

EFFECTIVE DATE OF 2006 AMENDMENT

Pub. L. 109-280, title VIII, §824(b)(1), Aug. 17, 2006, 120 Stat. 998, provided that the amendment made by section 824(b)(1) amends this section as in effect before the Tax Increase Prevention and Reconciliation Act of 2005, Pub. L. 109-222. See below.

Pub. L. 109-280, title VIII, §824(c), Aug. 17, 2006, 120 Stat. 999, provided that: “The amendments made by this section [amending this section] shall apply to distributions after December 31, 2007.”

Amendment by section 833(c) of Pub. L. 109-280 applicable to taxable years beginning after 2006, see section 833(d) of Pub. L. 109-280, set out as a note under section 25B of this title.

Pub. L. 109-222, title V, §512(c), May 17, 2006, 120 Stat. 366, provided that: “The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 2009.”

EFFECTIVE DATE OF 2001 AMENDMENT

Amendment by Pub. L. 107-16 applicable to taxable years beginning after Dec. 31, 2005, see section 617(f) of Pub. L. 107-16, set out as a note under section 402 of this title.

EFFECTIVE DATE OF 1998 AMENDMENTS

Amendment by Pub. L. 105-277 effective as if included in the provision of the Internal Revenue Service Restructuring and Reform Act of 1998, Pub. L. 105-206, to which such amendment relates, see section 4002(k) of Pub. L. 105-277, set out as a note under section 1 of this title.

Amendment by section 6005(b)(1)-(7), (9) of Pub. L. 105-206 effective, except as otherwise provided, as if included in the provisions of the Taxpayer Relief Act of 1997, Pub. L. 105-34, to which such amendment relates, see section 6024 of Pub. L. 105-206, set out as a note under section 1 of this title.

Pub. L. 105-206, title VII, §7004(b), July 22, 1998, 112 Stat. 833, provided that: “The amendment made by this section [amending this section] shall apply to taxable years beginning after December 31, 2004.”

EFFECTIVE DATE

Section applicable to taxable years beginning after Dec. 31, 1997, see section 302(f) of Pub. L. 105-34, set out as an Effective Date of 1997 Amendment note under section 219 of this title.

ROLLOVER OF AMOUNTS RECEIVED IN AIRLINE CARRIER BANKRUPTCY TO ROTH IRAS

Pub. L. 110-458, title I, §125, Dec. 23, 2008, 122 Stat. 5115, provided that:

“(a) GENERAL RULE.—If a qualified airline employee receives any airline payment amount and transfers any portion of such amount to a Roth IRA within 180 days of receipt of such amount (or, if later, within 180 days of the date of the enactment of this Act [Dec. 23, 2008]), then such amount (to the extent so transferred) shall be treated as a qualified rollover contribution described in section 408A(e) of the Internal Revenue Code of 1986, and the limitations described in section 408A(c)(3) of such Code shall not apply to any such transfer.

“(b) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

“(1) AIRLINE PAYMENT AMOUNT.—

“(A) IN GENERAL.—The term ‘airline payment amount’ means any payment of any money or other property which is payable by a commercial passenger airline carrier to a qualified airline employee—

“(i) under the approval of an order of a Federal bankruptcy court in a case filed after September 11, 2001, and before January 1, 2007, and

“(ii) in respect of the qualified airline employee’s interest in a bankruptcy claim against the carrier, any note of the carrier (or amount paid in lieu of a note being issued), or any other fixed obligation of the carrier to pay a lump sum amount.

The amount of such payment shall be determined without regard to any requirement to deduct and withhold tax from such payment under sections 3102(a) and 3402(a).

“(B) EXCEPTION.—An airline payment amount shall not include any amount payable on the basis of the carrier’s future earnings or profits.

“(2) QUALIFIED AIRLINE EMPLOYEE.—The term ‘qualified airline employee’ means an employee or former employee of a commercial passenger airline carrier who was a participant in a defined benefit plan maintained by the carrier which—

“(A) is a plan described in section 401(a) of the Internal Revenue Code of 1986 which includes a trust exempt from tax under section 501(a) of such Code, and

“(B) was terminated or became subject to the restrictions contained in paragraphs (2) and (3) of section 402(b) of the Pension Protection Act of 2006 [Pub. L. 109-280, 26 U.S.C. 430 note].

“(3) REPORTING REQUIREMENTS.—If a commercial passenger airline carrier pays 1 or more airline payment amounts, the carrier shall, within 90 days of such payment (or, if later, within 90 days of the date of the enactment of this Act [Dec. 23, 2008]), report—

“(A) to the Secretary of the Treasury, the names of the qualified airline employees to whom such amounts were paid, and

“(B) to the Secretary and to such employees, the years and the amounts of the payments.

Such reports shall be in such form, and contain such additional information, as the Secretary may prescribe.

“(c) EFFECTIVE DATE.—This section shall apply to transfers made after the date of the enactment of this Act [Dec. 23, 2008] with respect to airline payment amounts paid before, on, or after such date.”

**§ 409. Qualifications for tax credit employee stock ownership plans**

**(a) Tax credit employee stock ownership plan defined**

Except as otherwise provided in this title, for purposes of this title, the term “tax credit employee stock ownership plan” means a defined contribution plan which—

(1) meets the requirements of section 401(a),

(2) is designed to invest primarily in employer securities, and

(3) meets the requirements of subsections (b), (c), (d), (e), (f), (g), (h), and (o) of this section.

**(b) Required allocation of employer securities**

**(1) In general**

A plan meets the requirements of this subsection if—

(A) the plan provides for the allocation for the plan year of all employer securities transferred to it or purchased by it (because of the requirements of section 41(c)(1)(B))<sup>1</sup> to the accounts of all participants who are entitled to share in such allocation, and

(B) for the plan year the allocation to each participant so entitled is an amount which bears substantially the same proportion to the amount of all such securities allocated to all such participants in the plan for that year as the amount of compensation paid to such participant during that year bears to the compensation paid to all such participants during that year.

<sup>1</sup> See References in Text note below.

**(2) Compensation in excess of \$100,000 disregarded**

For purposes of paragraph (1), compensation of any participant in excess of the first \$100,000 per year shall be disregarded.

**(3) Determination of compensation**

For purposes of this subsection, the amount of compensation paid to a participant for any period is the amount of such participant's compensation (within the meaning of section 415(c)(3)) for such period.

**(4) Suspension of allocation in certain cases**

Notwithstanding paragraph (1), the allocation to the account of any participant which is attributable to the basic employee plan credit or the credit allowed under section 41<sup>1</sup> (relating to the employee stock ownership credit) may be extended over whatever period may be necessary to comply with the requirements of section 415.

**(c) Participants must have nonforfeitable rights**

A plan meets the requirements of this subsection only if it provides that each participant has a nonforfeitable right to any employer security allocated to his account.

**(d) Employer securities must stay in the plan**

A plan meets the requirements of this subsection only if it provides that no employer security allocated to a participant's account under subsection (b) (or allocated to a participant's account in connection with matched employer and employee contributions) may be distributed from that account before the end of the 84th month beginning after the month in which the security is allocated to the account. To the extent provided in the plan, the preceding sentence shall not apply in the case of—

(1) death, disability, separation from service, or termination of the plan;

(2) a transfer of a participant to the employment of an acquiring employer from the employment of the selling corporation in the case of a sale to the acquiring corporation of substantially all of the assets used by the selling corporation in a trade or business conducted by the selling corporation, or

(3) with respect to the stock of a selling corporation, a disposition of such selling corporation's interest in a subsidiary when the participant continues employment with such subsidiary.

