

January 12, 2010

409A Relief for Nonqualified Deferred Compensation Plan Document Failures

On January 5, 2010, the Internal Revenue Service (“IRS”) issued Notice 2010-6 (“Notice”), which provides a correction method for certain inadvertent and unintentional document failures under Code Section 409A (“Section 409A”) and Income Tax Regulation Section 1.409A-1(c). In some cases, if these failures are corrected, the amount of includible income may be limited and the amount of additional taxes under Code Section 409A may be reduced or eliminated if certain requirements are met. The intent of the correction program is to encourage taxpayers to review nonqualified deferred compensation plans and identify and correct any plan document failures, while at the same time not providing taxpayers who initially complied with less of an advantage than those who did not.

The Notice provides the following:

- Clarification that certain language commonly included in plan documents (for example, inconsistently defined terms, impermissible payment dates or events, etc.) will not cause a document failure;
- Relief permitting correction of certain document failures without current income inclusion or additional taxes under Section 409A, provided, in certain circumstances, that the corrected plan provision does not affect the operation of the plan within one year following the date of correction;
- Relief limiting the amount currently includible in income and the additional taxes under Section 409A for certain document failures if correction of the failure affects the operation of the plan within one year following the date of correction;
- Relief permitting correction of certain document failures without current income inclusion or additional taxes under Section 409A, if the plan is the service recipient’s first plan of that type (disregarding any plans not subject to Section 409A or any plans under which all deferred amounts have previously been paid or forfeited) and the failure is corrected within a limited period following adoption of the plan; and
- Transition relief permitting corrections of certain document failures without current income inclusion or additional taxes under Section 409A, if the document failure is corrected by December 31, 2010, and any operational failures resulting from the document failure are also corrected in accordance with Notice 2008-113, 2008-51 IRB 1305, by December 31, 2010.

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The IRS has announced that it plans to conduct audits on up to 6,000 companies over a three-year period beginning in 2010 to determine whether they pay all their required employment taxes. These audits will likely include nonqualified deferred compensation plans, which the IRS has identified as a common area of non-compliance. Because of this, it is vital that companies quickly take advantage of this correction program.

In addition to creating the much-needed correction program for plan document failures, the Notice also made certain clarifications regarding the correction of operational failures. Included in the Notice is clarification of the following:

- The application of subsequent year correction method to late payments of amounts deferred;
- The calculation of the amount that must be paid to the service provider as a correction of a late payment of an amount deferred under a plan if the payment would have been made in property, such as shares of stock; and
- The calculation of the amount that must be repaid by the service provider as a correction of an early payment of an amount deferred under a plan if the early payment was made in property, such as shares of stock.

If you have any questions regarding the new correction program or would like assistance in correcting your plan, please contact Dana Thrasher (205-226-5464), Dave Pearson (813-222-1367), Bob Ellerbrock (205-226-5462), or Jay Turner (205-226-5468).

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