

Final Section 409A Deferred Compensation Regulations



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In April, the IRS issued final regulations under Section 409A of the Internal Revenue Code. These regulations cover the scope of Section 409A – which continues to be quite broad – the available exemptions, and the rules on deferral elections and permitted distributions. The regulations also clarify what must be contained in a “non-qualified deferred compensation plan” in order for the plan to comply with the statute.

As expected, the regulations set December 31, 2007 as the end of the transition period. This means plans, contracts and other arrangements that are subject to Section 409A must be in writing, and those written documents must comply with the statute, by December 31. It also means that December 31 is the deadline for making new distribution elections. Failure to complete these steps by the end of the year could result in automatic statutory violations, which carry stiff penalties.

ACTIONS TO TAKE NOW

Given these deadlines, we recommend that you take the following steps as soon as possible:

1. **Identify Plans and Agreements** - If you’ve not already done so, carefully inventory all compensation arrangements, including those contained in individual employment, severance and change-in-control agreements, equity-based compensation plans, and bonus or long-term incentive plans, to ascertain which ones provide for the deferral or delay of compensation in any form and discuss with counsel which such arrangements are or may be “non-qualified deferred compensation plans” under Section 409A. Remember to canvass compensation arrangements for non-employee directors, too.

2. **Discuss Issues with Counsel** - Once you have identified the arrangements that are potentially affected by Section 409A, discuss with counsel:

- what changes, if any, must be made to the documentation of these arrangements to render them compliant with, or exempt from, Section 409A; and
- whether new distribution elections must be made.

3. **Prepare Revised Documents** - Prepare the necessary amendments, distribution election forms and employee communications.

4. **Approve Revised Documents** - Have the amendments approved by all necessary company action (which may include action by your board of directors or a committee of the board).

5. **Review Service Provider Agreements** - Review applicable service provider arrangements to make sure your plans will be operated in compliance with Section 409A. For example:

- 2007 W-2s (and 1099s, for non-employee directors) must report amounts deferred under non-qualified deferred compensation plans. Will you be responsible for generating this information, or will your service provider?
- Rabbi trust documents should be reviewed.

In addition, if your company is public, you will need to consider whether your plan amendments trigger Form 8-K, 10-Q or 10-K reporting obligations.

Please let us know if we can assist you in taking these steps.

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