This subsection shall not apply to any distribution required under section 401(a)(9) or to any distribution or reinvestment required under section 401(a)(28).

**(e) Voting rights**

**(1) In general**

A plan meets the requirements of this subsection if it meets the requirements of paragraph (2) or (3), whichever is applicable.

**(2) Requirements where employer has a registration-type class of securities**

If the employer has a registration-type class of securities, the plan meets the requirements of this paragraph only if each participant or beneficiary in the plan is entitled to direct the

plan as to the manner in which securities of the employer which are entitled to vote and are allocated to the account of such participant or beneficiary are to be voted.

**(3) Requirement for other employers**

If the employer does not have a registration-type class of securities, the plan meets the requirements of this paragraph only if each participant or beneficiary in the plan is entitled to direct the plan as to the manner in which voting rights under securities of the employer which are allocated to the account of such participant or beneficiary are to be exercised with respect to any corporate matter which involves the voting of such shares with respect to the approval or disapproval of any corporate merger or consolidation, recapitalization, reclassification, liquidation, dissolution, sale of substantially all assets of a trade or business, or such similar transaction as the Secretary may prescribe in regulations.

**(4) Registration-type class of securities defined**

For purposes of this subsection, the term, "registration-type class of securities" means—

(A) a class of securities required to be registered under section 12 of the Securities Exchange Act of 1934, and

(B) a class of securities which would be required to be so registered except for the exemption from registration provided in subsection (g)(2)(H) of such section 12.

**(5) 1 vote per participant**

A plan meets the requirements of paragraph (3) with respect to an issue if—

(A) the plan permits each participant 1 vote with respect to such issue, and

(B) the trustee votes the shares held by the plan in the proportion determined after application of subparagraph (A).

**(f) Plan must be established before employer's due date**

**(1) In general**

A plan meets the requirements of this subsection only if it is established on or before the due date (including any extension of such date) for the filing of the employer's tax return for the first taxable year of the employer for which an employee plan credit is claimed by the employer with respect to the plan.

**(2) Special rule for first year**

A plan which otherwise meets the requirements of this section shall not be considered to have failed to meet the requirements of section 401(a) merely because it was not established by the close of the first taxable year of the employer for which an employee plan credit is claimed by the employer with respect to the plan.

**(g) Transferred amounts must stay in plan even though investment credit is redetermined or recaptured**

A plan meets the requirement of this subsection only if it provides that amounts which are transferred to the plan (because of the requirements of section 48(n)(1) or 41(c)(1)(B))<sup>1</sup> shall remain in the plan (and, if allocated under the plan, shall remain so allocated) even though

part or all of the employee plan credit or the credit allowed under section 41<sup>1</sup> (relating to employee stock ownership credit) is recaptured or redetermined. For purposes of the preceding sentence, the references to section 48(n)(1)<sup>1</sup> and the employee plan credit shall refer to such section and credit as in effect before the enactment of the Tax Reform Act of 1984.

**(h) Right to demand employer securities; put option**

**(1) In general**

A plan meets the requirements of this subsection if a participant who is entitled to a distribution from the plan—

(A) has a right to demand that his benefits be distributed in the form of employer securities, and

(B) if the employer securities are not readily tradable on an established market, has a right to require that the employer repurchase employer securities under a fair valuation formula.

**(2) Plan may distribute cash in certain cases**

**(A) In general**

A plan which otherwise meets the requirements of this subsection or of section 4975(e)(7) shall not be considered to have failed to meet the requirements of section 401(a) merely because under the plan the benefits may be distributed in cash or in the form of employer securities.

**(B) Exception for certain plans restricted from distributing securities**

**(i) In general**

A plan to which this subparagraph applies shall not be treated as failing to meet the requirements of this subsection or section 401(a) merely because it does not permit a participant to exercise the right described in paragraph (1)(A) if such plan provides that the participant entitled to a distribution has a right to receive the distribution in cash, except that such plan may distribute employer securities subject to a requirement that such securities may be resold to the employer under terms which meet the requirements of paragraph (1)(B).

**(ii) Applicable plans**

This subparagraph shall apply to a plan which otherwise meets the requirements of this subsection or section 4975(e)(7) and which is established and maintained by—

(I) an employer whose charter or by-laws restrict the ownership of substantially all outstanding employer securities to employees or to a trust described in section 401(a), or

(II) an S corporation.

**(3) Special rule for banks**

In the case of a plan established and maintained by a bank (as defined in section 581) which is prohibited by law from redeeming or purchasing its own securities, the requirements of paragraph (1)(B) shall not apply if the plan provides that participants entitled to a distribution from the plan shall have a right to receive a distribution in cash.

**(4) Put option period**

An employer shall be deemed to satisfy the requirements of paragraph (1)(B) if it provides a put option for a period of at least 60 days following the date of distribution of stock of the employer and, if the put option is not exercised within such 60-day period, for an additional period of at least 60 days in the following plan year (as provided in regulations promulgated by the Secretary).

**(5) Payment requirement for total distribution**

If an employer is required to repurchase employer securities which are distributed to the employee as part of a total distribution, the requirements of paragraph (1)(B) shall be treated as met if—

(A) the amount to be paid for the employer securities is paid in substantially equal periodic payments (not less frequently than annually) over a period beginning not later than 30 days after the exercise of the put option described in paragraph (4) and not exceeding 5 years, and

(B) there is adequate security provided and reasonable interest paid on the unpaid amounts referred to in subparagraph (A).

For purposes of this paragraph, the term “total distribution” means the distribution within 1 taxable year to the recipient of the balance to the credit of the recipient’s account.

**(6) Payment requirement for installment distributions**

If an employer is required to repurchase employer securities as part of an installment distribution, the requirements of paragraph (1)(B) shall be treated as met if the amount to be paid for the employer securities is paid not later than 30 days after the exercise of the put option described in paragraph (4).

**(7) Exception where employee elected diversification**

Paragraph (1)(A) shall not apply with respect to the portion of the participant’s account which the employee elected to have reinvested under section 401(a)(28)(B) or subparagraph (B) or (C) of section 401(a)(35).

**(i) Reimbursement for expenses of establishing and administering plan**

A plan which otherwise meets the requirements of this section shall not be treated as failing to meet such requirements merely because it provides that—

**(1) Expenses of establishing plan**

As reimbursement for the expenses of establishing the plan, the employer may withhold from amounts due the plan for the taxable year for which the plan is established (or the plan may pay) so much of the amounts paid or incurred in connection with the establishment of the plan as does not exceed the sum of—

(A) 10 percent of the first \$100,000 which the employer is required to transfer to the plan for that taxable year under section 41(c)(1)(B),<sup>1</sup> and

(B) 5 percent of any amount so required to be transferred in excess of the first \$100,000; and

**(2) Administrative expenses**

As reimbursement for the expenses of administering the plan, the employer may withhold from amounts due the plan (or the plan may pay) so much of the amounts paid or incurred during the taxable year as expenses of administering the plan as does not exceed the lesser of—

(A) the sum of—

(i) 10 percent of the first \$100,000 of the dividends paid to the plan with respect to stock of the employer during the plan year ending with or within the employer's taxable year, and

(ii) 5 percent of the amount of such dividends in excess of \$100,000 or

(B) \$100,000.

**(j) Conditional contributions to the plan**

A plan which otherwise meets the requirements of this section shall not be treated as failing to satisfy such requirements (or as failing to satisfy the requirements of section 401(a) of this title or of section 403(c)(1) of the Employee Retirement Income Security Act of 1974) merely because of the return of a contribution (or a provision permitting such a return) if—

(1) the contribution to the plan is conditioned on a determination by the Secretary that such plan meets the requirements of this section,

(2) the application for a determination described in paragraph (1) is filed with the Secretary not later than 90 days after the date on which an employee plan credit is claimed, and

(3) the contribution is returned within 1 year after the date on which the Secretary issues notice to the employer that such plan does not satisfy the requirements of this section.

