**Internal Revenue Service**

Number: **200550007**
Release Date: 12/16/2005
Index Number:  162.36-08

Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:
             , ID No.
Telephone Number:

Refer Reply To:
CC:TEGE:EB:EC
PLR-110720-05
Date:
August 29, 2005

Corporation  =


Year X Plan  =


Year Y Plan  =


Year Z Plan  =


Date A         =


Dear

 This is in response to a letter dated February 18, 2005, submitted by your authorized representative, requesting rulings under sections 162(m) of the Internal Revenue Code.  Specifically, a ruling is requested that the Plan Amendment described below will not constitute a "change in the material terms of the performance goal" nor will it be treated as the grant of a new option.  In addition, you requested a ruling under section 409A.  We cannot rule on this issue because this has been designated as an area in which ruling letters will not be issued until the Service resolves the issue through publication of a Revenue Ruling, Revenue Procedure, Regulations or otherwise.  See section 5.02 of Revenue Procedure 2005-3, 2005-1 I.R.B. 118, 126.  The facts, as represented, are as follow.

 Corporation maintains the Year X Plan, the Year Y Plan and the Year Z Plan under which options to acquire the stock of Corporation have been granted to

employees.  The Year Z Plan was approved by Corporation's shareholders at its annual meeting held on Date A.   When the Year Z Plan became effective, the Year X Plan and the Year Y Plan (collectively the "Prior Plans") were amended to cease any further awards under those plans.  Options will continue to be granted under the Year Z Plan.

Under both the Year Z Plan and the Prior Plans, option holders can use a "Broker Assisted Cashless Exercise Method" to exercise their options.  Under this method, the number of option shares having a fair market value equal to the sum of the option exercise price and the amount of any required tax withholdings are delivered by the Plan to a broker who sells the shares on the market and delivers the sales proceeds to the Plan.

Corporation proposes to amend its Prior Plans to permit a "Net Cashless Exercise Method" (the "Amendment").  Under this method, Corporation will withhold shares having a fair market value equal to the aggregate exercise price as payment of the exercise price plus the amount of any taxes required to be withheld by Corporation in connection with such exercise.  An amount equal to the amount of the broker's commission that would have been charged had the option holder exercised pursuant to the Broker Assisted Cashless Exercise Method will be paid in cash by the option holder to Corporation as part of the exercise.  The Year Z Plan currently permits the Net Cashless Exercise Method.

The Amendment will only apply to nonqualified stock options issued under the Prior Plans that had an exercise price that was not less than the fair market value of the stock covered by such options at the time of the grant ("Outstanding Options").  It will not apply to any incentive stock options issued under the Prior Plans.

Following the adoption of the Amendment, Corporation will not require any options to be exercised by means of the Net Cashless Exercise Method.  Each option holder will have complete discretion as to whether or not to use the Net Cashless Exercise Method.  Corporation will not condition an option holder's eligibility for any awards of benefits upon such option holder's use of the Net Cashless Exercise Method as to any option.

Section 162(a)(1) of the Code allows a deduction for all of the ordinary and necessary business expenses paid or incurred during the taxably year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered.

Section 162(m)(1) provides that for any publicly held corporation, no deduction shall be allowed for applicable employee remuneration with respect to any covered employee to the extent that the amount of such remuneration for the taxable year exceeds $1,000,000.

Section 162(m)(4)(C) excepts from that limit "performance-based compensation" that, in relevant part, is payable solely on account of attaining one or more performance goals determined by a compensation committee of the board of directors, which is comprised solely of two or more "outside directors" and if the material terms under which the remuneration is to be paid are approved by a majority of the shareholders.

Under section 1.162-27(e)(2)(vi) of the regulations, grants of stock options and stock appreciation rights will satisfy the performance-goal requirement in section 1.162-27(e)(2) if (i) the grant or award is made by the compensation committee; (ii) the plan under which the option or right is granted states the maximum number of shares for which options or rights may be granted to any employee during a specific period; and (iii) under the terms of the option or right, the amount of compensation an employee could receive is based solely upon an increase in the value of the stock after the date of the grant or award.

Under section 1.162-27(e)(4)(i), "material terms" include (i) the employees eligible to receive the compensation; (ii) a description of the business criteria on which the performance goal is based; and (iii) either the maximum amount of compensation that could be paid to any employee or the formula used to calculate the amount of compensation to be paid to the employee if the performance goal is attained.

Section 1.162-27(e)(4)(vi) provides that once the material terms of a performance goal are disclosed to and approved by shareholders, no additional disclosure or approval is required unless the compensation committee changes the material terms of the performance goal.  If, however, the compensation committee has authority to change targets under a performance goal after shareholder approval of the goal, material terms of the performance goal must be disclosed and reapproved by shareholders no later than the first shareholder meeting that occurs in the fifth year following the year in which shareholders previously approved the performance goal.

Based on the information submitted, we rule as follows:

(1) The Amendment, as described above, will not constitute a change in the material terms of the performance goal, within the meaning of section 1.162-27(e)(4)(vi) of the regulations with respect to Outstanding Options that otherwise qualify as performance-based compensation under section 162(m).

(2) The Amendment, as described above, will not be considered the grant of a new option for purposes of section 162(m).

Except as specifically ruled on above, no opinion is expressed as to the consequences of the transaction described above under any other provisions of the Code.

This ruling letter is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent. The taxpayer should attach a copy of this ruling to the next federal income tax return it files.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representatives.

Sincerely yours,

_____

ROBERT B. MISNER
Senior Technician Reviewer
Executive Compensation Branch
Office of the Division Counsel/Associate Chief
Counsel (Tax Exempt and Government
Entities)

Enclosure:
    Copy for 6110 purposes