The ordinary income is calculated by subtracting the employee's exercise price from the fair market value of the stock purchased on the exercise date. The ordinary income should be reported on the employee's W-2 (Form 1099-NEC if the nonqualified stock option is exercised by someone who is not an employee).

The ordinary income reported on an employee's W-2 upon the exercise of a nonqualified stock option is subject to Social Security and Medicare taxes. When the ordinary income is reported on Form 1099-NEC for someone who is not an employee, the income recognized from the exercise of the nonqualfied stock options is subject to self-employment tax.

No AMT adjustment on exercise of nonqualified stock options

Remember, only ISOs are subject to AMT adjustments. There is no AMT adjustment upon the exercise of nonqualified stock options.

Practice Pointer

The amount of ordinary income recognized upon the exercise of a nonqualified stock option is calculated in exactly the same manner as the alternative minimum tax preference item adjustment upon the exercise of an incentive stock option:

Fair market value of stock on exercise date	\$100
Exercise price paid by the employee	<u>- 75</u>
Ordinary income reported on W-2/1099-NEC ¹	\$ 25

¹ If nonqualified stock option

Form 3921 is issued to an employee for the year in which an incentive stock option is exercised, but a similar form is not issued upon the exercise of a nonqualified stock option. A corporation may provide the taxpayer exercising the nonqualified stock option a statement that contains similar information, but it is not an official IRS form like the Form 3921.

DISPOSITION OF STOCK ACQUIRED THROUGH NONQUALIFIED STOCK OPTIONS

In addition to the ordinary income recognized on the exercise of a nonqualified stock option, taxpayers must recognize capital gain (or loss) calculated by subtracting the fair market value of the stock on the exercise date (the date when ordinary income was recognized) from the sale proceeds of the stock, as follows:

Sale proceeds - FMV on exercise = Capital gain (IRC §1222)

The capital gain or loss is classified as long-term if the shares are held for more than one year from the exercise date to the date of disposition. (IRC §1222(4))

Example of disposition of stock acquired through nonqualified stock options

On January 30, 2021, Fiona's employer granted her 5,000 shares of stock through a NQSO with an exercise price of \$12 per share. On January 5, 2022, she exercised her option to purchase the 5,000 shares at the fair market value on the exercise date of \$27 per share.

On April 15, 2023, Fiona sold 1,200 of the shares for \$24 per share.

Fiona's ordinary income reported in 2022 is calculated as follows:

Fair market value per share on exercise date	\$ 27.00*
Exercise price paid per share	<u>- 12.00</u>
Ordinary income per share	15.00
Number of shares exercised	× 5,000
Total ordinary income reported on Fiona's 2022 W-2	\$75,000

^{*} Fiona's basis per share used to calculate her capital gain when the shares are ultimately sold

Fiona sold her shares for \$24 per share, which represents a \$3 loss per share (\$24 sale price per share - \$27 fair market value on exercise date). Fiona held her shares for more than one year after her exercise date, so her loss is a long-term capital loss calculated as follows:

Sale proceeds per share	\$ 24.00
Fair market value per share on exercise date	<u>- 27.00</u>
Capital loss per share	(3.00)
Number of shares sold	× 1,200
Long-term capital loss	(\$ 3,600)

BASIS REPORTED ON FORM 1099-B (NQSOs)

When an employee exercises nonqualified stock options, the shares are transferred into the employee's brokerage account. The cost basis provided in the employee's brokerage account (as well as on Form 1099-B when the shares are sold) is the exercise price paid for the shares.

However, the true cost basis for shares acquired through the exercise of nonqualified stock options includes the amount paid for the stock plus the difference between the fair market value at exercise and the exercise price (the amount reported on Form W-2 or 1099-NEC if the person is not an employee).

Example of Form 1099-B basis adjustments on sale of stock acquired through nonqualified stock option plan

The facts are the same as the previous example. Fiona's 1099-B on the sale of her stock will contain the following relevant information:

Shares sold	Date sold	Date acquired	Proceeds	Cost basis	Gain (loss)	
1,200	4/15/2023	1/5/2022	\$28,800*	\$14,400**	\$14,400	
* 1,200 shares × \$24 per share						
** 1,200 shares × \$	S12 per share e	exercise price				

If Fiona's tax professional simply reports capital gain on her income tax return as shown on her Form 1099-B, then she will report \$14,400 of capital gain from the sale of the 1,200 shares. However, as the previous example illustrates, she actually has a \$3,600 capital loss on the sale of the shares.

The \$15 of ordinary income recognized per share (calculated in the previous example) and reported on Fiona's 2022 W-2 must be added to the basis shown on her 1099-B. The basis is added on Form 8949 using code "B" in column (f), as follows:

				Attach	ment Sequence No.	12A	Page 2
iame(s) shown on return. Name and SSN or taxpayer identification no, not required if shown on other side				Social security number or taxpayer identification number 123-45-6789			er
tion as Form 10							
			eld more than 1	1 year are	generally long-	-term (se	e
which no ad	justments o	r codes are re	quired. Enter th	ne totals d	irectly on Sche		
or each applica	able box. If y	ou have more lo	ng-term transac				
reported on l	Form(s) 1099	-B showing bas	· · · · · · · · · · · · · · · · · · ·		•	e)	
(b)	(c) Date sold or	Proceeds See		st or other basis enter a code in column (f). Gain or (loss)			ilumn (e)
(Mo., day, yr.)	disposed of (Mo., day, yr.)	(sales price) (see instructions)	and see Column (e) In the separate Instructions.	(f) Code(s) from Instructions	(g) Amount of adjustment	combine the with column	ne result
	ow, see whether attorn as Form 11 oox to check acctions invo whort-term traggregate all low which no adjuired to report or each application and form of the control of the	ow, see whether you received attion as Form 1099-B. Either took to check. sactions involving capitathort-term transactions, gregate all long-term travhich no adjustments of usined to report these trained to report the same or each applicable box. If you many forms with the same or reported on Form(s) 1096 or reported on Form(s) 1096 or reported to you on Form the part of the souling that the same of the same of the same of the souling that the same of the s	ow, see whether you received any Form(s) 1099- attion as Form 1099-B. Either will show whether box to check. sactions involving capital assets you he short-term transactions, see page 1. gregate all long-term transactions repo which no adjustments or codes are re- sired to report these transactions on Fo below. Check only one box. If more than or each applicable box. If you have more to many forms with the same box checked as as reported on Form(s) 1099-B showing bas as reported on Form(s) 1099-B showing bas as not reported to you on Form 1099-B (d) Date sold or Idea of the codes (sales price)	ow, see whether you received any Form(s) 1099-B or substitute station as Form 1099-B. Either will show whether your basis (usually own to check. Sactions involving capital assets you held more than short-term transactions, see page 1. gregate all long-term transactions reported on Form(which no adjustments or codes are required. Enter the sired to report these transactions on Form 8949 (see below. Check only one box. If more than one box applies or each applicable box. If you have more long-term transactions on Form 8949 (see below. Check only one box. If more than one box applies or each applicable box. If you have more long-term transactions on Form 8949 (see below any forms with the same box checked as you need. It is reported on Form(s) 1099-B showing basis wasn't report is not reported to you on Form 1099-B (b) (c) (c) (d) Proceeds (sales price) Cost or other basis See the Note below and see Column (e) (Mo., day, yr.) (Mo., day, yr.) (Mo., day, yr.) (In the separate in the service of the selection of the selecti	taxpayer identification no. not required if shown on other side Social security number of the provided and security number of the provide	taxpayer identification no. not required if shown on other side 123-45-6789 In the second of the s	www. see whether you received any Form(s) 1099-B or substitute statement(s) from your broker. A substitute statement on a Form 1099-B. Either will show whether your basis (usually your cost) was reported to the IRS by your cost to check. sactions involving capital assets you held more than 1 year are generally long-term (see short-term transactions, see page 1. gregate all long-term transactions reported on Form(s) 1099-B showing basis was repwhich no adjustments or codes are required. Enter the totals directly on Schedule D, sired to report these transactions on Form 8949 (see instructions). below. Check only one box. If more than one box applies for your long-term transactions, core ach applicable box. If you have more long-term transactions than will fit on this page for one many forms with the same box checked as you need. s reported on Form(s) 1099-B showing basis was reported to the IRS (see Note above) are ported on Form(s) 1099-B showing basis was reported to the IRS (see Note above) s reported on Form(s) 1099-B showing basis was reported to the IRS (see Note above) s reported to you on Form 1099-B (a) (b) Date adulted (Mo., day, yr.) (c) (c) (d) (d) (e) Cost or other basis See the Note below Adjustment, if any, to gain or loss if you enter an amount in column (g), enter a code in column (g), enter a

COMPARISON OF ISOS AND NOSOS

Comparison of ISOs and NQSOs					
	ISO	NQSO			
Who is eligible to receive?	Employees only	Anyone (employees, directors, consultants, etc.)			
Are there restrictions based on the option price?	Yes. By statute, the option price cannot be less than the FMV on the grant date	Yes. Generally, the option price is equal to the FMV on the grant date. If the option price is set lower than the FMV, then IRC §409A will apply			
Are there timing restrictions?	Yes. Options must be granted within 10 years of the plan's adoption, and the exercise period cannot be longer than 10 years from the date of the grant	No – But most plans contain a 10- year maximum exercise period			
Are there restrictions on the exercise price?	Yes. Only \$100,000 can be exercisable in any calendar year (based on the FMV on the grant date). Any exercisable amount over this threshold is treated as a NQSO	No			
Are the options taxed on the exercise date?	Not for regular tax purposes, but there is an AMT adjustment. See discussion on page 7	Yes.			
Is the stock acquired through the option taxed when sold?	Yes. The taxation depends on whether the disposition is a qualifying or nonqualifying disposition.	Yes.			

EMPLOYEE STOCK PURCHASE PLANS (ESPPS)

Employee stock purchase plans are similar to incentive stock options (ISOs). Both are defined as statutory stock options, and both require the issuance of an IRS form upon exercise:

- Upon exercise of an ISO: Form 3921, Exercise of an Incentive Stock Option Under Section 422(b); or
- Upon exercise of an ESPP: Form 3922, Transfer of Stock Acquired Through an Employee Stock Purchase Plan Under Section 423(c).

ESPPs are elective programs that allow employees to elect to purchase shares of company stock at a discount. The discount is usually between 5%–15% of the stock's fair market value on the grant date.

Employees will have an enrollment period where they select a percentage of their wages to be used to purchase shares at the end of an offering period. On the last day of the offering period, the total sum accumulated from the employee's contributions withheld from their paycheck are used to purchase the company stock. The date the shares are actually purchased is the exercise date.

Comment

Paycheck withholding for the purpose of purchasing stock through an ESPP plan is post-tax.

An employee does not have taxable income either on the grant date or on the exercise date of an employee stock purchase plan.

Example of employee stock purchase plan

Jackson's employer offers an employee stock purchase plan. Under the terms of the plan, any funds set aside from the employee's wages during the offering period are used to purchase company stock at a 15% discount based on the stock's fair market value on the grant date (which is also the first day of the offering period under the terms of the plan). The fair market value of the employer's stock at the beginning of the current offering period is \$100 per share.

During the current offering period, Jackson has set aside \$9,000 from his paycheck through the ESPP. After applying the 15% discount rate, Jackson's exercise price per share is \$85 (\$100 per share FMV on the grant date x 15% discount rate).

Jackson received 105.88 shares at the end of the offering period, calculated as follows:

Paycheck withholding set aside for ESPP	\$9,000
Exercise price per share	<u>÷ 85</u>
Number of shares purchased by Jackson	105.88

Even if Jackson does not hold the shares of stock he acquired through the ESPP and instead sells them right away, he has received an immediate 15% gain on his money. It only costs him \$85 to purchase a share of stock worth \$100.

The offering period is specified in the plan documents and can be one month, a calendar quarter, or a year, for example.