**(k) Requirements relating to certain withdrawals**

Notwithstanding any other law or rule of law—

(1) the withdrawal from a plan which otherwise meets the requirements of this section by the employer of an amount contributed for purposes of the matching employee plan credit shall not be considered to make the benefits forfeitable, and

(2) the plan shall not, by reason of such withdrawal, fail to be for the exclusive benefit of participants or their beneficiaries,

if the withdrawn amounts were not matched by employee contributions or were in excess of the limitations of section 415. Any withdrawal described in the preceding sentence shall not be considered to violate the provisions of section 403(c)(1) of the Employee Retirement Income Security Act of 1974. For purposes of this subsection, the reference to the matching employee plan credit shall refer to such credit as in effect before the enactment of the Tax Reform Act of 1984.

**(l) Employer securities defined**

For purposes of this section—

**(1) In general**

The term "employer securities" means common stock issued by the employer (or by a corporation which is a member of the same con-

trolled group) which is readily tradable on an established securities market.

**(2) Special rule where there is no readily tradable common stock**

If there is no common stock which meets the requirements of paragraph (1), the term "employer securities" means common stock issued by the employer (or by a corporation which is a member of the same controlled group) having a combination of voting power and dividend rights equal to or in excess of—

(A) that class of common stock of the employer (or of any other such corporation) having the greatest voting power, and

(B) that class of common stock of the employer (or of any other such corporation) having the greatest dividend rights.

**(3) Preferred stock may be issued in certain cases**

Noncallable preferred stock shall be treated as employer securities if such stock is convertible at any time into stock which meets the requirements of paragraph (1) or (2) (whichever is applicable) and if such conversion is at a conversion price which (as of the date of the acquisition by the tax credit employee stock ownership plan) is reasonable. For purposes of the preceding sentence, under regulations prescribed by the Secretary, preferred stock shall be treated as noncallable if after the call there will be a reasonable opportunity for a conversion which meets the requirements of the preceding sentence.

**(4) Application to controlled group of corporations****(A) In general**

For purposes of this subsection, the term "controlled group of corporations" has the meaning given to such term by section 1563(a) (determined without regard to subsections (a)(4) and (e)(3)(C) of section 1563).

**(B) Where common parent owns at least 50 percent of first tier subsidiary**

For purposes of subparagraph (A), if the common parent owns directly stock possessing at least 50 percent of the voting power of all classes of stock and at least 50 percent of each class of nonvoting stock in a first tier subsidiary, such subsidiary (and all other corporations below it in the chain which would meet the 80 percent test of section 1563(a) if the first tier subsidiary were the common parent) shall be treated as includible corporations.

**(C) Where common parent owns 100 percent of first tier subsidiary**

For purposes of subparagraph (A), if the common parent owns directly stock possessing all of the voting power of all classes of stock and all of the nonvoting stock, in a first tier subsidiary, and if the first tier subsidiary owns directly stock possessing at least 50 percent of the voting power of all classes of stock, and at least 50 percent of each class of nonvoting stock, in a second tier subsidiary of the common parent, such second tier subsidiary (and all other cor-

porations below it in the chain which would meet the 80 percent test of section 1563(a) if the second tier subsidiary were the common parent) shall be treated as includible corporations.

**(5) Nonvoting common stock may be acquired in certain cases**

Nonvoting common stock of an employer described in the second sentence of section 401(a)(22) shall be treated as employer securities if an employer has a class of nonvoting common stock outstanding and the specific shares that the plan acquires have been issued and outstanding for at least 24 months.

**(m) Nonrecognition of gain or loss on contribution of employer securities to tax credit employee stock ownership plan**

No gain or loss shall be recognized to the taxpayer with respect to the transfer of employer securities to a tax credit employee stock ownership plan maintained by the taxpayer to the extent that such transfer is required under section 41(c)(1)(B),<sup>1</sup> or subparagraph (A) or (B) of section 48(n)(1).<sup>1</sup>

**(n) Securities received in certain transactions**

**(1) In general**

A plan to which section 1042 applies and an eligible worker-owned cooperative (within the meaning of section 1042(c)) shall provide that no portion of the assets of the plan or cooperative attributable to (or allocable in lieu of) employer securities acquired by the plan or cooperative in a sale to which section 1042 applies may accrue (or be allocated directly or indirectly under any plan of the employer meeting the requirements of section 401(a))—

(A) during the nonallocation period, for the benefit of—

(i) any taxpayer who makes an election under section 1042(a) with respect to employer securities,

(ii) any individual who is related to the taxpayer (within the meaning of section 267(b)), or

(B) for the benefit of any other person who owns (after application of section 318(a)) more than 25 percent of—

(i) any class of outstanding stock of the corporation which issued such employer securities or of any corporation which is a member of the same controlled group of corporations (within the meaning of subsection (l)(4)) as such corporation, or

(ii) the total value of any class of outstanding stock of any such corporation.

For purposes of subparagraph (B), section 318(a) shall be applied without regard to the employee trust exception in paragraph (2)(B)(i).

**(2) Failure to meet requirements**

If a plan fails to meet the requirements of paragraph (1)—

(A) the plan shall be treated as having distributed to the person described in paragraph (1) the amount allocated to the account of such person in violation of paragraph (1) at the time of such allocation,

(B) the provisions of section 4979A shall apply, and

(C) the statutory period for the assessment of any tax imposed by section 4979A shall not expire before the date which is 3 years from the later of—

(i) the 1st allocation of employer securities in connection with a sale to the plan to which section 1042 applies, or

(ii) the date on which the Secretary is notified of such failure.

**(3) Definitions and special rules**

For purposes of this subsection—

**(A) Lineal descendants**

Paragraph (1)(A)(ii) shall not apply to any individual if—

(i) such individual is a lineal descendant of the taxpayer, and

(ii) the aggregate amount allocated to the benefit of all such lineal descendants during the nonallocation period does not exceed more than 5 percent of the employer securities (or amounts allocated in lieu thereof) held by the plan which are attributable to a sale to the plan by any person related to such descendants (within the meaning of section 267(c)(4)) in a transaction to which section 1042 applied.

**(B) 25-percent shareholders**

A person shall be treated as failing to meet the stock ownership limitation under paragraph (1)(B) if such person fails such limitation—

(i) at any time during the 1-year period ending on the date of sale of qualified securities to the plan or cooperative, or

(ii) on the date as of which qualified securities are allocated to participants in the plan or cooperative.

**(C) Nonallocation period**

The term “nonallocation period” means the period beginning on the date of the sale of the qualified securities and ending on the later of—

(i) the date which is 10 years after the date of sale, or

(ii) the date of the plan allocation attributable to the final payment of acquisition indebtedness incurred in connection with such sale.

**(o) Distribution and payment requirements**

A plan meets the requirements of this subsection if—

**(1) Distribution requirement**

**(A) In general**

The plan provides that, if the participant and, if applicable pursuant to sections 401(a)(11) and 417, with the consent of the participant's spouse elects, the distribution of the participant's account balance in the plan will commence not later than 1 year after the close of the plan year—

(i) in which the participant separates from service by reason of the attainment of normal retirement age under the plan, disability, or death, or

(ii) which is the 5th plan year following the plan year in which the participant

otherwise separates from service, except that this clause shall not apply if the participant is reemployed by the employer before distribution is required to begin under this clause.

