

CLIENT ALERT

April 24, 2007

Final regulations have been issued under Section 409A.

The deadline for compliance amendments remains December 31, 2007.

On April 10, 2007, final regulations under Section 409A of the Internal Revenue Code were issued.¹ **Taxpayers have until December 31, 2007, to make any necessary amendments to covered nonqualified deferred compensation plans or arrangements (discussed below) to comply with the requirements of the final regulations. The IRS has stated that this deadline will not be extended.**

Background.

In 2004, Section 409A was added to the Internal Revenue Code. Section 409A generally provides that all covered elective and nonelective nonqualified deferred compensation arrangements must comply in form and operation with specific rules regarding the method and timing of elections and payments. Section 409A generally provides that failure to comply with these rules will result in imposition of federal income tax and an additional 20% income tax on vested compensation provided under the noncompliant arrangement and any other compliant arrangements that are required to be aggregated with the noncompliant arrangement, plus interest at the underpayment rate plus one percentage point.

Covered Nonqualified Deferred Compensation Arrangements.

Covered nonqualified deferred compensation arrangements generally include any type of nonexempt arrangement that provides a legally enforceable right (whether or not vested) in a taxable year to receive compensation in a subsequent taxable year. Arrangements that are exempted from application of Section 409A and the final regulations include, among others, tax-qualified plans (e.g., 401(k) plans, pension plans, etc.), tax-qualified group annuity plans, Section 403(b) tax-sheltered annuities, simplified employee pensions (SEPs) and SIMPLE plans, eligible Section 457(b) plans of governmental or tax-exempt employers, certain foreign plans,

¹ In addition, at the same time that the final regulations under Section 409A were released, Notice 2007-34 was issued. The notice addresses how the final regulations impact split-dollar life insurance arrangements.

and certain welfare plans (including, among others, vacation leave, sick leave, compensatory time, disability pay, or death benefit plans).

Nonqualified deferred compensation arrangements that generally are covered by Section 409A include, among others, the following types of arrangements.

- Options (*e.g.*, nonstatutory stock options and unit options, but excluding ISOs)
- Equity appreciation rights (*e.g.*, SARs and UARs)
- Phantom equity plans (*e.g.*, phantom stock and phantom units plans)
- Restricted stock units
- Employment agreements with deferral features, severance features (including, among others, change-in-control features and/or termination for “good reason” definitions) and tax gross-up payments (*e.g.*, Section 280G gross-ups)
- Change-in-control agreements
- Certain annual or long-term bonus programs or arrangements
- Compensation deferral agreements, contracts, plans or other arrangements
- Supplemental executive retirement plans (SERPs) including “top-up” plans
- Excess benefit plans
- Severance pay plans

Action Items.

As a result of the issuance of the final regulations, employers should identify and amend all nonexempt nonqualified deferred compensation arrangements as necessary to comply with the requirements of applicable provisions of the final regulations before January 1, 2008.

For More Information or Assistance.

If you have questions or desire assistance regarding the matters addressed in this alert, please contact your usual contact attorney or any of the following members of our Employee Benefits & Executive Compensation practice:

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