FORM 3922

Employers must issue Form 3922, Transfer of Stock Acquired Through an Employee Stock Purchase Plan Under Section 423(c), by January 31 of the calendar year following the calendar year in which an employee purchases stock through an ESPP. Form 3922 provides the following relevant information that is used to calculate the employee's

ordinary income upon purchase of their employer's stock as well as taxable gain when the stock is ultimately sold by the employee:

- Grant date;
- Exercise date;
- Fair market value per share on the grant date;
- Fair market value per share on the exercise date;
- Exercise price paid per share;
- Number of shares transferred to the employee;
- Date legal title to the stock is transferred to the employee; and
- Exercise price per share determined as if the purchase option was exercised on the grant date.

An employee must receive a different Form 3922 for each stock block purchased during the year. For example, if an employee purchases two different blocks of employer stock on two different dates during the 2023 calendar year, then the employee must receive two separate Forms 3922 by January 31, 2024.

DISPOSITION OF STOCK ACQUIRED THROUGH AN ESPP

Like incentive stock options, the employee's federal tax treatment upon disposition of stock acquired through an employee stock purchase plan depends on whether the disposition is a qualifying or nonqualifying disposition.

A qualifying disposition occurs if the sale or other disposition of the stock takes place:

- More than two years after the date the ESPP option to purchase the stock was granted for the particular shares involved in the disposition; and
- More than one year after the date the option was exercised to purchase those shares. (IRC §422(a))

If both requirements are met, then the disposition is a qualifying disposition. Otherwise, the disposition is a nonqualifying disposition.

Tax treatment of qualifying dispositions

The employee recognizes ordinary income equal to the *lesser* of (A) or (B):

(A) Sale proceeds – Discounted purchase price = Ordinary income (not less than zero)

(B) FMV of stock at beginning of offering period (grant date) × Discount percentage = Ordinary income (not less than zero)

This calculation must be performed for each separate purchase lot of the shares sold. The remaining gain is classified as capital gain.

Example of ESPP qualifying disposition

On January 5, 2022, Danica was granted the right to purchase stock from her employer at a 15% discount through an employee stock purchase plan. The stock had a fair market value at the grant date of \$60 per share.

On August 14, 2022, Danica exercised her purchase option for 1,250 shares when the fair market value of the stock was \$62 per share. Danica paid \$52.70 per share (\$62 fair market value on exercise/purchase date – 15% discount).

Danica received the following Form 3922 by January 31, 2023:					
2626					
CORPORATION'S name, street address, city or town, state or province,		1 Date option granted	OMB No. 1545-2129	Transfer of Stock	
country, and ZIP or foreign posta	l code	D. F. S. G. C. S.		Acquired Through	
		1/5/2022	Form 3922	an Employee	
Employer		2 Date option exercised		Stock Purchase Plan Under	
One First Street		2446222	(Rev. September 2016)	Section 423(c)	
Anaheim, CA 92801 CORPORATION'S federal identification number EMPLOYEE'S identification number		8/14/2022 3 Fair market value per share	4 Fair market value per sha		
12-3456789 987-65-4321		on grant date	on exercise date	For	
EMPLOYEE'S name		\$ 60.00	\$ 62	.00 Internal Revenue	
		5 Exercise price paid per share	6 No. of shares transferred	Comica Conton	
Danica Employee		\$ 52.70	1,250	File with Form 1096.	
Street address (including apt. no.)		7 Date legal title transferred		For Privacy Act and	
123 Main Street		0.0450		Paperwork Reduction Act Notice, see the	
City or town, state or province, country, and ZIP or foreign postal code		8/14/2022 current version of the			
Anaheim, CA 92801 Account number (see instructions)				General Instructions for Certain Information	
Account number (see instructions)		Returns. \$ 51.00			
Form 3922 (Rev. 9-2016) Cat. No. 41180P www.irs.gov/form3922 Department of the Treasury - Internal Revenue Service Do Not Cut or Separate Forms on This Page — Do Not Cut or Separate Forms on This Page					
Example of ESPP qualifying disposition (Continued)					
On January 10, 2024, Danica sold the 1,250 shares that she purchased on August 14, 2022, for \$65 per share.					
Because the January 10, 2024, disposition of the shares was made more than one year after the August 14, 2022, exercise/purchase date and two years after the January 5, 2022, grant date, Danica's sale is a qualifying disposition. For federal tax purposes, Danica will recognize total gain calculated as follows:					
Sale 1		\$ 65.00			
Exerc	ise price paid per share (Form	n 3922, box 5)	<u>- 52.70</u>		
Total	gain per share		12.30		
Numl	per of shares sold		<u>× 1,250</u>		
Total gain on sale of stock			\$15,375		
The total gain of \$15,375 must be broken out between ordinary income and capital gain, calculated as follows:					
Ordinary income component					
Lesser of:					
(A) S	Sale proceeds (\$65.00 per share × 1,250 shares)			\$81,250	
Discounted purchase price (\$52.70 per share × 1,250 shares)		shares) <u>- 65,87</u>	<u>- 65,875</u>		
Ordinary income (\$12.30 per sha		hare)	\$15,37	\$15,375	
or					

Supplemental Materials		CPE Network® Tax Report
(B)	FMV at grant date ¹ (\$60.00 per share × 1,250 shares)	\$75,000
	Discounted purchase price ² (\$51.00 per share)	<u>× 15%</u>
	Ordinary income (\$9.00 per share)	\$11,250
	¹ Form 3922, box 3 × number of shares sold ² Form 3922, box 8	
Capital gain compo	nent	
То	tal gain per share	\$ 12.30
Or	dinary income recognized per share	<u>- 9.00</u>
Lo	ng-term capital gain per share	3.30
Nu	umber of shares sold	<u>× 1,250</u>
То	tal long-term capital gain on qualifying ESPP disposition	\$ 4,125

Tax treatment of nonqualifying dispositions

If the holding periods are not met before ESPP stock is sold (more than two years after the grant date and more than one year after the exercise date), then the entire spread between the fair market value on the exercise date and the exercise price paid per share is taxed as ordinary income.

Example of ESPP nonqualifying disposition

The facts are the same as the previous example, except that Danica sold her stock on October 30, 2023, so she has not met the two-year holding period from the date her ESPP options were granted.

Danica's Form 3922 received by January 31, 2023, is the same as from the previous example:

Country, and ZIP or foreign postal code 1/5/2022 Employer One First Street Anaheim, CA 92801 CORPORATION'S federal identification number 12-3456789 EMPLOYEE'S name Stephology	5P5P	VOID CORF	RECTED		
Employer One First Street Anaheim, CA 92801 CORPORATION'S federal identification number 12-3456789 EMPLOYEE'S name EMPLOYEE'S name Step on grant date \$ 60.00 \$ 62.00			1 Date option granted	OMB No. 1545-2129	Transfer of Stock
Employer One First Street Anaheim, CA 92801 CORPORATION'S federal identification number 12-3456789 EMPLOYEE'S identification number 987-65-4321 EMPLOYEE'S name \$ 60.00 \$ 62.00 5 Exercise price paid per share 6 No. of shares transferred File with Form Street address (including apt. no.)	soundly, and 211 or lorsign postal cou	•		Form 3922	Acquired Through an Employee
Anaheim, CA 92801 CORPORATION'S federal identification number 12-3456789 EMPLOYEE'S name Section 2 3 Fair market value per share on grant date on grant date \$ 60.00 \$ 62.00 5 Exercise price paid per share 7 Date legal title transferred 7 Date legal title transferred			2 Date option exercised		Plan Under
12-3456789 987-65-4321 on grant date on exercise date EMPLOYEE'S name \$ 60.00 \$ 62.00 5 Exercise price paid per share 6 No. of shares transferred Danica Employee \$ 52.70 1,250 Street address (including ant no.) 7 Date legal title transferred			8/14/2022	(Rev. September 2016)	Section 423(c)
12-3456789	CORPORATION'S federal identification number	EMPLOYEE'S identification number			re Copy A
Danica Employee \$ 52.70 1,250 File with Form	12-3456789	987-65-4321	on grant date	on exercise date	For
Danica Employee \$ 52.70 1,250 File with Form	EMPLOYEE'S name		\$ 60.00	\$ 62	
Street address (including ant no.) 7 Date legal title transferred			5 Exercise price paid per share	6 No. of shares transferred	Service Center
Street address (including apt. no.) 7 Date legal title transferred For Privacy	Danica Employee		\$ 52.70	1,250	File with Form 1096.
	Street address (including apt. no.)		7 Date legal title transferred		For Privacy Act and
123 Main Street Paperwork Ře	123 Main Street		110		Paperwork Reduction
	City or town, state or province, country	y, and ZIP or foreign postal code	8/14	/2022	Act Notice, see the current version of the
Anaheim, CA 92801 8 Exercise price per share determined as if the option was General Instruct	Anaheim, CA 92801				General Instructions for
ACCOUNT NUMBER (See Instructions)	Account number (see instructions)		exercised on the date showr	in box 1	Certain Information Returns.
\$ 51.00			\$	51	

www.irs.gov/form3922

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The tax effects of Danica's nonqualifying disposition are as follows:

Sale proceeds per share	\$ 65.00
Exercise price paid per share (Form 3922, box 5)	<u>- 52.70</u>
Total gain per share	12.30
Number of shares sold	<u>× 1,250</u>
Total gain on sale of stock	\$15,375

The total gain of \$15,375 must be broken out between ordinary income and capital gain, calculated as follows:

Fair market value of stock on exercise date (Form 3922, box 4)	\$ 62.00
Exercise price per share (Form 3922, box 5)	- 52.70
Ordinary income recognized per share (reported on her W-2)	9.30
Number of shares sold	× 1,250
Total ordinary income on sale of stock	\$11,625
Long-term capital gain per share*	\$ 3.00
Number of shares sold	× 1,250
Total long-term capital gain on qualifying ESPP disposition	\$ 3,750
* Total gain per share minus ordinary income recognized per sh	are

BASIS REPORTED ON FORM 1099-B (ESPPs)

When an employee purchases stock through an employee stock purchase plan, the shares are transferred into the employee's brokerage account. The cost basis provided in the employee's brokerage account (as well as on Form 1099-B when the shares are sold) is the exercise price paid for the shares.

Both qualifying and nonqualifying dispositions of stock acquired through an employee stock purchase plan can give rise to ordinary income that is reportable on the employee's W-2. Because of this, basis adjustments will always be required when an employee acquires stock through an employee stock purchase plan at a discounted rate.

If an employee stock purchase plan allows an employee to purchase company stock without a discount (for example, at the stock's full fair market value on the grant date), then the employee won't recognize ordinary income upon disposition and therefore won't be required to make any basis adjustments from the amounts shown on Form 1099-B.

Example of Form 1099-B basis adjustments on sale of stock acquired through employee stock purchase plan

The facts are the same as the previous example (Danica's sale of ESPP stock in a nonqualifying disposition). Danica's 1099-B on the sale of her stock will contain the following relevant information:

Shares sold	Date sold	Date acquired	Proceeds	Cost basis	Gain (loss)
1,250	10/30/2023	8/14/2022	\$81,250*	\$65,875**	\$15,375
	res × \$65 per s	hare			

** 1,250 shares × \$52.70 per share exercise price

If Danica's tax professional simply reports capital gain on her income tax return as shown on her Form 1099-B, then she will report \$15,375 of capital gain from the sale of the 1,250 shares. However, as the previous example illustrates, she actually has a \$3,750 capital gain on the sale of the shares.