**(B) Exception for certain financed securities**

For purposes of this subsection, the account balance of a participant shall not include any employer securities acquired with the proceeds of the loan described in section 404(a)(9) until the close of the plan year in which such loan is repaid in full.

**(C) Limited distribution period**

The plan provides that, unless the participant elects otherwise, the distribution of the participant's account balance will be in substantially equal periodic payments (not less frequently than annually) over a period not longer than the greater of—

- (i) 5 years, or
- (ii) in the case of a participant with an account balance in excess of \$800,000, 5 years plus 1 additional year (but not more than 5 additional years) for each \$160,000 or fraction thereof by which such balance exceeds \$800,000.

**(2) Cost-of-living adjustment**

The Secretary shall adjust the dollar amounts under paragraph (1)(C) at the same time and in the same manner as under section 415(d).

**(p) Prohibited allocations of securities in an S corporation**

**(1) In general**

An employee stock ownership plan holding employer securities consisting of stock in an S corporation shall provide that no portion of the assets of the plan attributable to (or allocable in lieu of) such employer securities may, during a nonallocation year, accrue (or be allocated directly or indirectly under any plan of the employer meeting the requirements of section 401(a)) for the benefit of any disqualified person.

**(2) Failure to meet requirements**

**(A) In general**

If a plan fails to meet the requirements of paragraph (1), the plan shall be treated as having distributed to any disqualified person the amount allocated to the account of such person in violation of paragraph (1) at the time of such allocation.

**(B) Cross reference**

**For excise tax relating to violations of paragraph (1) and ownership of synthetic equity, see section 4979A.**

**(3) Nonallocation year**

For purposes of this subsection—

**(A) In general**

The term “nonallocation year” means any plan year of an employee stock ownership plan if, at any time during such plan year—

- (i) such plan holds employer securities consisting of stock in an S corporation, and

- (ii) disqualified persons own at least 50 percent of the number of shares of stock in the S corporation.

**(B) Attribution rules**

For purposes of subparagraph (A)—

**(i) In general**

The rules of section 318(a) shall apply for purposes of determining ownership, except that—

- (I) in applying paragraph (1) thereof, the members of an individual's family shall include members of the family described in paragraph (4)(D), and

- (II) paragraph (4) thereof shall not apply.

**(ii) Deemed-owned shares**

Notwithstanding the employee trust exception in section 318(a)(2)(B)(i), an individual shall be treated as owning deemed-owned shares of the individual.

Solely for purposes of applying paragraph (5), this subparagraph shall be applied after the attribution rules of paragraph (5) have been applied.

**(4) Disqualified person**

For purposes of this subsection—

**(A) In general**

The term “disqualified person” means any person if—

- (i) the aggregate number of deemed-owned shares of such person and the members of such person's family is at least 20 percent of the number of deemed-owned shares of stock in the S corporation, or
- (ii) in the case of a person not described in clause (i), the number of deemed-owned shares of such person is at least 10 percent of the number of deemed-owned shares of stock in such corporation.

**(B) Treatment of family members**

In the case of a disqualified person described in subparagraph (A)(i), any member of such person's family with deemed-owned shares shall be treated as a disqualified person if not otherwise treated as a disqualified person under subparagraph (A).

**(C) Deemed-owned shares**

**(i) In general**

The term “deemed-owned shares” means, with respect to any person—

- (I) the stock in the S corporation constituting employer securities of an employee stock ownership plan which is allocated to such person under the plan, and

- (II) such person's share of the stock in such corporation which is held by such plan but which is not allocated under the plan to participants.

**(ii) Person's share of unallocated stock**

For purposes of clause (i)(II), a person's share of unallocated S corporation stock held by such plan is the amount of the unallocated stock which would be allocated to such person if the unallocated stock

were allocated to all participants in the same proportions as the most recent stock allocation under the plan.

**(D) Member of family**

For purposes of this paragraph, the term “member of the family” means, with respect to any individual—

- (i) the spouse of the individual,
- (ii) an ancestor or lineal descendant of the individual or the individual’s spouse,
- (iii) a brother or sister of the individual or the individual’s spouse and any lineal descendant of the brother or sister, and
- (iv) the spouse of any individual described in clause (ii) or (iii).

A spouse of an individual who is legally separated from such individual under a decree of divorce or separate maintenance shall not be treated as such individual’s spouse for purposes of this subparagraph.

**(5) Treatment of synthetic equity**

For purposes of paragraphs (3) and (4), in the case of a person who owns synthetic equity in the S corporation, except to the extent provided in regulations, the shares of stock in such corporation on which such synthetic equity is based shall be treated as outstanding stock in such corporation and deemed-owned shares of such person if such treatment of synthetic equity of 1 or more such persons results in—

- (A) the treatment of any person as a disqualified person, or
- (B) the treatment of any year as a non-allocation year.

For purposes of this paragraph, synthetic equity shall be treated as owned by a person in the same manner as stock is treated as owned by a person under the rules of paragraphs (2) and (3) of section 318(a). If, without regard to this paragraph, a person is treated as a disqualified person or a year is treated as a non-allocation year, this paragraph shall not be construed to result in the person or year not being so treated.

**(6) Definitions**

For purposes of this subsection—

**(A) Employee stock ownership plan**

The term “employee stock ownership plan” has the meaning given such term by section 4975(e)(7).

**(B) Employer securities**

The term “employer security” has the meaning given such term by section 409(l).

**(C) Synthetic equity**

The term “synthetic equity” means any stock option, warrant, restricted stock, deferred issuance stock right, or similar interest or right that gives the holder the right to acquire or receive stock of the S corporation in the future. Except to the extent provided in regulations, synthetic equity also includes a stock appreciation right, phantom stock unit, or similar right to a future cash payment based on the value of such stock or appreciation in such value.

**(7) Regulations and guidance**

**(A) In general**

The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this subsection.

**(B) Avoidance or evasion**

The Secretary may, by regulation or other guidance of general applicability, provide that a nonallocation year occurs in any case in which the principal purpose of the ownership structure of an S corporation constitutes an avoidance or evasion of this subsection.

(Added Pub. L. 95-600, title I, §141(a), Nov. 6, 1978, 92 Stat. 2787, §409A; amended Pub. L. 96-222, title I, §101(a)(7)(D)-(F), (I), (J), (L)(i)(VI), (ii)(I), (II), (iii)(V), (v)(VI), (VII), Apr. 1, 1980, 94 Stat. 198-200; Pub. L. 96-605, title II, §224(a), Dec. 28, 1980, 94 Stat. 3528; Pub. L. 97-34, title III, §§331(c)(1), 334, 336, 337(a), Aug. 13, 1981, 95 Stat. 293, 297, 298; Pub. L. 97-448, title I, §103(h), (i), Jan. 12, 1983, 96 Stat. 2379; renumbered §409 and amended Pub. L. 98-369, div. A, title IV, §474(r)(15), 491(e)(1), July 18, 1984, 98 Stat. 843, 852; Pub. L. 99-514, title XI, §§1172(b)(1), 1174(a)(1), (b)(1), (2), (c)(1)(A), 1176(b), title XVIII, §§1852(a)(4)(B), 1854(a)(3)(A), (f)(1), (3)(C), 1899A(11), Oct. 22, 1986, 100 Stat. 2514, 2516, 2517, 2520, 2865, 2873, 2881, 2882, 2958; Pub. L. 100-647, title I, §§1011B(g)(1), (2), (i)(1), (3), (j)(3), (5), (k)(3), 1018(t)(4)(B), (C), (H), Nov. 10, 1988, 102 Stat. 3490, 3492, 3493, 3588, 3589; Pub. L. 101-239, title VII, §§7304(a)(2)(A), (B), 7811(h)(1), Dec. 19, 1989, 103 Stat. 2352, 2353, 2409; Pub. L. 105-34, title XV, §1506(a), Aug. 5, 1997, 111 Stat. 1064; Pub. L. 107-16, title VI, §656(a), June 7, 2001, 115 Stat. 131; Pub. L. 107-147, title IV, §411(j)(2), Mar. 9, 2002, 116 Stat. 47; Pub. L. 109-280, title IX, §901(a)(2)(B), Aug. 17, 2006, 120 Stat. 1029; Pub. L. 113-295, div. A, title II, §221(a)(54), Dec. 19, 2014, 128 Stat. 4045; Pub. L. 115-141, div. U, title IV, §401(a)(79), Mar. 23, 2018, 132 Stat. 1187.)

