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Taxpayers No Longer Need to Attach Copy of Section 83(b) Election to Form 1040

Summary

The IRS finalized regulations on July 25, 2016, adopting the 2015 proposed regulations, without change, that eliminate the requirement to file a copy of an 83(b) election with an individual's income tax return for the year. An 83(b) election allows the taxpayer to report as income when nonvested property is transferred in connection with the performance of services rather than when the property becomes substantially vested as provided under Section 83(a).

There are both pros and cons to making an 83(b) election that should be discussed with your tax advisor prior to making such an election.

The final regulations apply to property transferred on or after January 1, 2016. For transfers of property on or after January 1, 2015, and before January 1, 2016, taxpayers may rely on the guidance in the proposed regulations, which is identical to the guidance contained in the final regulations.

Details

When property is transferred to a taxpayer in connection with the performance of services, Section 83(a) generally requires inclusion of the excess of the fair market value of the property over the amount paid for the property in the year in which the taxpayer's rights in the property are transferable or are not subject to a substantial risk of forfeiture.

Under Section 83(c)(1) and regulations thereunder, a substantial risk of forfeiture exists if the full enjoyment of the property is conditioned on the future performance of substantial services or the occurrence of a condition that provides a substantial possibility of forfeiture. Property often increases in value between the transfer date and the time when there is no longer a substantial risk of forfeiture, resulting in an increased amount taxed as ordinary income.

As an alternative to delaying the taxation until there is no longer a substantial risk of forfeiture, Section 83(b)(1) allows the person who performs services in connection

with which property is transferred to elect inclusion of the excess fair market value of the property over the amount paid for it in gross income for the tax year of the transfer.

Prior to these new regulations, an 83(b) election was made by filing a written statement within 30 days of the transfer date with the IRS office with which the taxpayer's return would be filed (a copy was also furnished to the service recipient). An additional copy of the statement had to be submitted with the taxpayer's income tax return for the year of transfer. The requirement to attach a copy of the 83(b) election with the taxpayer's income tax year proved to be an impediment to IRS's preferred electronic filing. The final regulations eliminate the requirement to attach a copy to the taxpayer's income tax return. Generally, a copy of any Section 83(b) election must be kept until the period of limitations expires (generally, three years from the due date of the return) for the return that reports the sale or other disposition of the property.

Insights

Taxpayers are not relieved of their general recordkeeping responsibilities under Section 6001 and accordingly must keep sufficient records to support the original cost of the property and the tax treatment as reported on their income tax returns.