The \$9.30 of ordinary income recognized per share (calculated in the previous example) and reported on Danica's W-2, must be added to the basis shown on her 1099-B. The basis is added on Form 8949 using code "B" in column (f), as follows:

Form 8949 (20	023)					Attachn	nent Sequence No.	12A	Page 2
	n on return. Name and SSN or to	expayer identificat	ion no. not requir	ed if shown on other s	ide Social secu	•	taxpayer Identifica	ation number	,
Fiona Empl	oyee					- 1	23-45-6789		
statement w	check Box D, E, or F belov vill have the same informat may even tell you which b	tion as Form 10							ur
Part II	Long-Term. Transa instructions). For sh				eld more than	1 year are	generally long	term (see	•
	Note: You may agg to the IRS and for v 8a; you aren't requi	vhich no ad	justments o	r codes are re	quired. Enter th	ne totals di	rectly on Sche		
a separate	check Box D, E, or F to Form 8949, page 2, for boxes, complete as m	r each applica	able box. If y	ou have more lo	ng-term transac	•	-		
(E) L	ong-term transactions ong-term transactions ong-term transactions	reported on l	Form(s) 1099	-B showing bas)	
1	(a)	(b)	(c) Date sold or	(d) Proceeds	(e) Cost or other basis See the Note below	If you enter an a	any, to gain or loss amount in column (g), de in column (f). arate instructions.	(h) Gain or (k Subtract colu	
(E	Description of property example: 100 sh. XYZ Co.)	Date acquired (Mo., day, yr.)	disposed of (Mo., day, yr.)	(sales price) (see instructions)	and see Column (e) In the separate Instructions.	(f) Code(s) from Instructions	(g) Amount of adjustment	from column combine the with column	result
Name of co	mpany - Nonqualifying of ESPP	8/14/2022	10/30/2023	\$81,250	\$65,875	В	(\$11,625)	112	\$3,750

RESTRICTED STOCK UNITS (RSUS)

An employee does not recognize income when a restricted stock unit is granted (the grant date). (IRC §83(a))

Unlike stock options, shares of stock acquired under restricted stock units are not purchased by the employee — they are automatically received by an employee through a vesting schedule provided in the employee's stock grant.

An employee receives shares of stock and recognizes ordinary income when the restricted stock unit vests (the vesting date) equal to the fair market value (on the vesting date) of the stock. (IRC §83(a)) Recognition occurs as the RSUs vest because that is the time when the stock is no longer subject to a substantial risk of forfeiture.

The ordinary income should be reported on the employee's W-2 (Form 1099-NEC if the restricted stock unit is vested to someone who is not an employee). The ordinary income is subject to Social Security and Medicare taxes (or self-employment taxes if received by someone who isn't an employee).

Practice Pointer

Because RSUs give rise to ordinary income when they are vested and therefore are reported on the employee's W-2, they are also subject to income tax withholding. It is common for employees to use vested shares to satisfy this withholding.

For example, an employee may have 100 shares of company stock vest but may only receive 70 shares transferred to their investment account. The remaining 30 shares are held back to satisfy the employee's withholding obligations. This is also referred to as "cashless vesting," "cashless exercise," or "sell-to-cover."

In this scenario, even though the taxpayer technically sold some of their RSUs to cover their paycheck withholding obligation, the sold shares may not appear on Form 1099-B at all. This is the case where the shares never pass through the broker, and the "sell" occurs directly through the employer.

DISPOSITION OF STOCK ACQUIRED THROUGH RESTRICTED STOCK UNITS

In addition to the ordinary income recognized on the vesting of restricted stock units, taxpayers will recognize capital gain (or loss) when they dispose of the stock calculated by subtracting the stock's fair market value on the vesting date (the date when ordinary income was recognized) from the sale proceeds as follows:

Sale proceeds – FMV on vesting = Capital gain (loss) (IRC §1222)

The capital gain or loss is classified as long-term if the shares are held for more than one year from the vesting date to the date of disposition. (IRC §1222(4))

RSU BASIS REPORTED ON FORM 1099-B

When an employee's restricted stock units vest, the stock is transferred into the employee's brokerage account. The cost basis provided in the employee's brokerage account (as well as on Form 1099-B when the shares are sold) is the fair market value of the shares on the vesting date.

Because the amount reported as the cost basis is the same as the amount that was reported on the employee's W-2 (or 1099-NEC for nonemployee recipients of RSUs), the basis reflected on the employee's brokerage statement should be accurate.

Practice Pointer

Even though the basis reported to the brokerage company should be accurate, the basis is not reported to the IRS because it's classified as a noncovered transaction. As such, if the Form 1099-B for the sale of the stock does not reflect any basis at all, the tax professional may be required to review old W-2s and RSU awards to track down the basis.

RESTRICTED STOCK AWARDS (RSAS)

Restricted stock awards (RSAs) are very similar to restricted stock units (RSUs): They are a form of equity compensation where the shares of company stock often do not have to be purchased by the employee — they are automatically received by an employee through an award. However, some RSAs do require employees to purchase them.

When an RSA is granted, the employee becomes the owner of the stock as soon as they accept the grant. However, there is a vesting period during which the stock may be subject to forfeiture if the employee leaves the company, is terminated, or fails to meet vesting conditions specified in the RSA grant. This is different from an RSU, where the employee does not own any stock when the RSU is granted and receives the company stock free of any restrictions at the *end* of the vesting period.

RSA vesting conditions

Stock acquired by an employee upon the grant of an RSA will contain vesting conditions detailed in the stock award documentation. Vesting conditions can be based on time, meeting individual performance goals, meeting company-wide performance goals, or any other condition.

If a vesting condition is not met, then the stock acquired through the RSA is subject to forfeiture or repurchase by the company. Clients who receive RSAs must read and understand their vesting conditions, especially if they are considering whether making an IRC §83(b) election makes sense to them. We will discuss RSAs and the IRC §83(b) election later in this section.

An employee does not recognize ordinary income upon the RSA grant because the stock is subject to vesting conditions during the vesting period. During the vesting period, the stock is still subject to a substantial risk of forfeiture and is therefore not taxable. (IRC §83(a))

Once the vesting conditions are met and the stock is no longer subject to a substantial risk of forfeiture, then the employee recognizes ordinary income equal to the fair market value of the stock at the end of the vesting period, less the amount paid by the employee upon the RSA grant (if anything).

Example of RSA ordinary income recognition

Lee accepted a job with a technology start-up company on February 2, 2022. As part of his compensation, he received an RSA of 100,000 shares of stock with a fair market value of \$0.10 per share. Lee was required to pay \$0.06 per share for the RSA (100,000 shares \times \$0.06 = \$6,000).

The RSA is subject to a vesting schedule that requires Lee to work for the company for two years before his vesting conditions are met and the stock is no longer subject to a substantial risk of forfeiture.

Lee meets his vesting conditions because he is still employed by the company on February 2, 2024. On that date, the stock is worth \$1.21 per share. Lee must recognize ordinary income of \$115,000, calculated as follows:

Number of vested shares	100,000
FMV per share on vesting	×\$ 1.21
Subtotal	\$121,000
Price paid for shares on grant date	<u>- 6,000</u>
Total ordinary income	\$115,000

The ordinary income recognized by Lee must be reported on his W-2 and is subject to Social Security and Medicare taxes.

Because stock is actually received by an employee upon the RSA grant, the employee can make an IRC §83(b) election. The election allows the employee to pay ordinary income tax on the value of the shares on the grant date instead of at the end of the vesting period.

In this example, if Lee filed an IRC §83(b) election, then his ordinary income would be \$4,000 in 2021 (100,000 shares x \$0.10 FMV per share on the grant date - \$0.06 per share paid by Lee).

If the IRC §83(b) election was filed, then Lee would not recognize any ordinary income in 2024. Instead, he would only recognize capital gain when he sells his shares. The IRC §83(b) election is discussed later.

DISPOSITION OF STOCK ACQUIRED THROUGH RESTRICTED STOCK AWARDS

In addition to the ordinary income recognized once restricted stock awards are vested, taxpayers will recognize capital gain (or loss) calculated as follows:

Sale proceeds

- (use the grant date if an IRC = Capital gain (loss) §83(b) election was timely filed)

The capital gain or loss is classified as long-term if the shares are held for more than one year from the vesting date to the date of disposition. (IRC §1222(4))

RSA BASIS REPORTED ON FORM 1099-B

The RSA basis reported on Form 1099-B is the same for RSAs and RSUs. When an employee's restricted stock award vests, the stock is transferred into the employee's brokerage account. The cost basis provided in the employee's brokerage account (as well as on Form 1099-B when the shares are sold) is the fair market value of the shares on the vesting date. However, if an IRC §83(b) election is timely filed, use the fair market value of the shares on the grant date as the taxpayer's basis

Because the amount reported as the cost basis is the same as the amount that was reported on the employee's W-2 (or 1099-NEC for nonemployee recipients of RSAs), the basis reflected on the employee's brokerage statement should be accurate.

Practice Pointer

Even though the basis reported to the brokerage company should be accurate, the basis is not reported to the IRS because it's classified as a noncovered transaction. As such, if the Form 1099-B for the sale of the stock does not reflect any basis at all, the tax professional may be required to review old W-2s and RSA awards to track down the basis.

PHANTOM STOCK AND STOCK APPRECIATION RIGHTS (SARS)

Phantom stock and stock appreciation rights are both forms of deferred compensation where the employee isn't given actual equity in their employer. Instead, the employee is given a mock unit of stock that follows the stock price of actual stock. Because both phantom stock and stock appreciation rights are forms of deferred compensation, the employer must have a written plan that meets the requirements of IRC §409A.

Similar to the other stock incentive plans discussed in these materials, phantom stock and stock appreciation rights are granted (so they have a grant date) and are subject to vesting (based on the terms of the employer's plan).

Employees must recognize ordinary income when they receive payments on their phantom stock or stock appreciation rights. Remember, the employee doesn't actually own any stock, so the payments are treated as wages and taxed as ordinary income and are subject to Social Security and Medicare tax. But, because the employee doesn't actually own any equity, they don't have anything to sell. This means that payments to the employee will not appear on a Form 1099-B, and the tax professional may never even know that the phantom stock or stock appreciation rights exist. The payments made to the employee will appear the same as any other compensation on the employee's W-2.

There are infinite variations on these two types of stock incentive plans, but the key differences are that the value of a phantom stock unit is usually valued as if it were the same as a share of the company's actual stock, but stock appreciation rights are usually based only on the stock appreciation during a defined period of time.

W-2 REPORTING FOR STOCK INCENTIVE PLANS

Each of the stock options discussed here is reported on an employee's W-2 in the year when ordinary income is recognized. The following chart details where, how, and when on the W-2 the ordinary income is disclosed and the year when the ordinary income is recognized as well as whether each type of stock incentive plan is eligible for either the IRC §83(b) or §83(i) election.

	<u>W-2 F</u>	Reporting for S	tock Incentive	<u>Plans</u>		
	ISO	NQSO	ESPP	RSU	RSA	Phantom stock and SARs
Date stock is actually received by the employee	When ISO is exercised	When NQSO is exercised	When stock is purchased by employee	End of vesting period	Beginning of vesting period	No equity is actually received by the employee
Subject to Social Security (W-2, Box 3)	No	Yes	Yes	Yes	Yes	Yes
Subject to Medicare (W-2, Box 5)	No	Yes	Yes	Yes	Yes	Yes
Disclosure box and code ¹	Box 14, "ISODD"	Box 12, "V"	Box 14, "ESPP"	Box 14, "RSU"	Box 14, "RSA"	None
Timing of ordinary income recognized (and reported on W-2) ²	When disqualifying disposition is made	When NQSO is exercised	When stock is sold	When RSU shares vest	When RSA shares vest	When cash is received
Eligible for §83(b) election	Yes	Yes	No	No	Yes	No
Eligible for §83(i) election ³	Yes	Yes	No	Yes	No	No

¹ The W-2 instructions outline a specific Box 12 code of "V" for the exercise of nonqualified stock options. The Box 14 codes in this chart are common codes used by employers, but may differ from what is shown here

 $^{^2}$ The year reported on an employee's W-2 can be an earlier year when an IRC §83(b) election is made or a later year when an IRC §83(i) election is made

³ Subject to the other requirements of IRC §83(i) discussed below

ELECTIONS

There are a couple of common elections under IRC §83 that tax professionals should be aware of when dealing with stock options. They are the elections under IRC §83(b) and (i).