**INFLATION ADJUSTED ITEMS FOR CERTAIN YEARS**

*For inflation adjustment of certain items in this section, see Internal Revenue Notices listed in a table under section 401 of this title.*

**REFERENCES IN TEXT**

Section 41, referred to in subsecs. (b)(1)(A), (4), (g), (i)(1)(A), and (m), which related to employee stock ownership credit, was repealed by Pub. L. 99-514, title XI, §1171(a), Oct. 22, 1986, 100 Stat. 2513. Section 30 of this title, relating to credit for increasing research activities, was renumbered section 41.

Section 12 of the Securities Exchange Act of 1934, referred to in subsec. (e)(4), is classified to section 78l of Title 15, Commerce and Trade.

Section 403(c)(1) of the Employee Retirement Income Security Act of 1974, referred to in subsecs. (j) and (k), is classified to section 1103(c)(1) of Title 29, Labor.

The enactment of the Tax Reform Act of 1984, referred to in subsecs. (g) and (k), means the enactment of div. A of Pub. L. 98-369, which was approved July 18, 1984.

Subsec. (n) of section 48, referred to in subsecs. (g) and (m), was repealed by section 474(o)(15) of Pub. L. 98-369.

**PRIOR PROVISIONS**

A prior section 409, added Pub. L. 93-406, title II, §2002(c), Sept. 2, 1974, 88 Stat. 964; amended Pub. L.

94-455, title XV, §1501(b)(6), title XIX, §§1901(a)(60), 1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1736, 1774, 1834; Pub. L. 95-600, title I, §§156(c)(2), (3), 157(e)(1)(B), Nov. 6, 1978, 92 Stat. 2803, 2806; Pub. L. 96-222, title I, §101(a)(14)(B), Apr. 1, 1980, 94 Stat. 204; Pub. L. 97-34, title III, §311(g)(1)(D), (3), Aug. 13, 1981, 95 Stat. 281; Pub. L. 97-248, title II, §243(b)(1)(B), title III, §335(a)(2), Sept. 3, 1982, 96 Stat. 523, 628; Pub. L. 97-452, §2(c)(1), Jan. 12, 1983, 96 Stat. 2478; Pub. L. 98-369, div. A, title I, §42(a)(7), title V, §522(d)(13), July 18, 1984, 98 Stat. 557, 871, related to retirement bonds, prior to repeal by Pub. L. 98-369, div. A, title IV, §491(b), (f)(1), July 18, 1984, 98 Stat. 848, 853, applicable to obligations issued after Dec. 31, 1983.

## AMENDMENTS

2018—Subsec. (n)(1)(A)(i). Pub. L. 115-141 substituted “securities,” for “securities...”.

2014—Subsec. (q). Pub. L. 113-295 struck out subsec. (q) which related to cross-references.

2006—Subsec. (h)(7). Pub. L. 109-280 inserted “or subparagraph (B) or (C) of section 401(a)(35)” before period at end.

2002—Subsec. (o)(1)(C)(ii). Pub. L. 107-147 substituted “\$800,000” for “\$500,000” in two places and “\$160,000” for “\$100,000”.

2001—Subsecs. (p), (q). Pub. L. 107-16 added subsec. (p) and redesignated former subsec. (p) as (q).

1997—Subsec. (h)(2). Pub. L. 105-34 designated existing provisions as subpar. (A), inserted subpar. heading, struck out “In the case of an employer whose charter or bylaws restrict the ownership of substantially all outstanding employer securities to employees or to a trust described in section 401(a), a plan which otherwise meets the requirements of this subsection or section 4975(e)(7) shall not be considered to have failed to meet the requirements of this subsection or of section 401(a) merely because it does not permit a participant to exercise the right described in paragraph (1)(A) if such plan provides that participants entitled to a distribution from the plan shall have a right to receive such distribution in cash, except that such plan may distribute employer securities subject to a requirement that such securities may be resold to the employer under terms which meet the requirements of paragraph (1)(B).” after “employer securities.”, and added subpar. (B).

1989—Subsec. (l)(5). Pub. L. 101-239, §7811(h)(1), substituted “the second sentence” for “the last sentence”.

Subsec. (n)(1). Pub. L. 101-239, §7304(a)(2)(A)(i), struck out “or section 2057” after “section 1042” in two places in introductory provisions.

Subsec. (n)(1)(A)(i). Pub. L. 101-239, §7304(a)(2)(A)(ii), struck out “or any decedent if the executor of the estate of such decedent makes a qualified sale to which section 2057 applies” after “employer securities.”.

Subsec. (n)(1)(A)(ii). Pub. L. 101-239, §7304(a)(2)(A)(iii), struck out “or the decedent” after “the taxpayer”.

Subsec. (n)(2)(C)(i), (3)(A)(ii). Pub. L. 101-239, §7304(a)(2)(B), struck out “or section 2057” after “section 1042”.

1988—Subsec. (d). Pub. L. 100-647, §1011B(j)(3), inserted “or to any distribution or reinvestment required under section 401(a)(28)” after “under section 401(a)(9)”.

Subsec. (e)(5). Pub. L. 100-647, §1018(t)(4)(H), substituted “paragraph (3)” for “paragraph (2) or (3)”.

Subsec. (h)(2). Pub. L. 100-647, §1018(t)(4)(B), substituted “paragraph (1)(B)” for “section 409(o)”.

Subsec. (h)(7). Pub. L. 100-647, §1011B(j)(5), added par. (7).

Subsec. (l)(4), (5). Pub. L. 100-647, §1011B(k)(3), redesignated par. (4), relating to nonvoting common stock may be acquired in certain cases, as (5).

Subsec. (n)(1). Pub. L. 100-647, §1011B(g)(1), made technical amendment to directory language of Pub. L. 99-514, §1172(b)(1). See 1986 Amendment note below.

Subsec. (n)(2)(C)(i), (3)(A)(ii). Pub. L. 100-647, §1011B(g)(2), inserted “or section 2057” after “which section 1042”.

Subsec. (n)(3)(C). Pub. L. 100-647, §1018(t)(4)(C), amended subpar. (C) generally. Prior to amendment,

subpar. (C) read as follows: “The term ‘nonallocation period’ means the 10-year period beginning on the later of—

“(i) the date of the sale of the qualified securities, or

“(ii) the date of the plan allocation attributable to the final payment of acquisition indebtedness incurred in connection with such sale.”

Subsec. (o)(1)(A). Pub. L. 100-647, §1011B(i)(3), substituted “if the participant and, if applicable pursuant to sections 401(a)(11) and 417, with the consent of the participant’s spouse elects” for “unless the participant otherwise elects”.

Subsec. (o)(1)(A)(ii). Pub. L. 100-647, §1011B(i)(1), substituted “distribution is required to begin under this clause” for “such year”.

1986—Subsec. (a)(3). Pub. L. 99-514, §1174(b)(2), inserted reference to subsec. (o).

