

Triangle Benefits Forum
§ 409A Basics
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History of Code § 409A

1978 – Congress tells IRS to back off from proposed regulation of nonqualified deferred compensation

2001-2002 – ENRON

2002-2004 – Congressional hearings on ENRON and other disclosure about executive compensation.*

- Haircuts
- Foreign trusts
- Rolling payment dates
- Triggers
- Discretionary acceleration

2004 – Code § 409A enacted, effective 2005

2005 to present – Volumes of IRS guidance, with the latest being

- Final Regulations – April 2007
- Notice 2007-78 – September 2007

* *Captain Renault: I'm shocked, shocked to find that gambling is going on here!*

Croupier: Your winnings, sir.

Captain Renault: Oh, thank you very much... Everybody out at once!

—*Casablanca*

This outline is intended to provide information about new ideas and developments, and is not to be considered specific legal advice, as each client's situation is unique. If you have need for legal advice, please seek advice from a lawyer. Wyrick Robbins Yates & Ponton LLP is always glad to discuss with our clients their specific employee benefits and compensation needs.

§ 409A Basics

1. “Nonqualified Deferred Compensation” Defined

“Compensation”

- Payment for services to an employee, directors, consultants and other independent contractors
- Cash, property, benefits

“Nonqualified”

- Doesn't apply to qualified plans, § 403(b) arrangements, 457(b) and (f) [but earnings may be regulated], § 83 property transfers, incentive stock options
- Other exceptions: traditional severance plans that meet certain requirements; stock options where the exercise price is not less the FMV when the options were granted; short term deferrals

“Deferred”

- Must be earned in one year and paid in another
- Not deferred compensation if paid in year in which earned or vested (if later) or a short term deferral
 - Short term deferral if paid by March 15 of calendar year following the calendar year in which earned or, if later, when vested
 - Vesting concepts – eliminates rolling vesting, and noncompetes.

2. § 409A requirements

- Election to defer compensation must be made in the year before it is earned. The election must designate a time for payment that is objectively determined and cannot be controlled by the service provider (exception separation from service) or employer. Election must be irrevocable once the year in which the compensation is earned begins.
- No triggers. Payment allowed only upon 6 events: separation from service, fixed calendar date, change of control, disability, death, unforeseeable emergency.
- Payment may not be accelerated, with some technical exceptions.
- Payment may not be delayed, with some technical exceptions, including the 12 month/5 year rule.
- Agreement must be in writing and must include § 409A basics.
- No foreign trusts.
- 6 month delay of payments on account of separation from service to specified employees of publicly traded companies

3. 409A penalties

- Service provider (employee, etc.) is taxed immediately when either: the form of the arrangement does not meet 409A, or the operation of the arrangement does not meet 409A
- Plus, 20% penalty
- Plus, interest
- Employer has withholding and reporting obligations

What Happens Next

- See September 2007 Wyrick Robbins Yates & Ponton LLP *Employee Benefits Alert* at www.wyrick.com .

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