ELECTION TO INCLUDE IN GROSS INCOME IN YEAR OF TRANSFER

The election available under IRC §83(b) allows an employee to elect to include the fair market value of stock granted to them in their ordinary income. Remember, no income is typically recognized when stock options are granted because the stock is still subject to a substantial risk of forfeiture. (IRC §83(a))

By making an IRC §83(b) election when the stock options are granted, the employee can benefit by reducing the amount of ordinary income they will recognize from the stock options and thereby shifting more of the income earned from the stock options to capital gain. This can be especially beneficial for taxpayers in higher tax brackets. However, the election under IRC §83(b) comes with its risks:

- If the employee is separated from the company before their stock vests or is able to exercise their options, the employee cannot unwind the IRC §83(b) election, and they do not receive a deduction for the income included in a prior year but which was never actually received (IRC §83(b)(1));
- If the company's stock drops in value between the date of the IRC §83(b) election and the date that the stock would have otherwise been vested or the options exercised, then the IRC §83(b) election would cause more income inclusion than if the election had not been made; and
- The employee's tax liability for the income recognized in the year of the election must be paid out-of-pocket by the employee because the employee hasn't actually received anything of value yet.

Timing and form of IRC §83(b) election

The election under IRC §83(b) must be filed with the IRS within 30 days of receiving the stock grant. (IRC §83(b)(2)) The election can only be revoked with the IRS's consent.

For stock grants issued before January 1, 2016, taxpayers were required to attach a copy of their IRC §83(b) election with their income tax return. Treasury regulations eliminated this requirement for stock grants issued after December 31, 2015. (Treas. Regs. §1.83-2(c))

The IRS has provided a sample form for making the IRC §83(b) election contained within Revenue Procedure 2012-29, which can be found at the following link:

□ Website

www.irs.gov/pub/irs-drop/rp-12-29.pdf

Practice Pointer

Because an election under IRC §83(b) must be filed within only 30 days of receiving a stock grant and because the income inclusion must be reported on the employee's W-2 (or 1099-NEC if the person performing services is an independent contractor), the election is often provided to the employee by the employer and filed without discussing the tax ramifications with the employee's tax professional ahead of time.

When an employee receives a stock grant, be sure to ask if an election under IRC §83(b) was made and request a copy of the election from the client.

QUALIFIED EQUITY GRANT ELECTION

The TCJA added IRC §83(i) for qualified equity grants. IRC §83(i) only applies to private corporations, defined as those corporations that:

- Do not have stock readily tradable on an established securities market; and
- Have a written plan under which not less than 80% of all employees who provide services to such corporation in the U.S. are granted stock options, or are granted restricted stock units, with the same rights and privileges to receive qualified stock. (IRC §83(i)(2)(C)(i))

An employee who makes the IRC §83(i) election may postpone recognition of ordinary income (includable in W-2 wages) until the earliest of the following dates:

- The date the qualified stock becomes transferable;
- The date the employee first becomes an "excluded employee";
- The first date on which any stock of the corporation becomes readily tradable on an established securities market;
- The date that is five years after the first date the rights of the employee in the stock are transferrable or are not subject to a substantial risk of forfeiture (whichever occurs earlier); or
- The date the employee revokes the election. (IRC $\S83(i)(1)(B)(i)-(v)$)

Withholding

The wages are subject to withholding at the maximum tax rate applicable to individuals (37% for taxable years after 2017), and withholding is determined without regard to the employee's Form W-4. (Notice 2018-97) This means withholding may not be increased or decreased based on requests of the employee.

By January 31 of the following year, the employer must determine the actual value of the deferral stock on the date it is includible in the employee's income and report that amount and the withholding on Form W-2 and Form 941, Employer's Quarterly Federal Tax Return.

Excluded employees

- "Excluded employees" are defined as those who are:
- 1% owners of the business at any time during the current year or at any time during the 10 preceding calendar years;
- Who have been at any prior time:
 - o The chief executive officer of the business or an individual acting in such a capacity; or
 - o The chief financial officer of the business or an individual acting in such a capacity;
- Who are related to anyone who has ever been, or acting as, the chief executive officer or chief financial officer through the family attribution rules of IRC §318(a)(1); or
- Who are one of the four highest compensated officers of the business for the taxable year or any of the 10 preceding taxable years. (IRC §83(i)(3)(B))

IRC §83(i) is generally applicable for options exercised, or RSUs granted, for tax years beginning after December 31, 2017.

The benefit of the qualified equity grant election is that employees can defer taxable income inclusion for up to five years beyond the date their stock vests without affecting the amount or character of the income they must recognize. This may be a huge advantage for taxpayers who will need to save up the money to pay the taxes on the unrealized income.

The ordinary income that must be recognized and reported on the employee's W-2 is equal to the difference between the fair market value of the stock received at the time it vested and the amount paid for the stock. Employers are required to withhold income taxes at the highest federal income tax rate in effect at the end of the deferral period, which is currently 37%. (IRC §83(i)(6)(B)(ii)(II))

In other words, when the employee eventually sells the stock, the amount of capital gain or loss recognized is the same as if the employee hadn't made the qualified equity grant election.

The 80% requirement

The determination of whether a corporation qualifies as an eligible corporation by meeting the 80% requirement is made annually. In other words, the corporation must have granted stock options (or RSUs) to 80% of its employees during the calendar year at issue.

In calculating whether the 80% requirement is satisfied, the corporation must take into account the total number of individuals employed throughout the year in question as well as the total number of employees receiving grants during the year (in each case, without regard to excluded employees (defined below) or certain part-time employees). (See IRC §4980E(d)(4)) This is regardless of whether the employees were employed by the corporation at the beginning or at the end of the calendar year.

Notification to employees

Corporations that transfer stock to their employees for which an IRC §83(i) is eligible must provide notification to their employees on the date the stock would first be includible in the employee's gross income by:

- Certifying to the employee that the stock is qualified stock;
- Notifying the employee that they may be eligible to defer income on the stock;
- Notifying the employee that the amount of income to be recognized at the end of the deferral period will be based on the value of the stock at the time at which the rights of the employee first become transferable or not subject to a risk of forfeiture, regardless of whether the value of the stock has declined during the deferral period;
- Notifying the employee that the amount of the income recognition at the end of the deferral period will be subject to withholding (IRC §§3401(i), 3402(t)); and
- Outlining employee responsibilities with respect to such withholding. (IRC §83(i)(3)(A)(ii)). (IRC §83(i)(6))

Employers that fail to provide adequate notice face a penalty of \$100 for each failure, up to a maximum penalty of \$50,000 per calendar year. (IRC §6652(p))

Timing and form of IRC §83(i) election

The qualified equity grant election must be made within 30 days after the first date that the rights of the employee in the stock are transferable or are not subject to a substantial risk of forfeiture, whichever occurs earlier. (IRC §83(i)(4)(a)) The qualified equity grant election cannot be made for any stock for which the taxpayer made an IRC §83(b) election.

Supplemental Materials CPE Network® Tax Report

The qualified equity grant election must be made in a manner similar to the manner in which an IRC §83(b) election is made. Taxpayers can use the same sample IRC §83(b) election from Revenue Procedure 2012-29 mentioned on page 27. The IRS has not provided a separate sample election statement for the qualified equity grant election.

Employer opt-out

Although the IRC §83(i) election, if allowed, may be made by a qualified employee, the corporation is ultimately responsible for creating the conditions that would allow an employee to make the election.

Corporations can preclude their employees from making the IRC §83(i) election by declining to establish an escrow account required under IRC §83(i). By doing so, a corporation won't inadvertently create the requisite conditions for its employees to make an IRC §83(i) election or be required to comply with the notice requirements and their related penalties.

Corporations that want to opt out of permitting their employees to make an IRC §83(i) election may designate that no election under IRC §83(i) will be available with respect to the stock received upon the exercise of the stock option or settlement of the RSU.

STOCK INCENTIVE PLAN CHECKLIST

When a client indicates that they are a participant in an employer's stock incentive plan or the employee has sold shares that they acquired years earlier through a stock incentive plan, there is a lot of information the tax professional must have in order to accurately track and report the gain from the stock owned.

Often, the most difficult task tax professionals have is simply tracking the history of stock received through stock incentive plans and determining whether shares were sold in prior years and which shares are still held by the client.

This checklist will help you gather the information you need:

Stock Incentive Plan Checklist
Copy of the plan documents granting the options, RSUs, ESPPs, or other type of stock incentive plan
Copy of all W-2 and 1099-NEC forms (1099-MISC for taxable years before 2020) for all years the client was a participant in the plan
Copies of all brokerage statements and 1099-B forms for all years the client held stock acquired through a stock incentive plan
Copies of all company-provided information and summary sheets provided to the client upon exercise of their options—these will be different from company to company
Copies of all tax returns for years when stock acquired through a stock incentive plan was sold
Copies of all IRC §83(b) or §83(i) elections filed with the IRS (for taxable years before 2016, a copy of the taxpayer's IRC §83(b) election should be attached to their income tax return)
Copies of all Forms 3921 for all years in which ISOs were exercised
Copies of all Forms 3922 for all years in which ESPP shares were exercised

GROUP STUDY MATERIALS

A. Discussion Questions

- 1. Discuss the two types of adjustments and preferences related to alternative minimum taxes.
- 2. Discuss the tax implications of a nonqualified stock option.
- 3. Discuss employee stock purchase plans and how they are similar to incentive stock options.
- 4. Discuss the basis reported on Form 1099-B when an employee purchases stock through an ESPP.
- 5. Discuss the differences between a restricted stock award and restricted stock units.
- 6. Discuss the IRC §83(i) equity grant election added by TCJA.

B. Suggested Answers to Discussion Questions

- 1. Alternative minimum taxes are caused by two types of adjustments and preference items:
 - Deferral items; and
 - Exclusion items.

Deferral items generally don't cause a permanent difference between regular taxable income and alternative minimum taxable income over time. Examples include regular versus AMT depreciation and the adjustment for the exercise of incentive stock options, among others.

Exclusion items include:

- Certain itemized deductions (including any investment interest expense reported on Schedule E);
- Certain tax-exempt interest;
- Depletion;
- The qualified small business stock exclusion under IRC §1202;
- The standard deduction; and
- Any other adjustments related to exclusion items (such as taxable refunds reported on Schedule 1).
- 2. An employee does not recognize income when a nonqualified stock option is granted (the grant date) unless the stock has:
 - A readily ascertainable fair market value when granted; and
 - The stock is not subject to a substantial risk of forfeiture. (IRC §83(a))

An employee recognizes ordinary income in the year in which a nonqualified stock option is exercised. (IRC §83(a)) The ordinary income is calculated by subtracting the employee's exercise price from the fair market value of the stock purchased on the exercise date. The ordinary income should be reported on the employee's W-2 (Form 1099-NEC if the nonqualified stock option is exercised by someone who is not an employee).

The ordinary income reported on an employee's W-2 upon the exercise of a nonqualified stock option is subject to Social Security and Medicare taxes. When the ordinary income is reported on Form 1099-NEC for someone who is not an employee, the income recognized from the exercise of the nonqualfied stock options is subject to self-employment tax.

- 3. Employee stock purchase plans are similar to incentive stock options (ISOs). Both are defined as statutory stock options, and both require the issuance of an IRS form upon exercise:
 - Upon exercise of an ISO: Form 3921, Exercise of an Incentive Stock Option Under Section 422(b); or
 - Upon exercise of an ESPP: Form 3922, Transfer of Stock Acquired Through an Employee Stock Purchase Plan Under Section 423(c).

ESPPs are elective programs that allow employees to elect to purchase shares of company stock at a discount. The discount is usually between 5%–15% of the stock's fair market value on the grant date.

Employees will have an enrollment period where they select a percentage of their wages to be used to purchase shares at the end of an offering period. On the last day of the offering period, the total sum accumulated from the employee's contributions withheld from their paycheck are used to purchase the company stock. The date the shares are actually purchased is the exercise date.

4. When an employee purchases stock through an employee stock purchase plan, the shares are transferred into the employee's brokerage account. The cost basis provided in the employee's brokerage account (as well as on Form 1099-B when the shares are sold) is the exercise price paid for the shares.

Both qualifying and nonqualifying dispositions of stock acquired through an employee stock purchase plan can give rise to ordinary income that is reportable on the employee's W-2. Because of this, basis adjustments will always be required when an employee acquires stock through an employee stock purchase plan at a discounted rate.

If an employee stock purchase plan allows an employee to purchase company stock without a discount (for example, at the stock's full fair market value on the grant date), then the employee won't recognize ordinary income upon disposition and therefore won't be required to make any basis adjustments from the amounts shown on Form 1099-B.