Subsec. (d). Pub. L. 99-514, §1899A(11), substituted “participant’s” for “participants’s”.

Pub. L. 99-514, §1852(a)(4)(B), inserted at end “This subsection shall not apply to any distribution required under section 401(a)(9).”

Subsec. (d)(1). Pub. L. 99-514, §1174(a)(1), substituted “separation from service, or termination of the plan” for “or separation from service”.

Subsec. (e)(2). Pub. L. 99-514, §1854(f)(1)(C), (D), inserted “or beneficiary” after “participant” in two places and substituted “securities of the employer” for “employer securities”.

Subsec. (e)(3). Pub. L. 99-514, §1854(f)(1)(B)–(D), inserted “or beneficiary” after “participant” in two places and substituted “securities of the employer” for “employer securities” and “any corporate matter which involves the voting of such shares with respect to the approval or disapproval of any corporate merger or consolidation, recapitalization, reclassification, liquidation, dissolution, sale of substantially all assets of a trade or business, or such similar transaction as the Secretary may prescribe in regulations” for “a corporate matter which (by law or charter) must be decided by more than a majority vote of outstanding common shares voted”.

Subsec. (e)(5). Pub. L. 99-514, §1854(f)(1)(A), added par. (5).

Subsec. (h)(2). Pub. L. 99-514, §1854(f)(3)(C), inserted “, except that such plan may distribute employer securities subject to a requirement that such securities may be resold to the employer under terms which meet the requirements of section 409(o)”.

Subsec. (h)(5), (6). Pub. L. 99-514, §1174(c)(1)(A), added pars. (5) and (6).

Subsec. (l)(4). Pub. L. 99-514, §1176(b), added par. (4) relating to acquisition of nonvoting common stock.

Subsec. (n). Pub. L. 99-514, §1854(a)(3)(A), added subsec. (n). Former subsec. (n) redesignated (o).

Subsec. (n)(1). Pub. L. 99-514, §1172(b)(1), as amended by Pub. L. 100-647, §1011B(g)(1), inserted “or section 2057” in two places in introductory provisions, “or any decedent if the executor of the estate of such decedent makes a qualified sale to which section 2057 applies,” in subpar. (A)(i), and “or the decedent” in subpar. (A)(ii).

Subsec. (o). Pub. L. 99-514, §1174(b)(1), added subsec. (o). Former subsec. (o) redesignated (p).

Pub. L. 99-514, §1854(a)(3)(A), redesignated former subsec. (n) as (o).

Subsec. (p). Pub. L. 99-514, §1174(b)(1), redesignated former subsec. (o) as (p).

1984—Subsec. (b)(1)(A). Pub. L. 98-369, §474(r)(15)(A), (B), substituted “41” for “44G” and struck out “48(n)(1)(A) or” after “requirements of section”.

Subsec. (b)(4). Pub. L. 98-369, §474(r)(15)(A), substituted “41” for “44G”.

Subsec. (g). Pub. L. 98-369, §474(r)(15)(A), (C), substituted “41” for “44G” in two places, and inserted provision directing that, for purposes of the preceding sentence, the references to section 48(n)(1) and the employee plan credit shall refer to such section and credit as in effect before the enactment of the Tax Reform Act of 1984.



Subsec. (i)(1)(A). Pub. L. 98-369, § 474(r)(15)(A), (D), substituted “41” for “44G”, and struck out “48(n)(1) or” after “taxable year under section”.

Subsec. (k). Pub. L. 98-369, § 474(r)(15)(E), inserted provision requiring that, for purposes of this subsection, the reference to the matching employee plan credit refer to such credit as in effect before the enactment of the Tax Reform Act of 1984.

Subsec. (m). Pub. L. 98-369, § 474(r)(15)(A), substituted “41” for “44G”.

Subsec. (n)(3). Pub. L. 98-369, § 474(r)(15)(A), substituted “41” for “44G”.

1983—Subsec. (d)(2). Pub. L. 97-448, § 103(i), struck out provisions covering the sale of substantially all of the stock of a subsidiary of the employer.

Subsec. (h)(2). Pub. L. 97-448, § 103(h), substituted “the requirements of this subsection or of section 401(a)” for “the requirements of section 401(a)”.

1981—Subsec. (b). Pub. L. 97-34, § 331(c)(1)(A), (B), inserted in par. (1)(A) reference to section 44G(c)(1)(B), and inserted in par. (4) “or the credit allowed under section 44G (relating to the employee stock ownership credit)” after “basic employee plan credit”.

Subsec. (d). Pub. L. 97-34, § 337, designated provision relating to death, disability, or separation from service as par. (1) and added pars. (2) and (3).

Subsec. (g). Pub. L. 97-34, § 331(c)(1)(C), (D), inserted reference to section 44G(c)(1)(B) and inserted “or the credit allowed under section 44G (relating to employee stock ownership credit)” after “employee plan credit”.

Subsec. (h)(2). Pub. L. 97-34, § 334, substituted “this subsection” for “this section” and inserted provision respecting receipt of distributions in cash where employer’s charter or bylaws restrict ownership of substantially all outstanding employer securities to employees or to a section 401(a) trust where a participant is not permitted to exercise the right described in par. (1)(A).

Subsec. (h)(3), (4). Pub. L. 97-34, § 336, added pars. (3) and (4).

Subsec. (i)(1)(A). Pub. L. 97-34, § 331(c)(1)(E), inserted reference to section 44G(c)(1)(B).

Subsec. (m). Pub. L. 97-34, § 331(c)(1)(F), inserted reference to section 44G(c)(1)(B).

Subsec. (n)(2), (3). Pub. L. 97-34, § 331(c)(1)(G), (H), inserted “or employee stock ownership credit” after “employee plan credit” in par. (2) and added par. (3).

1980—Pub. L. 96-222, § 101(a)(7)(L)(v)(VII), substituted “tax credit employee stock ownership plans” for “ESOPs” in section catchline.

Subsec. (a). Pub. L. 96-222, § 101(a)(7)(L)(ii)(I), (v)(VI), substituted in heading and in text “tax credit employee stock ownership plan” for “ESOP”.

Subsec. (b)(4). Pub. L. 96-222, § 101(a)(7)(L)(iii)(V), substituted “employee plan credit” for “ESOP credit”.

Subsec. (d). Pub. L. 96-222, § 101(a)(7)(F), inserted “(or allocated to a participant’s account in connection with matched employer and employee contributions)” after “under subsection (b)”.

Subsec. (f)(1). Pub. L. 96-222, § 101(a)(7)(I)(i), substituted “only if it is established on or before the due date (including any extension of such date) for the filing of the employer’s tax return for the first taxable year of the employer for which an employee plan credit is claimed by the employer with respect to the plan” for “for a plan year only if it is established on or before the due date for the filing of the employer’s tax return for the taxable year (including any extension of such date) in which or with which the plan year ends”.

Subsec. (f)(2). Pub. L. 96-222, § 101(a)(7)(I)(ii), (L)(v)(VII), substituted “employee plan” for “ESOP” and inserted “with respect to the plan” after “by the employer”.

Subsec. (g). Pub. L. 96-222, § 101(a)(7)(L)(iii)(V), substituted “employee plan credit” for “ESOP credit”.

Subsec. (h)(2). Pub. L. 96-222, § 101(a)(7)(E), inserted “or of section 4975(e)(7)” after “the requirements of this section”.

Subsecs. (j)(2), (k)(1). Pub. L. 96-222, § 101(a)(7)(L)(iii)(V), substituted “employee plan credit” for “ESOP credit”.

