



EXECUTIVE COMPENSATION

# ALERT

## DEADLINE APPROACHING FOR CORRECTING CERTAIN SECTION 409A PROBLEMS

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The deadline for amending certain non-conforming employment contracts and severance agreements that are eligible for relief from the adverse consequences of Section 409A of the Internal Revenue Code is December 31, 2012.

For reasons discussed below, many severance arrangements under employment contracts and stand-alone severance agreements risk being held in violation of Section 409A. This has caused quite a bit of consternation among practitioners in the executive compensation area. In response to this pushback from the legal community, a few years ago the Internal Revenue Service issued Notice 2010-80, which provides correction methods that would allow certain nonconforming arrangements to be revised so that the penalties for failure to comply with Section 409A will not be imposed.

The uproar had its genesis in the Section 409A requirement providing that amounts of non-qualified deferred compensation may be paid only upon one or more specified events, such as termination of service, a change in control of the employer, death or disability of the service provider, an unforeseeable emergency or a specific time or fixed schedule. Treasury regulations state that non-qualified deferred compensation programs may provide that payments triggered by one

or more of the events described above (other than payments made at a specific time or pursuant to a fixed schedule) can be made during a specified period rather than on a specific date but only if the payment period (1) both begins and ends during one taxable year of the employee/service provider or (2) lasts no more than 90 days and, if the 90-day period straddles two taxable years, the employee/service provider does not have the right to designate the calendar year of payment.

A non-qualified deferred compensation program will be in violation of Section 409A if the payment date or period is not specified in a sufficiently precise manner. Unfortunately, many employment contracts and severance agreements have not been drafted with the required specificity. Quite often, the arrangements are drafted to merely provide that severance payments will be made once the employee executes a release of claims against the employer, with no time limitation being imposed on when the release must be executed.

Notice 2010-80 provides significant relief for nonconforming agreements that were drafted on or before December 31, 2010. Complete relief is granted for payment triggering events occurring on or before March 31, 2011 and relief is also provided for documentary failures if the payments are triggered on or before December 31, 2012. In either situation, the non-

conforming employment contracts and severance agreements eligible for the relief must be amended to bring them into compliance with the Notice on or before December 31, 2012. To be eligible for relief under Notice 2010-80, the amended arrangements must reflect rules contained in the Notice that set forth when severance payments must be made.

As the corrective measures described under the

Notice are quite detailed, we strongly advise you to consult your legal advisor well before the deadline so that any nonconforming arrangements can be rectified in a timely manner.

For questions on this alert, contact Robert M. Fields at [rfields@foxrothschild.com](mailto:rfields@foxrothschild.com) or 215.905.2315 or any member of Fox Rothschild's Executive Compensation Practice.



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