5. Restricted stock awards (RSAs) are very similar to restricted stock units (RSUs): They are a form of equity compensation where the shares of company stock often do not have to be purchased by the employee — they are automatically received by an employee through an award. However, some RSAs do require employees to purchase them.

When an RSA is granted, the employee becomes the owner of the stock as soon as they accept the grant. However, there is a vesting period during which the stock may be subject to forfeiture if the employee leaves the company, is terminated, or fails to meet vesting conditions specified in the RSA grant. This is different from an RSU, where the employee does not own any stock when the RSU is granted and receives the company stock free of any restrictions at the *end* of the vesting period.

An employee does not recognize ordinary income upon the RSA grant because the stock is subject to vesting conditions during the vesting period. During the vesting period, the stock is still subject to a substantial risk of forfeiture and is therefore not taxable. (IRC §83(a))

Once the vesting conditions are met and the stock is no longer subject to a substantial risk of forfeiture, then the employee recognizes ordinary income equal to the fair market value of the stock at the end of the vesting period, less the amount paid by the employee upon the RSA grant (if anything).

- 6. The TCJA added IRC §83(i) for qualified equity grants. IRC §83(i) only applies to private corporations, defined as those corporations that:
 - Do not have stock readily tradable on an established securities market; and
 - Have a written plan under which not less than 80% of all employees who provide services to such corporation in the U.S. are granted stock options, or are granted restricted stock units, with the same rights and privileges to receive qualified stock. (IRC §83(i)(2)(C)(i))

An employee who makes the IRC §83(i) election may postpone recognition of ordinary income (includable in W-2 wages) until the earliest of the following dates:

- The date the qualified stock becomes transferable;
- The date the employee first becomes an "excluded employee";
- The first date on which any stock of the corporation becomes readily tradable on an established securities market;
- The date that is five years after the first date the rights of the employee in the stock are transferrable or are not subject to a substantial risk of forfeiture (whichever occurs earlier); or
- The date the employee revokes the election. (IRC $\S83(i)(1)(B)(i)-(v)$)

"Excluded employees" are defined as those who are:

- 1% owners of the business at any time during the current year or at any time during the 10 preceding calendar years;
- Who have been at any prior time:
 - o The chief executive officer of the business or an individual acting in such a capacity; or
 - o The chief financial officer of the business or an individual acting in such a capacity;
- Who are related to anyone who has ever been, or acting as, the chief executive officer or chief financial officer through the family attribution rules of IRC §318(a)(1); or
- Who are one of the four highest compensated officers of the business for the taxable year or any of the 10 preceding taxable years. (IRC §83(i)(3)(B))

IRC §83(i) is generally applicable for options exercised, or RSUs granted, for tax years beginning after December 31, 2017.

The benefit of the qualified equity grant election is that employees can defer taxable income inclusion for up to five years beyond the date their stock vests without affecting the amount or character of the income they must recognize. This may be a huge advantage for taxpayers who will need to save up the money to pay the taxes on the unrealized income.

The ordinary income that must be recognized and reported on the employee's W-2 is equal to the difference between the fair market value of the stock received at the time it vested and the amount paid for the stock. Employers are required to withhold income taxes at the highest federal income tax rate in effect at the end of the deferral period, which is currently 37%. (IRC §83(i)(6)(B)(ii)(II))

In other words, when the employee eventually sells the stock, the amount of capital gain or loss recognized is the same as if the employee hadn't made the qualified equity grant election.

GLOSSARY OF KEY TERMS

Charitable Deduction—Donations to a qualified charity

Charitable Remainder Trust—Irrevocable trusts that permit the donation of assets to charity and allow for drawing annual income for life or for a specific time period

Charitable Remainder Annuity Trust (CRATs)—Distribute a fixed annuity amount each year and additional contributions are not permitted

Conservation Easement—Voluntary, legal agreement that permanently limits uses of the land in order to protect its conservation values

Digital Assets—A digital representation of value that is recorded on a cryptographically secured, distributed ledger or any similar technology. Common digital assets include: convertible virtual currency and cryptocurrency; stablecoins; Non-fungible tokens (NFTs)

ERC—Employee Retention Credit

ESPPs—Employee Stock Purchase Plans

Incentive Stock Options (ISOs)—An employee benefit that gives the right to buy stock at a discount with a tax break on any profits

NQSOs—Nonqualified Stock Options

OIC—Offer In Compromise

Phishing—An email sent by fraudsters claiming to come from the IRS. The email lures the victims into the scam with a variety of ruses such as enticing victims with a phony tax refund or threatening them with false legal or criminal charges for tax fraud.

RSAs—Restricted Stock Awards

RSUs—Grant an employee the stock itself once the vesting period is completed

Smishing—A text or smartphone SMS message where scammers often use alarming language such as, "Your account has now been put on hold," or "Unusual Activity Report," with a bogus "Solutions" link to restore the recipient's account. Unexpected tax refunds are another potential lure for scam artists.

Spear phishing—A type of phishing attack that targets specific individuals or organizations typically through malicious emails. The goal of spear phishing is to steal sensitive information such as login credentials or infect the targets' device with malware.

TEOS—Tax Exempt Organization Search

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Choose the best response and record your answer in the space provided on the answer sheet.

- 1. According to Ian Redpath, what should a taxpayer or tax professional do if they receive a suspicious email claiming to be from the IRS?
 - A. Reply to the email and provide the requested information
 - B. Open any attachments or click on any links in the email
 - C. Forward the full email header to phishing@irs.gov and then delete the original email
 - D. Ignore the email and take no further action
- 2. According to Ian Redpath, which of the following is *not* a common flag for potentially fraudulent Employee Retention Credit (ERC) claims?
 - A. Too many quarters being claimed
 - B. Government orders that don't qualify as a shutdown of the business
 - C. The business paying all required payroll taxes during the eligibility period
 - D. The business not existing during the eligibility period
- 3. According to Ian Redpath, what is the difference between phishing and spear phishing scams?
 - A. Spear phishing scams target a wide audience, while phishing targets specific individuals or organizations
 - B. Spear phishing scams are less dangerous than general phishing scams
 - C. Phishing scams always involve emails, while spear phishing scams always involve text messages
 - D. Spear phishing scams are targeted attempts to steal sensitive information from specific individuals or organizations
- 4. According to Ian Redpath, which of the following is an example of a scheme aimed at high-income taxpayers, according to the IRS "Dirty Dozen" list?
 - A. Ghost preparers who don't sign returns or use PTINs
 - B. Improper use of charitable remainder annuity trusts (CRATs) to avoid recognizing gain on appreciated assets
 - C. Fake charities that pop up after natural disasters
 - D. Fraudulently claiming the fuel tax credit for personal vehicle use
- 5. According to Ian Redpath, what is the purpose of the new box 11D on the draft 2025 Form 1099-DA for digital asset reporting??
 - A. To indicate if the digital asset transaction involved a wash sale under Section 1091
 - B. To provide the digital asset address or transaction ID for all reported transactions
 - C. To indicate if the digital asset sale was not recorded on a distributed ledger
 - D. To report the fair market value of the digital assets at the time of the transaction

Continued on next page

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- 6. According to Mike Giangrande, which type of incentive stock plan requires an AMT adjustment?
 - A. Non-qualified stock options
 - B. Incentive stock options (ISOs)
 - C. Employee stock purchase plans (ESPPs)
 - D. Restricted stock units (RSUs)
- 7. According to Mike Giangrande, under what circumstance is there no AMT adjustment required for an ISO?
 - A. When the stock is sold in the same year it is exercised, resulting in a non-qualifying disposition
 - B. When the stock is held for more than one year after exercise
 - C. When the stock is sold at a loss
 - D. When the stock is donated to charity
- 8. According to Mike Giangrande, according to the \$100,000 annual limit on ISOs, any ISOs exercisable during the year in excess of this limit are classified as which of the following?
 - A. Disqualified stock options
 - B. Phantom stock options
 - C. Non-qualified stock options
 - D. Restricted stock awards
- 9. According to Mike Giangrande, under Section 83(a), income is recognized on non-qualified stock options at the grant date under which of the following circumstances?
 - A. The stock has a readily ascertainable fair market value and is not subject to a substantial risk of forfeiture
 - B. The options are granted to the employee
 - C. The employee leaves the company
 - D. The stock price reaches a predetermined target
- 10. According to Mike Giangrande, when disposing of non-qualified stock options, the capital gain or loss is calculated by which of the following?
 - A. Subtracting the exercise price from the sale proceeds
 - B. Subtracting the fair market value on the exercise date from the sale proceeds
 - C. Subtracting the grant price from the sale proceeds
 - D. Adding the exercise price to the sale proceeds
- 11. According to Mike Giangrande, in the context of employee stock purchase plans (ESPPs), which of the following statements is true?
 - A. There is no income recognition on the grant date, but there is income recognition on the exercise date
 - B. There is income recognition on both the grant date and the exercise date
 - C. There is no income recognition on either the grant date or the exercise date
 - D. Income recognition occurs when the stock is sold, regardless of the holding period
- 12. According to Mike Giangrande, for a qualifying disposition of stock acquired through an ESPP, ordinary income is which of the following?
 - A. Not recognized, as only long-term capital gain is reported
 - B. The entire gain from the sale of the stock
 - C. The lesser of (a) the sale price minus the discounted purchase price (not less than zero), or (b) the fair market value at the grant date multiplied by the discount percentage offered
 - D. Always equal to the discount percentage multiplied by the sale price

Continued on next page

13. According to Mike Giangrande, when are restricted stock units (RSUs) typically taxed as ordinary income?

- A. On the grant date
- B. When the employee purchases the shares
- C. When the employee sells the shares
- D. As the RSUs vest
- 14. According to Mike Giangrande, which of the following is a key difference between restricted stock units (RSUs) and restricted stock awards (RSAs)?
 - A. RSUs are subject to Social Security and Medicare taxes, while RSAs are not
 - B. RSUs do not allow for a Section 83(b) election, while RSAs do
 - C. RSUs are always purchased by the employee, while RSAs are always granted at no cost
 - D. RSUs are taxed as ordinary income upon vesting, while RSAs are taxed as capital gains upon vesting
- 15. According to Mike Giangrande, what is the purpose of a Section 83(b) election?
 - A. To defer taxation of stock options until they are exercised
 - B. To accelerate taxation of restricted stock to the grant date, typically when the stock has a lower value
 - C. To convert ordinary income from stock options into long-term capital gains
 - D. To avoid paying Social Security and Medicare taxes on stock-based compensation

Volume 37, Issue 5 June 2024

SUBSCRIBER SURVEY Evaluation Form

Please take a few minutes to complete this survey related to the **CPE Network® Tax Report** and return with your quizzer or group attendance sheet to CeriFi, LLC. All responses will be kept confidential. Comments in addition to the answers to these questions are also welcome. Please send comments to **CPLgrading@cerifi.com**.

How would you rate the topics covered in the June 2024 **CPE Network® Tax Report**? Rate each topic on a scale of 1–5 (5=highest):

	Topic	Topic Content/	Topic	Video	Audio	Written
Experts' Forum	Relevance	Coverage	Timeliness	Quality	Quality	Material
Stock Incentive Plans: Part II						
Which segments of the June 2024 issue of CPE No.	etwork® Tax Report did	you like th	ne most, and	why?		
Which segments of the June 2024 issue of CPE No	etwork® Tax Report did	you like th	e least, and	why?		
What would you like to see included or changed in	future issues of CPE Ne	twork® Ta	x Report?			
Are there any other ways in which we can improve	CPE Network® Tax Re	port?				

