



# NYLEX News

*News and Events in the Executive Benefit Program Marketplace*

## **Section 409A Final Regulations Issued** *Section 409A Alert*

*TO OUR CLIENTS AND FRIENDS*

THIS ISSUE OF NYLEX NEWS DISCUSSES THE FINAL REGULATIONS UNDER SECTION 409A OF THE INTERNAL REVENUE CODE ISSUED APRIL 10, 2007. TAXPAYERS ARE GIVEN UNTIL DECEMBER 31, 2007 TO AMEND PLANS TO CONFORM TO THESE REGULATIONS. PLEASE SEND COMMENTS ABOUT THIS NEWSLETTER, AS WELL AS SUGGESTIONS FOR FUTURE ISSUES, TO OUR STAMFORD, CT OFFICE.

### **Summary**

Section 409A, enacted as part of the American Jobs Creation Act of 2004, provides rules for the income tax treatment of amounts deferred under nonqualified deferred compensation plans. Under the law, amounts accruing under supplemental executive retirement plans (“SERPS”) also are subject to these rules. On April 10, 2007 Treasury and the

Internal Revenue Service issued final regulations under Section 409A.

The final 409A regulations are effective April 17, 2007 (when the regulations will be published in the Federal Register) and do not extend the existing transition period beyond December 31, 2007. Therefore, all plans must operate in accordance with these rules by the end of 2007 and required amendments to plan documents must be made by that date.

### **The Final Regulations**

The regulations generally follow the proposed regulations published in 2005, but do include revisions reflecting numerous comments received from taxpayers and practitioners.

Although the regulations provide useful new rules and guidance, there seem to be few changes that would narrow the scope of Section 409A or make it easier for companies and employees to comply.

Under the regulations, all plans must be in writing, although a plan may be contained in more than one document. Each plan must provide:

1. The amount payable.
2. The schedule or event that determines payment.
3. A six month delay for payments to the specified top executives of public companies.
4. The conditions for making a deferral election.

### **Final 409A Regulations**

Issuance of final regulations under Section 409A signals the end of the transition period that has been in effect since October 2004. Employers have until the end of 2007 to amend their plans to conform to the new requirements.

## **Retirement Plans and 409A**

Although Section 409A also applies to nonqualified supplementary executive retirement plans (“SERPs”), the regulations deal almost entirely with deferral arrangements and there seems to have been little attempt to address how SERPs are affected by these new rules. Therefore, SERP sponsors and their advisors must rely on regulations that seemingly were not written to address SERP issues.

However, the regulations do provide some welcome guidance and relief to SERP participants who wish to change their lifetime retirement benefit to some other actuarially equivalent form in order to meet their own personal financial situation.

### **Stock-based Plans**

The regulations continue the exclusion of statutory stock options from coverage. Thus, incentive stock options (ISOs) and employee stock purchase plans (ESPPs) are not covered by Section 409A.

Also, under the regulations nondiscounted stock options and stock appreciation rights (SARs) on employer stock that do not include any additional deferral features generally are excluded from Section 409A. The stock option or SAR must be with respect to employer stock, but that includes stock of a related company

in a chain of ownership that ends with the employer.

### **Split-dollar Life Insurance Arrangements**

At the same time as the 409A regulations were released, the IRS released Notice 2007-34, which addresses the application of Section 409A to split-dollar life insurance arrangements.

The IRS indicated that:

1. Split-dollar life insurance arrangements that provide only death benefits for the employee are excluded from Section 409A.
2. Collateral assignment split-dollar life insurance arrangements generally also are not covered by Section 409A.
3. Endorsement split-dollar life insurance arrangements, where the benefit is not limited to a death benefit, and where the employer has the obligation to continue premium payments which result in taxable compensation to the employee, generally will be considered deferred compensation arrangements.

Responding to many questions and comments regarding the effect of changes required with respect to split-dollar life insurance arrangements, the Notice provides that modifications required to comply with Section 409A or to avoid the application of that Section, will not be treated as material modifications, so that the benefits of grandfathering

under the split-dollar rules will not be lost.

### **What the Regulations Do Not Address**

The regulations do not include guidance on the calculation and timing of amounts included in income under Section 409A or the reporting and withholding of such amounts. Treasury and the IRS intend to issue such guidance in the future, including “transition guidance as may be appropriate with respect to the reporting and withholding requirements”.

Also, the regulations do not address the application of Section 409A to arrangements between partners and the IRS are continuing to study this area and until further guidance is issued, taxpayers can continue to rely on interim guidance previously issued.

### **Operation and Amendment of Plans**

The final 409A regulations signal the end of the transition period that followed the enactment of Section 409A in October 2004. By the end of 2007 taxpayers and their advisors must conform the operation of nonqualified deferred compensation plans to the new regulations and amend these plans in order to meet these new requirements.

## About NYLEX Benefits

NYL Executive Benefits LLC (“NYLEX Benefits”) provides supplemental executive benefit programs to a wide range of commercial clients. We focus on developing cost effective executive benefit solutions that are designed to attract, reward and retain key employees. Our services are designed to assist clients at all stages in the adoption and operation of executive benefit programs and include:

- Initial assessment
- Plan design
- Funding
- Plan implementation
- Ongoing administration

NYLEX Benefits’ professional staff includes the following professional disciplines, all

dedicated to supporting our client’s programs, processes, systems and services:

- Accountants
- Actuaries
- Attorneys
- Benefit specialists
- Insurance specialists

We take great care to assure that client programs are practical and cost effective and that they are designed to achieve our clients’ strategic and operational goals.

NYLEX Benefits

281 Tresser Boulevard, Suite 1110

Stamford, CT 06901

(203) 353-5800 FAX (203) 353-5844

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

Nothing contained herein is, or should be construed as, legal, tax, or accounting advice, nor was it intended nor can it be used for the purpose of avoiding penalties under the Internal Revenue Code or applicable state or local tax provisions. This communication was written to support the promotion or marketing of the matters or transactions addressed herein, and clients should always consult with their independent professional advisors to seek advice on the applicability of this information to their particular circumstances.