



IRS to resume examining stock-based compensation issues

Global Transfer Pricing Alert 2019-021

The Large Business and International Division (LB&I) of the Internal Revenue Service on July 31 formally withdrew a 2018 directive that provided instructions for tax examiners on transfer pricing issue selection related to stock-based compensation costs (SBCs) in cost sharing arrangements (CSAs). As a result, the IRS will now resume opening issues on examination related to whether SBCs have been included in the pool of CSA intangible development costs (IDCs).

Background

[Directive LB&I-04–0719-008](#), dated July 31 but published August 5, formally withdraws Directive LB&I-04-0118-005, dated January 12, 2018, which instructed IRS examiners to stop opening issues related to SBCs included in CSA IDCs until the US Ninth Circuit Federal Court of Appeals rendered an opinion on the Tax Court's decision in *Altera Corp. v.*

Commissioner, 145 T.C. 91 (2015). On June 7, 2019, a three-judge panel of the Ninth Circuit reversed the Tax Court.^[1] Altera has filed a petition with the Ninth Circuit for a rehearing *en banc*.

The Ninth Circuit's majority opinion upheld as valid the final cost sharing regulations (T.D. 9088), which require taxpayers to include SBCs when determining operating expenses under a qualified CSA.

Overview of CSA SBC directive

When the CSA SBC directive was put in place, SBC issues were to be examined as follows:

- If, at the time the CSA SBC directive was announced, the IRS examination team had already begun developing the SBC issue, and if the taxpayer agreed to extend the statute of limitations until the outcome of the *Altera* appeal was known and for any additional development work thereafter, then the IRS examiner would stop developing the SBC issue.
- If, however, the taxpayer did not agree to extend the statute of limitations, then the IRS examiner was instructed to continue to develop the SBC issue.

Observations

Based on the Ninth Circuit's decision in *Altera*, the commissioner of LB&I has formally withdrawn the CSA SBC directive. The withdrawal is effective July 31, 2019.

Now that the CSA SBC directive has been formally withdrawn, examinations of SBC issues will begin anew with respect to qualified CSAs under Treas. Reg. §1.482-7 and Treas. Reg. §1.482-7A.

^[1] *Altera Corp. & Subsidiaries v. Comm'r*, 926 F.3d 1061 (9th Cir. 2019). For the Deloitte alert discussing the Ninth Circuit's opinion, please see [Global Transfer Pricing Alert 2019-019](#).

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