How would you rate the effectiveness of the speak 1–5 (5=highest):	cers in th	ne Jui	ne 2024	4 CPE N	letwork	κ® Tax F	eport? F	Rate eac	h speaker	on a scale of
	Overall	l		edge of pic	Presen Ski					
Ian Redpath		_								
Mike Giangrande		_								
Which of the following would you use for viewing	g CPE N	Netwo	ork® T	ax Repo	ort? DV	'D □ Str	eaming [Both [
Are you using CPE Network® Tax Report for:	CPE Cr	edit [nformati	on 🗆	Both [
Were the stated learning objectives met? Yes □	No	0 🗆								
If applicable, were prerequisite requirements appro	opriate?	Y	es 🗆	No □						
Were program materials accurate? Yes □	No 🗆	_								
Were program materials relevant and contribute to	the ach	nieven	ment of	the lear	ning ob	jectives'	Yes 🗆	N	o □ _	
Were the time allocations for the program appropr	riate?	Yes		No 🗆						
Were the supplemental reading materials satisfactor	ory?	Yes		No 🗆						
Were the discussion questions and answers satisfa	ctory?	Yes		No \square						
Were the audio and visual materials effective?		Yes		No 🗆						
Specific Comments:										
Name/Company										
Address										
City/State/Zip										
Fmail										

Once Again, Thank You... Your Input Can Have a Direct Influence on Future Issues!

CPE Network® CPE Group Attendance Sheet

Firm/Company Name:					
Account #:					
Location:					
Program Title:					Date:
Name	<u>Email</u>	Total Hrs	IRS PTIN ID (if applicable Tax only)	Sign In	Sign Out
I certify that the above individuals viewed and were participants in the group discussion with this issue/segment of the CPE Network [®] newsletter, and earned the number of hours shown.	wed and were participants in	the group	discussion with this issue/segmen	t of the CPE Netw	ork $^{\scriptscriptstyle{ ext{@}}}$ newsletter, and earned
Instructor Name:			Date:		
E-mail address:					
License State and Number:			ĺ		

CPE Network/Webinar Delivery Tracking Report

Course Title	
Course Date:	
Start Time:	
End Time:	
Moderator Name, Credentials, and Signature Attestation of Attendance:	
Delivery Method:	Group Internet Based
Total CPE Credit:	3.0
Instructions:	During the webinar, the moderator must verify student presence a minimum of 3 times per CPE hour. This is achieved via polling questions. Sponsors must have a report which documents the responses from each student. The timing of the polling questions should be random and not made known to students prior to delivery of the course. Record the polling question responses below. Refer to the CPL Network User Guide for more instructions. Partial credit will not be issued for students who do not respond to at least 3 polling questions per CPE hour.
Brief Description of Method of Polling	Example: Zoom: During this webinar, moderator asked students to raise their hands 3 times per CPE hour. The instructor then noted the hands that were raised in the columns below.

			First CPE Hour		st CPE Hour CPE Hour 2		CPE Hour 3			FOR TR USE ONLY		
First Name	Last Name	Student Email	Poll 1	Poll 2	Poll 3	Poll 1	Poll 2	Poll 3	Poll 1	Poll 2	Poll 3	Certificate Issued?
									-			

CHECKPOINT LEARNING NETWORK

CPE NETWORK® USER GUIDE

REVISED December 31, 2023

Welcome to CPE Network!

CPE Network programs enable you to deliver training programs to those in your firm in a manageable way. You can choose how you want to deliver the training in a way that suits your firm's needs: in the classroom, virtual, or self-study. You must review and understand the requirements of each of these delivery methods before conducting your training to ensure you meet (and document) all the requirements.

This User Guide has the following sections:

- "Group Live" Format: The instructor and all the participants are gathered into a common area, such as a conference room or training room at a location of your choice.
- "Group Internet Based" Format: Deliver your training over the internet via Zoom, Teams, Webex, or other application that allows the instructor to present materials that all the participants can view at the same time.
- "Self-Study" Format: Each participant can take the self-study version of the CPE Network
 program on their own computers at a time and place of their convenience. No instructor
 is required for self-study.
- Transitioning From DVDs: For groups playing the video from the online platform, we suggest downloading the video from the Checkpoint Learning player to the desktop before projecting.
- What Does It Mean to Be a CPE Sponsor?: Should you decide to vary from any of the
 requirements in the 3 methods noted above (for example, provide less than 3 full CPE
 credits, alter subject areas, offer hybrid or variations to the methods described above),
 Checkpoint Learning Network will not be the sponsor and will not issue certificates. In
 this scenario, your firm will become the sponsor and must issue its own certificates of
 completion. This section outlines the sponsor's responsibilities that you must adhere to if
 you choose not to follow the requirements for the delivery methods.
- **Getting Help:** Refer to this section to get your questions answered.

IMPORTANT: This User Guide outlines in detail what is required for each of the 3 formats above. Additionally, because you will be delivering the training within your firm, you should review the Sponsor Responsibilities section as well. To get certificates of completion for your participants following your training, you must submit all the required documentation. (This is noted at the end of each section.) Checkpoint Learning Network will review your training documentation for completeness and adherence to all requirements. If all your materials are received and complete, certificates of completion will be issued for the participants attending your training. Failure to submit the required completed documentation will result in delays and/or denial of certificates.

IMPORTANT: If you vary from the instructions noted above, your firm will become the sponsor of the training event and you will have to create your own certificates of completions for your participants. In this case, you do not need to submit any documentation back to CeriFi, LLC.

If you have any questions on this documentation or requirements, refer to the "Getting Help" section at the end of this User Guide **BEFORE** you conduct your training.

We are happy that you chose CPE Network for your training solutions. Thank you for your business and HAPPY LEARNING!

Copyrighted Materials

CPE Network program materials are copyrighted and may not be reproduced in another document or manuscript in any form without the permission of the publisher. As a subscriber of the **CPE Network Series,** you may reproduce the necessary number of participant manuals needed to conduct your group study session.

"Group Live" Format

CPE Credit

All CPE Network products are developed and intended to be delivered as 3 CPE credits. You should allocate sufficient time in your delivery so that there is no less than 2.5 clock hours:

50 minutes per CPE credit TIMES 3 credits = 150 minutes = 2.5 clock hours

If you wish to have a break during your training session, you should increase the length of the training beyond 2.5 hours as necessary. For example, you may wish to schedule your training from 9 AM to 12 PM and provide a ½ hour break from 10:15 to 10:45.

*Effective November 1, 2018: Checkpoint Learning CPE Network products 'group live' sessions must be delivered as 3 CPE credits and accredited to the field(s) of study as designated by Checkpoint Learning Network. Checkpoint Learning Network will not issue certificates for "group live" deliveries of less than 3 CPE credits (unless the course was delivered as 3 credits and there are partial credit exceptions (such as late arrivals and early departures). Therefore, if you decide to deliver the "group live" session with less than 3 CPE credits, your firm will be the sponsor as Checkpoint Learning Network will not issue certificates to your participants.

Advertising / Promotional Page

Create a promotion page (use the template after the executive summary of the transcript). You should circulate (e.g., email) to potential participants prior to training day. You will need to submit a copy of this page when you request certificates.

Monitoring Attendance

You must monitor individual participant attendance at "group live" programs to assign the correct number of CPE credits. A participant's self-certification of attendance alone is not sufficient.

Use the **attendance sheet.** This lists the instructor(s) name and credentials, as well as the first and last name of each participant attending the seminar. The participant is expected to initial the sheet for their morning attendance and provide their signature for their afternoon attendance. If a participant arrives late, leaves early, or is a "no show," the actual hours they attended should be documented on the sign-in sheet and will be reflected on the participant's CPE certificate.

Real Time Instructor During Program Presentation

"Group live" programs must have a **qualified**, **real time instructor while the program is being presented**. Program participants must be able to interact with the instructor while the course is in progress (including the opportunity to ask questions and receive answers during the presentation).

Elements of Engagement

A "group live" program must include at least one element of engagement related to course content during each credit of CPE (for example, group discussion, polling questions, instructor-posed question with time for participant reflection, or use of a case study with different engagement elements throughout the program).

Make-Up Sessions

Individuals who are unable to attend the group study session may use the program materials for self-study online.

- If the emailed materials are used, the user should read the materials, watch the video, and answer the quizzer questions on the CPE Quizzer Answer Sheet. Send the answer sheet and course evaluation to the email address listed on the answer sheet and the CPE certificate will be mailed or emailed to the user. Detailed instructions are provided on Network Program Self-Study Options.
- If the online materials are used, the user should log on to her/his individual Checkpoint Learning account to read the materials, watch the interviews, and answer the quizzer questions. The user will be able to print her/his/their CPE certificate upon completion of the quizzer. (If you need help setting up individual user accounts, please contact your firm administrator or customer service.)

Awarding CPE Certificates

The CPE certificate is the participant's record of attendance and is awarded by Checkpoint Learning Network after the "group live" documentation is received (and providing the course is delivered as 3 CPE credits). The certificate of completion will reflect the credit hours earned by the individual, with special calculation of credits for those who arrived late or left early.

Subscriber Survey Evaluation Forms

Use the evaluation form. You must include a means for evaluating quality. At the conclusion of the "group live" session, evaluations should be distributed and any that are completed are collected from participants. Those evaluations that are completed by participants should be returned to Checkpoint Learning Network along with the other course materials. While it is required that you circulate the evaluation form to all participants, it is NOT required that the participants fill it out. A preprinted evaluation form is included in the transcript each month for your convenience.

Retention of Records

Regardless of whether Checkpoint Learning Network is the sponsor for the "group live" session, it is required that the firm hosting the "group live" session retain the following information for a period of five years from the date the program is completed unless state law dictates otherwise:

- Record of participation (Group Study Attendance sheets; indicating any late arrivals and/or early departures)
- Copy of the program materials
- Timed agenda with topics covered and elements of engagement used
- Date and location of course presentation
- Number of CPE credits and field of study breakdown earned by participants
- Instructor name and credentials
- Results of program evaluations.

Finding the Transcript

Note: DVDs no longer ship with this product effective 3/1/2023.

When the DVD is inserted into a DVD drive, the video will immediately begin to play and the menu screen will pop up, taking the entire screen. Hitting the Esc key should minimize it to a smaller window. To locate the pdf file of the transcript either to save or email to others, go to the start button on the computer. In My Computer, open the drive with the DVD. The Adobe Acrobat files are the transcript files. If you do not currently have Adobe Acrobat Reader (Mac versions of the reader are also available), a free version of the reader may be downloaded at:

https://get.adobe.com/reader/

The entire transcript is also available as a pdf in the Checkpoint Learning player in the resource toolbox at the top of the screen, or via the link in the email sent to administrators.

Requesting Participant CPE Certificates

When delivered as 3 CPE credits, documentation of your "group live" session should be sent to Checkpoint Learning Network by the following means:

Email: CPLgrading@cerifi.com

When sending your package to CeriFi, you must include ALL of the following items:

Form Name	Included?	Notes
Advertising /		Complete this form and circulate to your audience
Promotional Page		before the training event.
Attendance Sheet		Use this form to track attendance during your training
		session.
Subscriber Survey		Circulate the evaluation form at the end of your
Evaluation Form		training session so that participants can review and
		comment on the training. Return to CeriFi any
		evaluations that were completed. You do not have to
		return an evaluation for every participant.

Incomplete submissions will be returned to you.

"Group Internet Based" Format

CPE Credit

All CPE Network products are developed and intended to be delivered as 3 CPE credits. You should allocate sufficient time in your delivery so that there is no less than 2.5 clock hours:

50 minutes per CPE credit TIMES 3 credits = 150 minutes = 2.5 clock hours

If you wish to have a break during your training session, you should increase the length of the training beyond 2.5 hours as necessary. For example, you may wish to schedule your training from 9 AM to 12 PM and provide a ½ hour break from 10:15 to 10:45.

*Effective November 1, 2018: Checkpoint Learning CPE Network products 'group live' sessions must be delivered as 3 CPE credits and accredited to the field(s) of study as designated by Checkpoint Learning Network. Checkpoint Learning Network will not issue certificates for "group live" deliveries of less than 3 CPE credits (unless the course was delivered as 3 credits and there are partial credit exceptions (such as late arrivals and early departures). Therefore, if you decide to deliver the "group live" session with less than 3 CPE credits, your firm will be the sponsor as Checkpoint Learning Network will not issue certificates to your participants.

Advertising / Promotional Page

Create a promotion page (use the template following the executive summary in the transcript). You should circulate (e.g., email) to potential participants prior to training day. You will need to submit a copy of this page when you request certificates.