Subsec. (J)(2)(B). Pub. L. 96-222, § 101(a)(7)(J)(i), substituted “class of common stock” for “class of stock”.

Subsec. (J)(3). Pub. L. 96-222, § 101(a)(7)(J)(ii), (L)(ii)(II), substituted “as employer securities” for “as meeting the requirements of paragraph (1)”, “paragraph (1) or (2)” for “paragraph (2)”, and “tax credit employee stock ownership plan” for “ESOP” and inserted provisions requiring preferred stock to be treated as noncallable if after the call there will be a reasonable opportunity for a conversion which meets the requirements of the preceding sentence.

Subsec. (I)(4). Pub. L. 96-605 substituted in heading “Application to controlled group of corporations” for “Controlled group of corporations defined” and in subpar. (B) heading “Where common parent owns at least” for “Common parent may own only” and added subpar. (C).

Subsec. (m). Pub. L. 96-222, § 101(a)(7)(D), (L)(i), substituted provisions relating to nonrecognition of gain or loss on contribution of employer securities to a tax credit employee stock ownership plan for provisions relating to contributions of stock of a controlling corporation.

Subsec. (n). Pub. L. 96-222, § 101(a)(7)(L)(iii)(V), substituted “employee plan credit” for “ESOP credit” in pars. (1) and (2).

#### EFFECTIVE DATE OF 2014 AMENDMENT

Amendment by Pub. L. 113-295 effective Dec. 19, 2014, subject to a savings provision, see section 221(b) of Pub. L. 113-295, set out as a note under section 1 of this title.

#### EFFECTIVE DATE OF 2006 AMENDMENT

Amendment by Pub. L. 109-280 applicable to plan years beginning after Dec. 31, 2006, with special rules for collectively bargained agreements and certain employer securities held in an ESOP, see section 901(c) of Pub. L. 109-280, set out as a note under section 401 of this title.

#### EFFECTIVE DATE OF 2002 AMENDMENT

Amendment by Pub. L. 107-147 effective as if included in the provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. 107-16, to which such amendment relates, see section 411(x) of Pub. L. 107-147, set out as a note under section 25B of this title.

#### EFFECTIVE DATE OF 2001 AMENDMENT

Pub. L. 107-16, title VI, § 656(d), June 7, 2001, 115 Stat. 135, provided that:

“(1) IN GENERAL.—The amendments made by this section [amending this section and sections 4975 and 4979A of this title] shall apply to plan years beginning after December 31, 2004.

“(2) EXCEPTION FOR CERTAIN PLANS.—In the case of any—

“(A) employee stock ownership plan established after March 14, 2001, or

“(B) employee stock ownership plan established on or before such date if employer securities held by the plan consist of stock in a corporation with respect to which an election under section 1362(a) of the Internal Revenue Code of 1986 is not in effect on such date, the amendments made by this section shall apply to plan years ending after March 14, 2001.”

#### EFFECTIVE DATE OF 1997 AMENDMENT

Pub. L. 105-34, title I, § 1506(c), Aug. 5, 1997, 111 Stat. 1066, provided that: “The amendments made by this section [amending this section, section 4975 of this title, and section 1108 of Title 29, Labor] shall apply to taxable years beginning after December 31, 1997.”

#### EFFECTIVE DATE OF 1989 AMENDMENT

Pub. L. 101-239, title VII, § 7304(a)(3), Dec. 19, 1989, 103 Stat. 2353, provided that: “The amendments made by this subsection [amending this section and sections 4978 and 4979A of this title and repealing sections 2057 and

4978A of this title] shall apply to the estates of decedents dying after the date of the enactment of this Act [Dec. 19, 1989].”

Amendment by section 7811(h)(1) of Pub. L. 101-239 effective, except as otherwise provided, as if included in the provision of the Technical and Miscellaneous Revenue Act of 1988, Pub. L. 100-647, to which such amendment relates, see section 7817 of Pub. L. 101-239, set out as a note under section 1 of this title.

#### EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by Pub. L. 100-647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99-514, to which such amendment relates, see section 1019(a) of Pub. L. 100-647, set out as a note under section 1 of this title.

#### EFFECTIVE DATE OF 1986 AMENDMENT

Pub. L. 99-514, title XI, §1172(c), Oct. 22, 1986, 100 Stat. 2515, provided that: “The amendments made by this section [enacting section 2057 of this title and amending this section and section 4979A of this title] shall apply to sales after the date of the enactment of this Act [Oct. 22, 1986] with respect to which an election is made by the executor of an estate who is required to file the return of the tax imposed by the Internal Revenue Code of 1986 on a date (including extensions) after the date of the enactment of this Act.”

Pub. L. 99-514, title XI, §1174(a)(2), Oct. 22, 1986, 100 Stat. 2516, as amended by Pub. L. 100-647, title I, §1011B(i)(2), Nov. 10, 1988, 102 Stat. 3492, provided that: “The amendment made by this subsection [amending this section] shall apply to distributions after December 31, 1984.”

Pub. L. 99-514, title XI, §1174(b)(3), Oct. 22, 1986, 100 Stat. 2517, provided that: “The amendments made by this subsection [amending this section] shall apply to distributions attributable to stock acquired after December 31, 1986.”

Pub. L. 99-514, title XI, §1174(c)(1)(B), Oct. 22, 1986, 100 Stat. 2518, provided that: “The amendment made by this paragraph [amending this section] shall apply to distributions attributable to stock acquired after December 31, 1986, except that a plan may elect to have such amendment apply to all distributions after the date of the enactment of this Act [Oct. 22, 1986].”

Amendment by section 1176(b) of Pub. L. 99-514 applicable to acquisitions of securities after Dec. 31, 1986, see section 1176(c) of Pub. L. 99-514, set out as a note under section 401 of this title.

Amendment by section 1852(a)(4)(B) of Pub. L. 99-514 effective, except as otherwise provided, as if included in the provisions of the Tax Reform Act of 1984, Pub. L. 98-369, div. A, to which such amendment relates, see section 1881 of Pub. L. 99-514, set out as a note under section 48 of this title.

Pub. L. 99-514, title XVIII, §1854(a)(3)(C), Oct. 22, 1986, 100 Stat. 2874, as amended by Pub. L. 100-647, title I, §1018(t)(4)(G), Nov. 10, 1988, 102 Stat. 3588, provided that:

“(i) Except as provided in clause (ii), the amendments made by this paragraph [amending this section and section 1042 of this title] shall apply to sales of securities after the date of the enactment of this Act [Oct. 22, 1986].

“(ii) A taxpayer or executor may elect to have section 1042(b)(3) of the Internal Revenue Code of 1954 (as in effect before the amendment made by subparagraph (B)) apply to sales before the date of the enactment of this Act as if such section included the last sentence of section 409(n)(1) of the Internal Revenue Code of 1986 (as added by subparagraph (A)).”

Pub. L. 99-514, title XVIII, §1854(f)(4)(A), (B), Oct. 22, 1986, 100 Stat. 2882, provided that:

“(A) The amendments made by paragraph (1)(A) and (3) [amending this section and sections 1042 and 4975 of this title] shall take effect on the date of the enactment of this Act [Oct. 22, 1986].”

“(B) The amendments made by subparagraphs (B), (C), and (D) of paragraph (1) [amending this section]

shall apply after December 31, 1986, to stock acquired after December 31, 1979.”

#### EFFECTIVE DATE OF 1984 AMENDMENT

Amendment by section 474(r)(15) of Pub. L. 98-369 applicable to taxable years beginning after Dec. 31, 1983, and to carrybacks from such years, see section 475(a) of Pub. L. 98-369, set out as a note under section 21 of this title.

