

THE LAW OF EQUITY COMPENSATION

A Guide to Recent Litigation and Administrative Rulings 2001–2005

ALISA J. BAKER AND COREY ROSEN

The National Center for Employee Ownership (NCEO)
Oakland, California

This publication is designed to provide accurate and authoritative information in regard to the subject matter covered. It is sold with the understanding that the publisher is not engaged in rendering legal, accounting, or other professional service. If legal advice or other expert assistance is required, the services of a competent professional person should be sought.

Legal, accounting, and other rules affecting business often change. Before making decisions based on the information you find here or in any publication from any publisher, you should ascertain what changes might have occurred and what changes might be forthcoming. The NCEO's Web site (including the members-only area) and newsletter for members provide regular updates on these changes. If you have any questions or concerns about a particular issue, check with your professional advisor or, if you are an NCEO member, call or email us.

The Law of Equity Compensation

Alisa J. Baker and Corey Rosen

Editing and book design by Scott S. Rodrick

Copyright © 2006 by The National Center for Employee Ownership. All rights reserved. Printed in the United States of America. No part of this book may be reproduced or transmitted in any form or by any means, electronic or mechanical, including photocopying, recording, or by any information storage and retrieval system, without prior written permission from the publisher.

The National Center for Employee Ownership

1736 Franklin Street, 8th Floor

Oakland, CA 94612

(510) 208-1300

(510) 272-9510 (fax)

Web site: <http://www.nceo.org/>

ISBN: 1-932924-24-8

Summary Table of Contents

Prefacexv

Introduction xvii

Part I: Litigation Review

1. General Contract Interpretation and Implementation Issues.....	3
1. Waiver, Oral Modification, and Related Claims.....	5
2. Inconsistent Documents and Ambiguous Language.....	9
3. Ignorance Is Not Bliss.....	13
4. Miscellaneous Contract Issues	15
2. Equity Issues Related to Employment Disputes	19
1. Recent Cases on the Effects of Termination	20
2. Options as Wages.....	22
3. Noncompete Agreements and Stock Option Forfeitures	25
4. Calculating Damages When the Breach of an Equity Agreement Is Related to Termination	29
3. Treatment of Equity in Corporate Transactions	33
1. Change-in-Control Date Issues.....	34
2. Exercise After Spin-Off or Divestiture	36
4. Choice of Law Issues.....	39
1. Disputes Implicating International Issues.....	40
2. Federal/State Preemption Issues.....	41
3. Stock Options in Bankruptcy Claims.....	44
4. Miscellaneous.....	46
5. Allocation of Equity Rights Under Family Law	47
Arizona	49
Arkansas	50

California.....	50
Connecticut	51
Florida.....	52
Maryland.....	53
Massachusetts.....	53
Minnesota.....	53
Missouri	54
New Hampshire	55
New Jersey	55
North Carolina	56
Ohio	57
Pennsylvania.....	57
Washington	58
6. Tax Litigation Arising from Equity Compensation Issues	61
1. U.S. Tax Court Rulings	62
2. State Tax Law Issues	65

Part II: Recent Administrative Rulings and Regulations

7. IRS Rulings on Equity Compensation.....	71
1. Corporate Matters.....	72
2. Individual Matters.....	75
3. Stock Plan Administration	79
4. Section 423 ESPPs	81
5. Tax Shelters	84
8. Final and Proposed Tax Regulations	87
1. Section 409A Deferred Compensation Rules.....	88
2. Final Regulations for Statutory Stock Options	97
9. Securities Law Legislation and Rulings	105
1. The Sarbanes-Oxley Act of 2002.....	106
2. SEC Rulings and No-Action Letters.....	114

Part III: Table of Cases

Table of Cases..... 135

About the Authors 141

About Levine & Baker LLP..... 143

About the NCEO 145

(Full table of contents follows on next page)