



REID AND RIEGE, P.C.

COUNSELLORS AT LAW

# EMPLOYEE BENEFITS AND EXECUTIVE COMPENSATION ALERT

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**DECEMBER 31, 2012 DEADLINE**

**DEFERRED COMPENSATION PLANS AND AGREEMENTS:  
TIMING CONDITIONED ON EMPLOYEE ACTION**

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October 2012

We alert you to the need to review your deferred compensation plans and agreements to be sure that the terms of each document comply with guidance recently issued by the Internal Revenue Service (IRS). In this new guidance, the IRS is requiring certain nonqualified deferred compensation plans to be amended by December 31, 2012, in order to avoid harsh tax penalties under Section 409A.

## **Section 409A**

Section 409A applies to all amounts deferred under a “nonqualified deferred compensation plan.” A nonqualified deferred compensation plan is defined broadly to mean any arrangement that provides for the deferral of compensation to a later taxable year. An arrangement provides for the deferral of compensation if an individual has a legally binding right during a taxable year to compensation that, pursuant to the terms of the arrangement, is or may be payable to (or on behalf of) the individual in a later taxable year. For further information regarding nonqualified deferred compensation plans, please consult our May 2008 and November 2008 Client Alerts available [here](#).

## **Documents to Be Reviewed Now**

The recent IRS guidance focuses on those severance and other deferred compensation plans and agreements that condition the payment of deferred compensation on the employee’s taking some action – typically, executing a non-competition agreement, a non-solicitation agreement, or a release of claims. These arrangements are most likely found in:

- employment agreements;
- severance plans and separation agreements;
- change-in-control arrangements;
- performance pay arrangements; and
- equity incentive arrangements.

For example, an employee may be entitled to receive severance payments upon termination of employment, but only if the employee executes a release of claims.

The IRS takes the position that such a provision does not comply with the requirements of Section 409A, because the employee could impermissibly control the timing of the distribution and the recognition of income by determining when he or she will execute the release.

## **Necessary Amendment to Address the Issue**

The recent IRS guidance specifies the following alternative methods for addressing this issue, as long as the correction is made by December 31, 2012 (and before the date the permissible payment event under the compensation arrangement occurs):

- A. ***If a document currently specifies a permissible designated period after termination*** in which an employee is required to execute a release or agreement, the document is amended either:
- to specify that the payment will be made on the last day of such period; or
  - to specify that, if the period spans two calendar years, payment cannot be made before the second calendar year, regardless of when the release or agreement is executed.
- B. ***If a document does not currently specify a permissible designated period after termination*** in which an employee is required to execute a release or agreement, but merely requires the employee to execute a release or agreement before receiving payment, the document is amended either:
- to provide that payment will be made on the 60th or 90th day after termination, provided the employee has executed the release or agreement; or
  - to provide for payment during a period (not longer than 90 days) after termination, and after the employee has executed the release or agreement, and to specify that if the period spans two calendar years, payment cannot be made before the second calendar year, regardless of when the release or agreement is executed.

The amendment cannot otherwise change the time or form of payment.

***If you have a concern regarding your document after reading this Alert, please contact us as soon as possible***, so that we have time to review the relevant document for compliance. Any required amendment will need to be executed by December 31, 2012. Therefore, it is crucial to allow time for the necessary communication, review and approval process.

*Note from the Editor* This edition of the Employee Benefits and Executive Compensation Alert highlights the need to review deferred compensation documents and amend the documents, if necessary, for compliance with Code Section 409A guidance by year-end. The Alert was written by Ronald J. Koniuta, a member of the Employee Benefits & Pension Practice Area at Reid and Riege, P.C., One Financial Plaza, Hartford, CT 06103. The Practice Area works closely with clients to design and draft tax-qualified and nonqualified retirement plans, and counsels on compliance with the complex and changing rules governing such plans. For information or additional copies of this Alert, or to be placed on our mailing list, please contact Ron (tel. 860-240-1034)(e-mail [rkoniuta@rrlawpc.com](mailto:rkoniuta@rrlawpc.com)), another member of the Practice Area: John J. Jacobson, Chairman (tel. 860-240-1006) (e-mail [jjacobson@rrlawpc.com](mailto:jjacobson@rrlawpc.com)), John V. Galiette (tel. 860-240-1009) (e-mail [jgaliette@rrlawpc.com](mailto:jgaliette@rrlawpc.com)), Devin M. Karas (tel. 860-240-1063) (e-mail [dkaras@rrlawpc.com](mailto:dkaras@rrlawpc.com)) or Erik M. Sharp (tel. 860-240-1074) (e-mail [esharp@rrlawpc.com](mailto:esharp@rrlawpc.com)), or the Reid and Riege attorney with whom you regularly work. For other information regarding Reid and Riege, P.C., please visit our web site at [www.rrlawpc.com](http://www.rrlawpc.com).

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