Redesignation of section 409A as 409 by section 491(e)(1) of Pub. L. 98-369 effective Jan. 1, 1984, see section 491(f)(3) of Pub. L. 98-369, set out as a note under section 401 of this title.

#### EFFECTIVE DATE OF 1983 AMENDMENT

Amendment by Pub. L. 97-448 effective, except as otherwise provided, as if it had been included in the provision of the Economic Recovery Tax Act of 1981, Pub. L. 97-34, to which such amendment relates, see section 109 of Pub. L. 97-448, set out as a note under section 1 of this title.

#### EFFECTIVE DATE OF 1981 AMENDMENT

Amendment by section 331(c)(1) of Pub. L. 97-34 applicable to taxable years ending after Dec. 31, 1982, see section 331(f)(2) of Pub. L. 97-34, set out as a note under section 404 of this title.

Pub. L. 97-34, title III, §337(b), Aug. 13, 1981, 95 Stat. 298, as amended by Pub. L. 99-514, §2, Oct. 22, 1986, 100 Stat. 2095, provided that: “The amendments made by this section [amending this section] shall apply to distributions described in section 409A(d) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954] (or any corresponding provision of prior law) made after March 29, 1975.”

Amendment by sections 334 and 336 of Pub. L. 97-34 applicable to taxable years beginning after Dec. 31, 1981, see section 339 of Pub. L. 97-34, set out as a note under section 401 of this title.

#### EFFECTIVE DATE OF 1980 AMENDMENTS

Pub. L. 96-605, title II, §224(b), Dec. 28, 1980, 94 Stat. 3529, provided that: “The amendment made by subsection (a) [amending this section] shall apply with respect to qualified investment for taxable years beginning after December 31, 1978.”

Amendment by Pub. L. 96-222 effective, except as otherwise provided, as if it had been included in the provisions of the Revenue Act of 1978, Pub. L. 95-600, to which such amendment relates, see section 201 of Pub. L. 96-222, set out as a note under section 32 of this title.

#### EFFECTIVE DATE

Pub. L. 95-600, title I, §141(g), Nov. 6, 1978, 92 Stat. 2795, as added by Pub. L. 96-222, title I, §101(a)(7)(B), Apr. 1, 1980, 94 Stat. 197; amended by Pub. L. 99-514, §2, Oct. 22, 1986, 100 Stat. 2095, provided that:

“(1) IN GENERAL.—Except as otherwise provided in this subsection and subsection (h) [set out as an Effective Date of 1978 Amendment note under section 4975 of this title], the amendments made by this section [enacting sections 409A [now 409] and 6699 of this title and amending sections 46, 48, 56, 401, 404, 415, 805, 1504, and 4975 of this title] shall apply with respect to qualified investment for taxable years beginning after December 31, 1978.

“(2) ELECTION TO HAVE AMENDMENTS APPLY DURING 1978.—At the election of the taxpayer, paragraph (1) shall be applied by substituting ‘December 31, 1977’ for ‘December 31, 1978’; except that in the case of a plan in existence before December 31, 1978, any such election shall not affect the required allocation of employer securities attributable to qualified investment for taxable years beginning before January 1, 1979. An election under the preceding sentence shall be made at such time and in such manner as the Secretary of the Treasury or his delegate shall prescribe. Such an election, once made, shall be irrevocable.

“(3) VOTING RIGHT PROVISIONS.—Section 409A(e) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954] (as

added by subsection (a) [now section 409] shall apply to plans to which section 409A of such Code applies, beginning with the first day of such application.

“(4) RIGHT TO DEMAND EMPLOYER SECURITIES, ETC.—Paragraphs (1)(A) and (2) of section 409A(h) of the Internal Revenue Code of 1986 (as added by subsection (a)) [now section 409] shall apply to distributions after December 31, 1978, made by a plan to which section 409A of such Code applies.

“(5) SUBSECTION (f)(7).—The amendment made by subsection (f)(7) [amending section 415 of this title] shall apply to years beginning after December 31, 1978.

“(6) RETROACTIVE APPLICATION OF AMENDMENT MADE BY SUBSECTION (d).—In determining the regular tax deduction under [former] section 56(c) of the Internal Revenue Code of 1986 for any taxable year beginning before January 1, 1979, the amount of the credit allowable under section 38 of such Code shall be determined without regard to section 46(a)(2)(B) of such Code (as in effect before the enactment of the Energy Tax Act of 1978 [Nov. 9, 1978]).”

PLAN AMENDMENTS NOT REQUIRED UNTIL  
JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§ 1101–1147 and 1171–1177] or title XVIII [§§ 1800–1899A] of Pub. L. 99–514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99–514, as amended, set out as a note under section 401 of this title.

**§ 409A. Inclusion in gross income of deferred compensation under nonqualified deferred compensation plans**

**(a) Rules relating to constructive receipt**

**(1) Plan failures**

**(A) Gross income inclusion**

**(i) In general**

If at any time during a taxable year a nonqualified deferred compensation plan—

(I) fails to meet the requirements of paragraphs (2), (3), and (4), or

(II) is not operated in accordance with such requirements,

all compensation deferred under the plan for the taxable year and all preceding taxable years shall be includible in gross income for the taxable year to the extent not subject to a substantial risk of forfeiture and not previously included in gross income.

**(ii) Application only to affected participants**

Clause (i) shall only apply with respect to all compensation deferred under the plan for participants with respect to whom the failure relates.

**(B) Interest and additional tax payable with respect to previously deferred compensation**

**(i) In general**

If compensation is required to be included in gross income under subparagraph (A) for a taxable year, the tax imposed by this chapter for the taxable year shall be increased by the sum of—

(I) the amount of interest determined under clause (ii), and

(II) an amount equal to 20 percent of the compensation which is required to be included in gross income.

**(ii) Interest**

For purposes of clause (i), the interest determined under this clause for any taxable year is the amount of interest at the underpayment rate plus 1 percentage point on the underpayments that would have occurred had the deferred compensation been includible in gross income for the taxable year in which first deferred or, if later, the first taxable year in which such deferred compensation is not subject to a substantial risk of forfeiture.

**(2) Distributions**

**(A) In general**

The requirements of this paragraph are met if the plan provides that compensation deferred under the plan may not be distributed earlier than—

(i) separation from service as determined by the Secretary (except as provided in subparagraph (B)(i)),

(ii) the date the participant becomes disabled (within the meaning of subparagraph (C)),

(iii) death,

(iv) a specified time (or pursuant to a fixed schedule) specified under the plan at the date of the deferral of such compensation,

(v) to the extent provided by the Secretary, a change in the ownership or effective control of the corporation, or in the ownership of a substantial portion of the assets of the corporation, or

(vi) the occurrence of an unforeseeable emergency.

**(B) Special rules**

**(i) Specified employees**

In the case of any specified employee, the requirement of subparagraph (A)(i) is met only if distributions may not be made before the date which is 6 months after the date of separation from service (or, if earlier, the date of death of the employee). For purposes of the preceding sentence, a specified employee is a key employee (as defined in section 416(i) without regard to paragraph (5) thereof) of a corporation any stock in which is publicly traded on an established securities market or otherwise.

**(ii) Unforeseeable emergency**

For purposes of subparagraph (A)(vi)—

**(I) In general**

The term “unforeseeable emergency” means a severe financial hardship to the participant resulting from an illness or accident of the participant, the participant's spouse, or a dependent (as defined in section 152(a)) of the participant, loss of the participant's property due to casualty, or other similar extraordinary and unforeseeable circumstances arising as a result of events beyond the control of the participant.

**(II) Limitation on distributions**

The requirement of subparagraph (A)(vi) is met only if, as determined