



## 409A Remediation Now Available

by Jeffrey D. Snavelly

While the 409A regulations, and the requirement to operate nonqualified deferred compensation plans in compliance with those regulations, were effective some time ago, the deadlines to amend nonqualified deferred compensation plans to comply, in form, with those rules took effect just a little over a year ago. Many employers were aware of the requirements and consequences of failure to comply with the regulations, but many more were not, and in an effort to encourage employers to comply with those regulations, the IRS has recently issued procedures by which employers may amend their plans to comply with those regulations and avoid some or all of the consequences of their failure to comply.

### Background

In the wake of the financial scandals earlier in the decade, the IRS set its sights on curbing abuses in the use of nonqualified deferred compensation plans. Nonqualified deferred compensation plans are very broadly defined to include any arrangement (other than qualified employer plans such as a 401(k)) whereby the employee obtains the legally binding right to receive compensation in a later taxable year. This could include not only traditional deferred compensation agreements but also employment agreements that provide for deferred bonuses or salary continuation, covenants not to compete, and even, in certain cases, share redemption arrangements. The 409A regulations, adopted in 2004, greatly restricted both an employer's and an employee's ability to make changes in the time (death, termination of service, fixed date, etc.) and form (lump sum, installments, etc.) of payments under these nonqualified deferred compensation plans.

### Offices

#### Toledo Office:

One Seagate, 24th Floor  
P.O. Box 10032  
Toledo, Ohio 43699-0032  
Telephone: 419-241-6000  
Fax: 419-247-1777

#### Columbus Office:

100 E. Broad Street, Suite 600  
Columbus, Ohio 43215  
Telephone: 614-564-1445  
Fax: 614-280-1777

#### Findlay Office:

725 S. Main Street  
Findlay, Ohio 45840  
Telephone: 419-424-5847  
Fax: 419-424-9860

#### Novi Office:

28175 Haggerty Road  
Novi, Michigan 48377  
Telephone: 248-994-7757  
Fax: 248-994-7758

[www.eastmansmith.com](http://www.eastmansmith.com)

Under the 409A regulations, employers were required to operate their plans in compliance with the regulations beginning in 2005 and were required to amend their plans to conform to the regulations no later than December 31, 2008. Not surprisingly, many employers did not comply with these operational and documentary deadlines, but this notice will, in many instances, give employers another opportunity to comply.

### Available Remediation

In order to assist employers and employees who inadvertently failed to comply with the 409A regulations, the IRS has recently released Notice 2010-6, which allows employers, under certain circumstances, to correct both documentary failures and to reduce or eliminate taxes that would otherwise be required because of the failure. The remediation is not available for all failures, but rather only for those failures specifically referenced in the notices.

Specifically, the notice, among other things, allows the correction of:

- certain commonly used language in nonqualified plans that does not otherwise comport with the Regulations will be deemed compliant (e.g., as soon as practicable);
- ambiguous payment events;
- impermissible definitions of otherwise permissible payment events (e.g., separation of service, change of control and disability);
- impermissible payment periods (e.g., payment periods allowing a payment later than 90 days after a payment event);
- impermissible payment schedules (e.g., a payment schedule to be determined at a later date);
- impermissible deferral elections; and
- impermissible reimbursement of certain expenses.

In most instances, the employer can make these corrections and avoid or significantly reduce the negative tax consequences attendant to a 409A failure, and those consequences are significant. Noncompliance can result in the current recognition of income tax on all amounts deferred, a 20% tax on the amount otherwise included in income, and additional penalties.

### Opportunities for the Employer

This gives employers who have not previously done so the perfect opportunity to:

- take inventory of all plans, agreements and arrangements that fall within the purview of 409A;
- review both the operation and underlying documents of those 409A plans to ensure compliance; and
- to the extent that there have been failures, to make use of the remediation programs currently available.



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*Mr. Snavelly, a member in the Business Section of Eastman & Smith, concentrates his practice in the areas of commercial transactions and general corporate law. To contact Mr. Snavelly, please call our Toledo office (419-241-6000).*

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