Monitoring Attendance in a Webinar

You must monitor individual participant attendance at "group internet based" programs to assign the correct number of CPE credits. A participant's self-certification of attendance alone is not sufficient.

Use the **Webinar Delivery Tracking Report.** This form lists the moderator(s) name and credentials, as well as the first and last name of each participant attending the seminar. During a webinar you must set up a monitoring mechanism (or polling mechanism) to periodically check the participants' engagement throughout the delivery of the program. Participants' two-way video should remain on during the entire presentation.

In order for CPE credit to be granted, you must confirm the presence of each participant **3 times per CPE hour and the participant must reply to the polling question**. Participants that respond to less than 3 polling questions in a CPE hour will not be granted CPE credit. For example, if a participant only replies to 2 of the 3 polling questions in the first CPE hour, credit for the first CPE hour will not be granted. (Refer to the Webinar Delivery Tracking Report for examples.)

Examples of polling questions:

You are using **Zoom** for your webinar. The moderator pauses approximately every 15 minutes and asks that participants confirm their attendance by using the "raise hands"

- feature. Once the participants raise their hands, the moderator records the participants who have their hands up in the **webinar delivery tracking report** by putting a YES in the webinar delivery tracking report. After documenting in the spreadsheet, the instructor (or moderator) drops everyone's hands and continues the training.
- 2. You are using **Teams** for your webinar. The moderator will pause approximately every 15 minutes and ask that participants confirm their attendance by typing "Present" into the Teams chat box. The moderator records the participants who have entered "Present" into the chat box into the **webinar delivery tracking report**. After documenting in the spreadsheet, the instructor (or moderator) continues the training.
- 3. If you are using an application that has a way to automatically send out polling questions to the participants, you can use that application/mechanism. However, following the event, you should create a **webinar delivery tracking report** from your app's report.

Additional Notes on Monitoring Mechanisms:

- 1. The monitoring mechanism does not have to be "content specific." Rather, the intention is to ensure that the remote participants are present and paying attention to the training.
- You should only give a minute or so for each participant to reply to the prompt. If, after a minute, a participant does not reply to the prompt, you should put a NO in the webinar delivery tracking report.
- 3. While this process may seem unwieldy at first, it is a required element that sponsors must adhere to. And after some practice, it should not cause any significant disruption to the training session.
- 4. You must include the Webinar Delivery Tracking report with your course submission if you are requesting certificates of completion for a "group internet based" delivery format.

Real Time Moderator During Program Presentation

"Group internet based" programs must have a **qualified**, **real time moderator while the program is being presented**. Program participants must be able to interact with the moderator while the course is in progress (including the opportunity to ask questions and receive answers during the presentation). This can be achieved via the webinar chat box, and/or by unmuting participants and allowing them to speak directly to the moderator.

Where individual participants log into a group live program they are required to enable two-way video to participate in a virtual face-to-face setting (with cameras on), elements of engagement are required (such as group discussion, polling questions, instructor posed questions with time for reflection, or a case study with engagement throughout the presentation) in order to award CPE credits to the participants. Participation in the two-way video conference must be monitored and documented by the instructor or attendance monitor in order to authenticate attendance for program duration. The participant-to-attendance

monitor ratio must not exceed 25:1, unless there is a dedicated attendance monitor in which case the participant-to-attendance monitor ratio must not exceed 100:1.

Make-Up Sessions

Individuals who are unable to attend the "group internet based" session may use the program materials for self-study either in print or online.

- If emailed materials are used, the user should read the materials, watch the
 video, and answer the quizzer questions on the CPE Quizzer Answer Sheet. Send
 the answer sheet and course evaluation to the email address listed on the
 answer sheet and the CPE certificate will be mailed or emailed to the user.
 Detailed instructions are provided on Network Program Self-Study Options.
- If the online materials are used, the user should log on to her/his individual
 Checkpoint Learning account to read the materials, watch the interviews, and
 answer the quizzer questions. The user will be able to print her/his CPE
 certificate upon completion of the quizzer. (If you need help setting up individual
 user accounts, please contact your firm administrator or customer service.)

Awarding CPE Certificates

The CPE certificate is the participant's record of attendance and is awarded by Checkpoint Learning Network after the "group internet based" documentation is received (and providing the course is delivered as 3 CPE credits). The certificate of completion will reflect the credit hours earned by the individual, with special calculation of credits for those who may not have answered the required amount of polling questions.

Subscriber Survey Evaluation Forms

Use the evaluation form. You must include a means for evaluating quality. At the conclusion of the "group live" session, evaluations should be distributed and any that are completed are collected from participants. Those evaluations that are completed by participants should be returned to Checkpoint Learning Network along with the other course materials. While it is required that you circulate the evaluation form to all participants, it is NOT required that the participants fill it out. A preprinted evaluation form is included in the transcript each month for your convenience.

Retention of Records

Regardless of whether Checkpoint Learning Network is the sponsor for the "group internet based" session, it is required that the firm hosting the session retain the following information for a period of five years from the date the program is completed unless state law dictates otherwise:

- Record of participation (Webinar Delivery Tracking Report)
- Copy of the program materials
- Timed agenda with topics covered
- Date and location (which would be "virtual") of course presentation
- Number of CPE credits and field of study breakdown earned by participants
- Instructor name and credentials
- Results of program evaluations

Finding the Transcript

Note: DVDs are no longer shipped effective 3/1/2023

When the DVD is inserted into a DVD drive, the video will immediately begin to play and the menu screen will pop up, taking the entire screen. Hitting the Esc key should minimize it to a smaller window. To locate the pdf file of the transcript either to save or email to others, go to the start button on the computer. In My Computer, open the drive with the DVD. It should look something like the screenshot below. The Adobe Acrobat files are the transcript files. If you do not currently have Adobe Acrobat Reader (Mac versions of the reader are also available), a free version of the reader may be downloaded at:

https://get.adobe.com/reader/

Alternatively, for those without a DVD drive, the email sent to administrators each month has a link to the pdf for the newsletter. The email may be forwarded to participants who may download the materials or print them as needed.

Requesting Participant CPE Certificates

When delivered as 3 CPE credits, documentation of your "group internet based" session should be sent to Checkpoint Learning Network by the following means:

Email: CPLgrading@CeriFi.com

When sending your package to CeriFi, you must include ALL the following items:

Form Name	Included?	Notes
Advertising /		Complete this form and circulate to your audience
Promotional Page		before the training event.
Webinar Delivery		Use this form to track the attendance (i.e., polling
Tracking Report		questions) during your training webinar.
Evaluation Form		Circulate the evaluation form at the end of your
		training session so that participants can review and
		comment on the training. Return to CeriFi any
		evaluations that were completed. You do not have to
		return an evaluation for every participant.

Incomplete submissions will be returned to you.

"Self-Study" Format

If you are unable to attend the live group study session, we offer two options for you to complete your Network Report program.

Self-Study—Email

Follow these simple steps to use the printed transcript and video:

- Watch the video.
- Review the supplemental materials.
- Read the discussion problems and the suggested answers.
- Complete the quizzer by filling out the bubble sheet enclosed with the transcript package.
- Complete the survey. We welcome your feedback and suggestions for topics of interest to you.
- E-mail your completed quizzer and survey to:

CPLgrading@cerifi.com

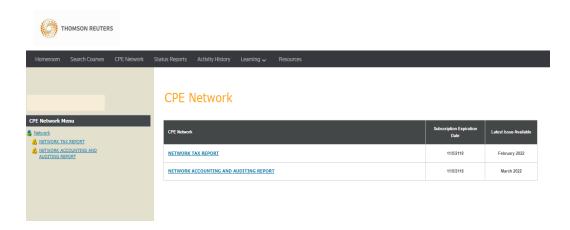
Self-Study-Online

Follow these simple steps to use the online program:

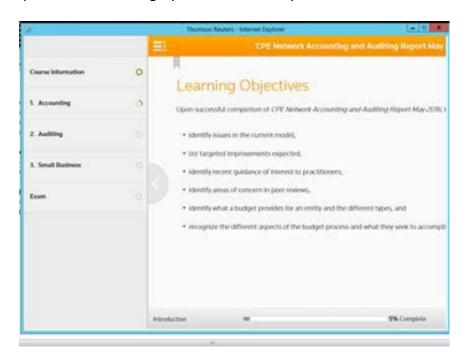
- Go to www.checkpointlearning.thomsonreuters.com.
- Log in using your username and password assigned by your firm's administrator in the upper right-hand margin ("Login or Register").



• In the **CPE Network** tab, select the desired Network Report and then the appropriate edition.

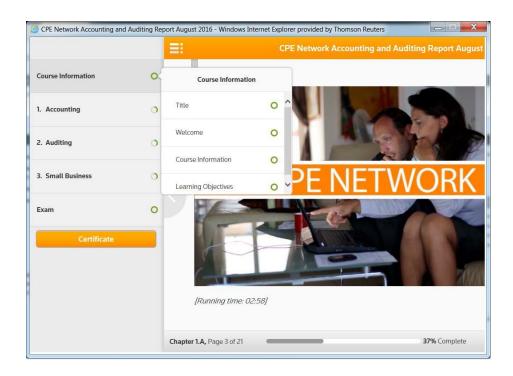


The Chapter Menu is in the gray bar at the left of your screen:



Click down to access the dropdown menu and move between the program Chapters.

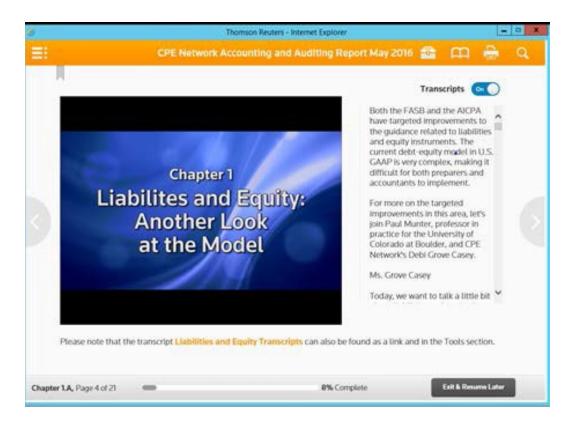
• **Course Information** is the course Overview, including information about the authors and the program learning objectives



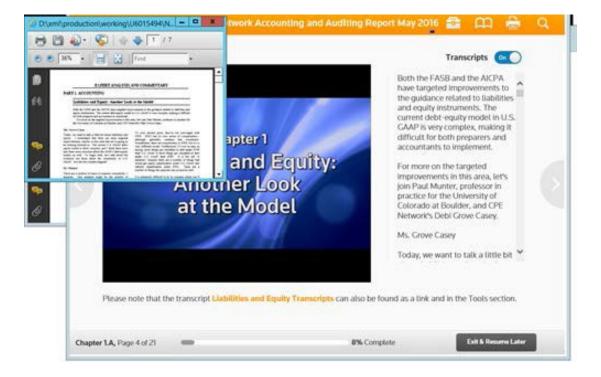
• Each Chapter is self-contained. Each chapter contains the executive summary and learning objectives for that segment, followed by the interview, the related supplemental materials, and then the discussion questions. This streamlined approach allows administrators and users to more easily access the related materials.



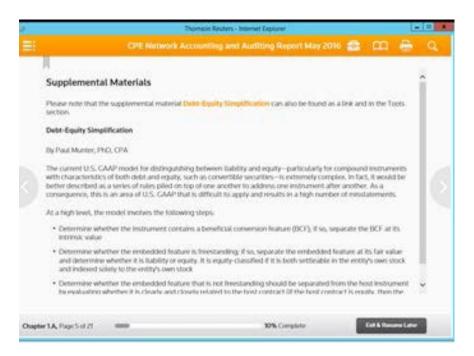
Video segments may be downloaded from the CPL player by clicking on the download button. Tip: you may need to scroll down to see the download button.

