Cooley

Year-End Reporting for ISO Exercises and ESPP Stock Transfers

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This alert serves as a reminder of certain year-end reporting requirements imposed under Section 6039 of the Internal Revenue Code of 1986, as amended, with respect to:

- Incentive stock option (ISO) exercises by current and former employees.
- Transfers of stock acquired by current and former employees under a tax-qualified employee stock purchase plan (ESPP).

For each ISO exercise and ESPP stock transfer that occurred in 2023, a corporation must furnish an information statement to the current or former employee regarding such transaction no later than January 31, 2024, and it must file an information return with the IRS regarding such transaction no later than February 28, 2024,[1] if filing by paper, and no later than April 1, 2024,[2] if filing electronically. These reporting requirements are intended to provide current and former employees with sufficient information to enable them to calculate their tax obligations.

Employee information statement

Every corporation that in 2023 issued stock upon the exercise of an ISO – meaning a stock option as described in Section 422 of the Internal Revenue Code – must, on or before January 31, 2024, furnish to the current or former employee who exercised the option a written statement containing the information on Form 3921. Copy A of Form 3921 is filed with the IRS, copy B is furnished to the current or former employee, and copy C is retained by the corporation for its records.

The reporting deadlines noted above and below may be extended for taxpayers eligible for IRS-announced disaster relief. A full list of these extensions can be found on the IRS website.

Form 3921 is available on the IRS website, but a copy A downloaded from the IRS website should not be filed. The official printed version of this IRS form is scannable, but the online version of it, printed from the IRS website, is not. The official form may be ordered from the IRS website. Corporations also should note:

- A penalty of $310 per information return may be imposed for failing to file a correct form by the due date.
- The penalty is lowered to $60 if corrected within 30 days (by March 29 if the due date is February 28) and is lowered to $120 if corrected by August 1, 2024, up to an aggregate annual limit of $3,783,000, or $1,261,000 for small businesses.
- Penalties will not apply to any failure that the corporation can show was due to reasonable cause and not willful neglect.

Similarly, every corporation that in 2023 records or has recorded by its transfer agent a “first transfer”[3] by a current or former employee of stock acquired by such employee under an ESPP – meaning a plan that is established under Section 423 of the Internal Revenue Code – must, on or before January 31, 2024, furnish to the current or former employee who is transferring the stock a written statement containing the information on Form 3922 when the purchase price is either:

- Less than 100% of the value of the stock on the grant date.
- Not fixed or determinable on the grant date.

Form 3922 is available on the IRS website. Copy A of Form 3922 is filed with the IRS, copy B is furnished to the current or former employee, and copy C is retained by the corporation for its records. As explained above, the copy A that is filed with the IRS needs to be scannable.

Form of employee information statement

The employee information statement must either be:

- Contained on the appropriate form (i.e., Form 3921 for ISO exercises or Form 3922 for ESPP stock transfers).
- Contained on a substitute form that meets the format and content requirements in Publication 1179.

A separate form must be filed for each transaction and, if an employee has more than one transaction during the year, each form must contain a unique account number, such as a number provided by equity tracking software. However, if a substitute form is used, the company may aggregate transactions, providing a single form to each employee.

Delivery of employee information statement

Employee information statements, either copy B of the applicable form or an acceptable substitute, may be mailed or delivered to the current or former employee's last known address or may be sent electronically, provided that the person has given their consent to receive the statement electronically and the corporation meets certain other specified requirements.

IRS information return

A corporation is required to file an information return with the IRS, in addition to providing information statements to employees. For exercises and transfers occurring in 2023, the information returns must be filed no later than February 28, 2024, if filing by paper, and no later than April 1, 2024, if filing electronically (subject to extensions in certain declared disaster zones as noted above).

Companies filing 10 or more copies of Form 3921 or Form 3922 in a year (determined separately and not aggregated between them for purposes of this 10-form threshold) must file their information returns electronically. This limit has been significantly reduced from the 250-form limit applicable in prior years due to the 2023 finalization of regulations pursuant to T.D. 9972

The information returns must contain the same information required by the Section 6039 regulations with respect to employee information statements. Information returns for ISO exercises must be made on Form 3921, and information returns for ESPP stock transfers must be made on Form 3922.

It is possible to file Form 8809 to get an automatic 30-day extension to the due date for filing information returns. Form 8809 is available on the IRS website, and the extension will only extend the due date for filing the returns with the IRS, not the due date for furnishing statements to recipients.

Information requirements

As explained above, the information that corporations must provide to a current or former employee in an information statement is the same information that corporations must report to the IRS in an information return. When reporting this information, corporations should use the applicable form for both the information statement and the information return. Also, as described above, copy A of the applicable form is filed with the IRS, copy B is provided to the current or former employee, and copy C is retained for the corporation's records.

Form 3921 for ISO exercises must contain:

- The name, address and employer identification number of the corporation transferring the shares.
- The name, address and taxpayer identification number of the current or former employee to whom the shares were transferred pursuant to the exercise of the ISO.
- The grant date, the exercise price per share, the date of exercise, the fair market value per share on the date of exercise and the number of shares transferred pursuant to the exercise of the ISO.

Form 3922 for ESPP stock transfers must contain:

- The name, address and employer identification number of the corporation whose shares were transferred.
- The name, address and taxpayer identification number of the current or former employee who transferred the shares.
- The date the purchase right was granted to the current or former employee and the fair market value per share on the grant date.
- The purchase date, the fair market value per share on the purchase date and the purchase price paid per share on the purchase date.
- The number of shares to which legal title was transferred by the current or former employee, the date the legal title of the shares was first transferred by the current or former employee and – if the purchase price was not fixed or determinable on the grant date – the purchase price per share determined as if the shares were purchased on the grant date.

If you have any questions about the information contained in this alert, please contact a member of the Cooley compensation & benefits group.

Notes

1. Although there is a February 29 falling on a business day in 2024, the IRS publication setting forth 2024 filing deadlines has kept the February 28 deadline used in prior years.
2. In most years, this deadline is March 31, but as March 31 falls on a Sunday in 2024, the next business day applies.
3. The “first transfer” of ESPP stock from the employee/original owner includes a transfer to a brokerage account. This means that, generally speaking, the tax reporting obligation is triggered when the stock is deposited into the employee’s brokerage account. No transfer will be deemed to have occurred if the stock is issued directly to the employee (or held in book entry form by the company or a transfer agent). Instead, the reporting requirement will generally be triggered by the subsequent sale or transfer of the stock (including to a brokerage account).

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