



EMPLOYEE BENEFITS CLIENT ALERT

September 11, 2007

IRS EXTENDS DEADLINE FOR WRITTEN COMPLIANCE WITH FINAL NONQUALIFIED DEFERRED COMPENSATION REGULATIONS AND PROVIDES FURTHER GUIDANCE UNDER CODE SECTION 409A

Introduction

In April of this year, the Internal Revenue Service (the “IRS”) published long awaited final regulations under Section 409A of the Internal Revenue Code (“Code”), providing guidance with respect to nonqualified deferred compensation arrangements. Pursuant to the final regulations, all nonqualified deferred compensation arrangements were required to be in writing and in full compliance with Code Section 409A after December 31, 2007. Yesterday, the IRS issued Notice 2007-78, which generally extends the deadline for documentary compliance with Code Section 409A and which provides additional guidance on select issues.

Compliance Extension

In Notice 2007-78, the IRS extended to December 31, 2008 the deadline to adopt written plan documents that comply with Code Section 409A. As discussed below, however, a few provisions must still be in writing before December 31, 2007. In all cases, plan sponsors must operate their nonqualified deferred compensation arrangements in compliance with Code Section 409A and the final regulations during 2008.

Despite the general compliance extension, if an arrangement has permitted deferrals of compensation as of January 1, 2008 that have not been distributed as of that date, the plan sponsor must specify in writing the time and form of payment for the deferrals on or before December 31, 2007. The time and form of payment for deferrals from January 1, 2008 through December 31, 2008 must be specified in writing before January 1, 2009. Consequently, plan sponsors of arrangements which have not been memorialized or which have complied with the time and form of payment rules of Code Section 409A in operation only **must still take action**



Atlanta • Chicago • Denver • Des Moines • Fayetteville • Irvine
Kansas City • Little Rock • Los Angeles • Oklahoma City • Omaha
Richmond • Scottsdale • Washington, D.C. • Wichita

before year-end. As a result of the operational compliance requirement and the limited relief applicable to the time and form of payments, some plan sponsors should not delay updating their plan documents.

Additional Guidance Under Code Section 409A

In addition to providing a limited compliance delay, Notice 2007-78 addresses select issues under Code Section 409A, some of which may require action before year-end, including limited changes to severance benefits on account of terminations for good reason, provisions for the accelerated cashout of installment or annuity payments and explanation of a limited voluntary correction program for nonqualified deferred compensation plan operation errors. We highlight this guidance below.

Severance for Good Reason Terminations

The final regulations under Code Section 409A provide that a severance payment is subject to a substantial risk of forfeiture if it is payable upon a termination for good reason. This provision may make the severance payment eligible for an exception to Code Section 409A. Under Notice 2007-78, plan sponsors may modify their good reason provisions in accordance with the final regulations without violating certain other provisions of the guidance, but these modifications are generally required by December 31, 2007. Any plan sponsors with arrangements that pay severance for a voluntary termination, including a termination for good reason, are encouraged to review their arrangements for compliance with Code Section 409A prior to year-end.

Cashout of Installment or Annuity Payments

Notice 2007-78 also provides for a new rule relating to the cashout of installment or annuity payments. Under the final regulations, if the value of installment or annuity payments falls below a predetermined threshold, the plan may cash out the remaining benefits in a lump sum payment. This right, however, only applies after payments have begun. Notice 2007-78 explains that an installment or annuity payment schedule may include a feature permitting cashout of the total benefit on the original payment date. This cashout is permitted only if the present value of the total benefit as of the original payment date is below a predetermined threshold. The threshold must be established at the time the permissible payment event is designated and the provision must be operated in an objective, nondiscretionary manner.

Voluntary Compliance Program for Operational Errors

Finally, the IRS indicated that it is in the process of designing a voluntary compliance program for nonqualified deferred compensation arrangements. The IRS anticipates that its program will provide methods for plan sponsors to correct unintentional operational failures



occurring during the year of correction to avoid the application of Code Section 409A. The IRS may provide other methods by which unintentional operational failures result in only limited exposure to the consequences of violating Code Section 409A, including limited income inclusion and tax penalties.

Action Items

Plan sponsors of nonqualified deferred compensation arrangements or any compensation program should carefully review such arrangements and programs to determine whether Code Section 409A applies to them. If Code Section 409A applies, plan sponsors should review and implement any required design changes and consider any other discretionary changes. For the most part, nonqualified deferred compensation plans must reflect the changes required by Code Section 409A no later than December 31, 2008. However, certain provisions must be in place before year-end and plans currently must operate in good-faith compliance with Code Section 409A. Therefore, we recommend that plan sponsors begin reviewing their plans, agreements, policies and administrative practices as soon as possible.

If you have any questions regarding your nonqualified deferred compensation arrangements or benefits programs please contact your Kutak Rock attorney or a member of our Employee Benefits Practice Group, listed below. For more information on our Employee Benefits practice and for recent Employee Benefits news and alerts, please visit us at www.kutakrock.com.

John E. Schembari	402-346-6000	john.schembari@kutakrock.com
Peter C. Langdon	402-346-6000	peter.langdon@kutakrock.com
Kathryn M. Magli	402-346-6000	kathryn.magli@kutakrock.com
Janis J. Winterhof	402-346-6000	janis.winterhof@kutakrock.com
Juliana Reno	402-346-6000	juliana.reno@kutakrock.com

©Kutak Rock LLP 2007
All Rights Reserved

This communication may be considered advertising in some jurisdictions.