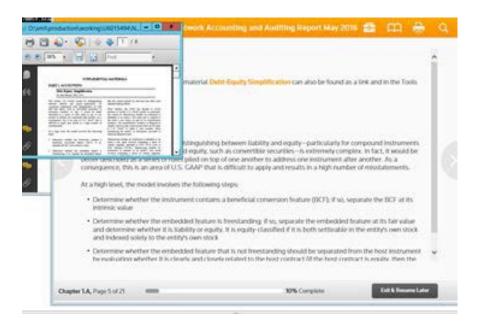


Transcripts for the interview segments can be viewed at the right side of the screen via a toggle button at the top labeled **Transcripts** or via the link to the pdf below the video (also available in the toolbox in the resources section). The pdf will appear in a separate pop-up window.



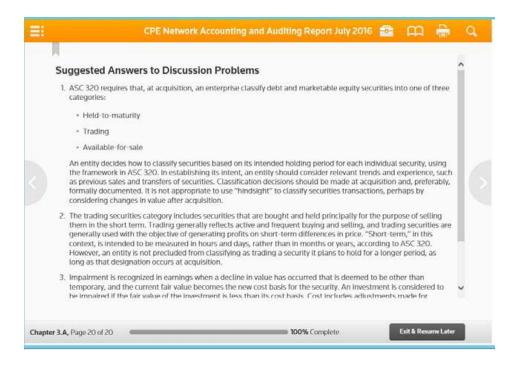
Click the arrow at the bottom of the video to play it, or click the arrow to the right side of the screen to advance to the supplemental material. As with the transcripts, the supplemental materials are also available via the toolbox and the link will pop up the pdf version in a separate window.





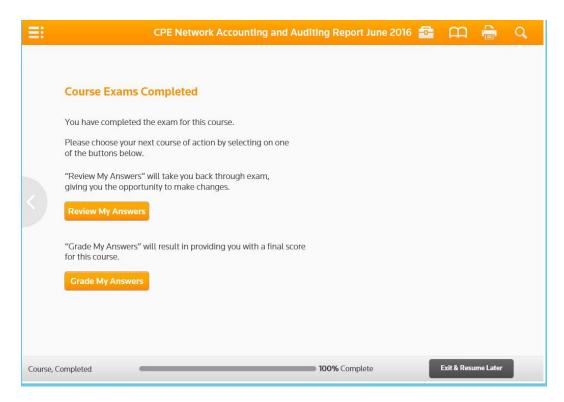
Continuing to click the arrow to the right side of the screen will bring the user to the Discussion p roblems related to the segment.

The Suggested Answers to the Discussion Problems follow the Discussion Problems.



The **Exam** is accessed by clicking the last gray bar on the menu at the left of the screen or clicking through to it. Click the orange button to begin.

When you have completed the quizzer, click the button labeled **Grade or the Review button**.



- Click the button labeled Certificate to print your CPE certificate.
- The final quizzer grade is displayed and you may view the graded answers by clicking the button labeled view graded answer.

Additional Features Search

Checkpoint Learning offers powerful search options. Click the **magnifying glass** at the upper right of the screen to begin your search. Enter your choice in the **Search For:** box.

Search Results are displayed with the number of hits.

Print

To display the print menu, click the printer icon in the upper bar of your screen. You can print the entire course, the transcript, the glossary, all resources, or selected portions of the course. Click your choice and click the orange **Print**.

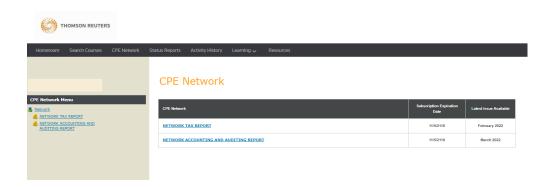
Transitioning From DVDs

Follow these simple steps to access the video and pdf for download from the online platform:

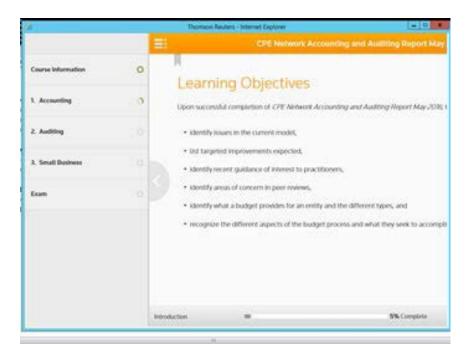
- Go to <u>www.checkpointlearning.thomsonreuters.com</u>.
- Log in using your username and password assigned by your firm's administrator in the upper right-hand margin ("Login").



• In the CPE **Network** tab, select the desired Network Report by clicking on the title, then select the appropriate edition.

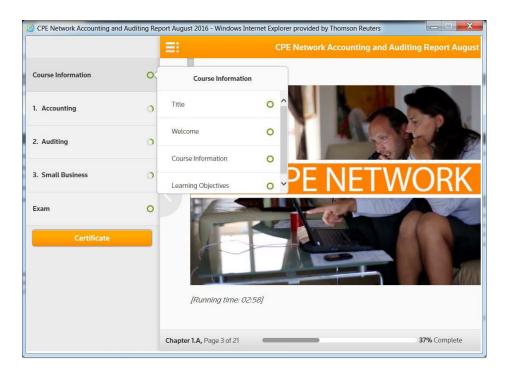


The Chapter Menu is in the gray bar at the left of your screen:



Click down to access the dropdown menu and move between the program Chapters.

• **Course Information** is the course Overview, including information about the authors and the program learning objectives



• Each Chapter is self-contained. Each chapter contains the executive summary and learning objectives for that segment, followed by the interview, the related supplemental materials, and then the discussion questions.



Video segments may be downloaded from the CPL player by clicking on the download button noted above. You may need to use the scroll bar to the right of the video to see the download button. Tip: You may need to use the scroll bar to the right of the video to see the download button.

PDFs may be downloaded from either the course toolbox in the upper right corner of the Checkpoint Learning screen or from the email sent to administrators with each release.

What Does It Mean to Be a CPE Sponsor?

If your organization chooses to vary from the instructions outlined in this User Guide, your firm will become the CPE Sponsor for this monthly series. The sponsor rules and requirements noted below are only highlights and reflect those of NASBA, the national body that sets guidance for development, presentation, and documentation for CPE programs. For any specific questions about state sponsor requirements, please contact your state board. They are the final authority regarding CPE Sponsor requirements. Generally, the following responsibilities are required of the sponsor:

- Arrange for a location for the presentation
- Advertise the course to your anticipated participants and disclose significant features of the program in advance
- Set the start time
- Establish participant sign-in procedures
- Coordinate audio-visual requirements with the facilitator
- Arrange appropriate breaks
- Have a real-time instructor during program presentation
- Ensure that the instructor delivers and documents elements of engagement
- Monitor participant attendance (make notations of late arrivals, early departures, and "no shows")
- Solicit course evaluations from participants
- Award CPE credit and issue certificates of completion
- Retain records for five years

The following information includes instructions and generic forms to assist you in fulfilling your responsibilities as program sponsor.

CPE Sponsor Requirements

Determining CPE Credit Increments

Sponsored seminars are measured by program length, with one 50-minute period equal to one CPE credit. One-half CPE credit increments (equal to 25 minutes) are permitted after the first credit has been earned. Sponsors must monitor the program length and the participants' attendance in order to award the appropriate number of CPE credits.

Program Presentation

CPE program sponsors must provide descriptive materials that enable CPAs to assess the appropriateness of learning activities. CPE program sponsors must make the following information available in advance:

- Learning objectives.
- Instructional delivery methods.
- Recommended CPE credit and recommended field of study.
- Prerequisites.
- Program level.
- Advance preparation.
- Program description.
- Course registration and, where applicable, attendance requirements.
- Refund policy for courses sold for a fee/cancellation policy.
- Complaint resolution policy.
- Official NASBA sponsor statement, if an approved NASBA sponsor (explaining final authority of acceptance of CPE credits).

Disclose Significant Features of Program in Advance

For potential participants to effectively plan their CPE, the program sponsor must disclose the significant features of the program in advance (e.g., through the use of brochures, website, electronic notices, invitations, direct mail, or other announcements). When CPE programs are offered in conjunction with non-educational activities, or when several CPE programs are offered concurrently, participants must receive an appropriate schedule of events indicating those components that are recommended for CPE credit. The CPE program sponsor's registration and attendance policies and procedures must be formalized, published, and made available to participants and include refund/cancellation policies as well as complaint resolution policies.

Monitor Attendance

While it is the participant's responsibility to report the appropriate number of credits earned, CPE program sponsors must maintain a process to monitor individual attendance at group programs to assign the correct number of CPE credits. A participant's self-certification of attendance alone is not sufficient. The sign-in sheet should list the names of each instructor and her/his credentials, as well as the name of each participant attending the seminar. The participant is expected to initial the sheet for their morning attendance and provide their signature for their afternoon attendance. If a participant leaves early, the hours they attended should be documented on the sign-in sheet and on the participant's CPE certificate.

Real Time Instructor During Program Presentation

"Group live" programs must have a qualified, real-time instructor while the program is being presented. Program participants must be able to interact with the real time instructor while the course is in progress (including the opportunity to ask questions and receive answers during the presentation).

Elements of Engagement

A "group live" program must include at least one element of engagement related to course content during each credit of CPE (for example, group discussion, polling questions, instructor-posed question with time for participant reflection, or use of a case study with different engagement elements throughout the program).

Awarding CPE Certificates

The CPE certificate is the participant's record of attendance and is awarded at the conclusion of the seminar. It should reflect the credit hours earned by the individual, with special calculation of credits for those who arrived late or left early.

CFP credit is available if the firm registers with the CFP board as a sponsor and meets the CFP board requirements. IRS credit is available only if the firm registers with the IRS as a sponsor and satisfies their requirements.

Seminar Quality Evaluations for Firm Sponsor

NASBA requires the seminar to include a means for evaluating quality. At the seminar conclusion, evaluations should be solicited from participants and retained by the sponsor for five years. The following statements are required on the evaluation and are used to determine whether:

- 1. Stated learning objectives were met.
- 2. Prerequisite requirements were appropriate (if any).
- 3. Program materials were accurate.
- 4. Program materials were relevant and contributed to the achievement of the learning objectives.
- 5. Time allotted to the learning activity was appropriate.
- 6. Individual instructors were effective.
- 7. Facilities and/or technological equipment were appropriate.
- 8. Handout or advance preparation materials were satisfactory.
- 9. Audio and video materials were effective.

You may use the enclosed preprinted evaluation forms for your convenience.

Retention of Records

The seminar sponsor is required to retain the following information for a period of five years from the date the program is completed unless state law dictates otherwise:

- Record of participation (the original sign-in sheets, now in an editable, electronic signable format)
- Copy of the program materials
- Timed agenda with topics covered and elements of engagement used
- Date and location of course presentation
- Number of CPE credits and field of study breakdown earned by participants
- Instructor name(s) and credentials
- Results of program evaluations

Appendix: Forms

Here are the forms noted above and how to get access to them.

Delivery Method	Form Name	Location	Notes
"Group Live" /	Advertising /	Transcript	Complete this form and
"Group Internet	Promotional Page		circulate to your audience
Based"			before the training event.
"Group Live"	Attendance Sheet	Transcript	Use this form to track
			attendance during your
			training session.
"Group Internet	Webinar Delivery	Transcript	Use this form to track the
Based"	Tracking Report		'polling questions' which
			are required to monitor
			attendance during your
			webinar.
"Group Live" /	Evaluation Form	Transcript	Circulate the evaluation
"Group Internet			form at the end of your
Based"			training session so that
			participants can review
			and comment on the
			training.
Self Study	CPE Quizzer Answer	Transcript	Use this form to record
	Sheet		your answers to the quiz.

Getting Help

Should you need support or assistance with your account, please see below:

Support Group	Phone Number	Email Address	Typical Issues/Questions
Technical Support	844.245.5970	Cplsupport@cerifi.com	 Browser-based Certificate discrepancies Accessing courses Migration questions Feed issues
Product Support	844.245.5970	Cplsupport@cerifi.com	 Functionality (how to use, where to find) Content questions Login Assistance
Customer Support	844.245.5970	Cplsupport@cerifi.com	 Billing Existing orders Cancellations Webinars Certificates