SECTION 409A TRANSITION RELIEF EXTENDED THROUGH DECEMBER 31, 2008

On October 22, 2007, the IRS issued Notice 2007-86, which extends until December 31, 2008 the deadline by which nonqualified deferred compensation plans must be brought into documentary compliance with the final regulations under Section 409A of the Internal Revenue Code. The notice also extends the availability of important transition relief regarding compliance with Section 409A. Although this extension comes as welcome news, the scope and complexity of the final regulations will continue to present significant compliance issues. To minimize the likelihood of noncompliance, we urge clients to continue reviewing and making necessary amendments to all compensation arrangements that may fall within the scope of Section 409A.

- Applicable Guidance. Prior to January 1, 2008, compliance with the proposed regulations, the final regulations, or Notice 2005-1 will meet the standard of reasonable, good faith compliance required for nonqualified deferred compensation plans. After December 31, 2007, taxpayers may rely only on the final regulations and Notice 2005-1, except that the preamble to the proposed regulations may be relied upon for the application of Section 409A to partners and partnerships (until further guidance is issued).
- Changes in Payment Elections or Conditions. The transition relief provided by Notice 2006-79 has been extended through December 31, 2008. This relief allows nonqualified deferred compensation plans to be amended to provide for new payment elections as to the time or form of payment of previously deferred compensation, subject to certain limitations.
- Payments Linked to Qualified Plans. The notice also extends through December 31, 2008, the existing transition relief that allows payment elections to be linked to elections under a qualified plan.
- Substitution of Discounted Stock Options and Stock Appreciation Rights. The ability to replace discounted stock rights (i.e., options or stock appreciation rights) otherwise subject to Section 409A with non-discounted stock rights has been extended to December 31, 2008, but only to the extent such cancellation and reissuance does not result in an exchange for cash or vested property in the year of cancellation. As with past relief, this transition relief does not apply to discounted stock rights granted by public companies to executive officers if the company has reported or reasonably expects to report a financial expense due to the issuance of the stock right that was not timely reported for the period in which the related expense should have been reported under GAAP.

- Employment Agreements. Certain exemptions from Section 409A require compensation to be subject to a substantial risk of forfeiture, and Notice 2005-1 provides that the addition or extension of a substantial risk of forfeiture after the beginning of the service period to which the compensation relates will be disregarded for purposes of determining whether such exemptions apply. Notice 2007-78, however, granted relief to taxpayers by permitting them to modify on or before December 31, 2007, existing "good reason" definitions in employment agreements to satisfy the final regulations without such modification being treated as an impermissible extension of a substantial risk of forfeiture. Notice 2007-86 has extended this relief through December 31, 2008.

It is virtually certain that Notice 2007-86 is the final extension for bringing nonqualified deferred compensation arrangements into compliance with Section 409A. Given the draconian penalties Section 409A imposes on employees participating in noncompliant arrangements, companies should not neglect or slow current efforts to review and amend plans and agreements. If you have not already asked us for assistance and would like us to review your deferred compensation plans, please call us as soon as possible so that we can schedule the work that will be needed and make sure that we have obtained all of your plans for review.

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If you have any questions concerning the foregoing or would like additional information, please contact Stephen T. Lindo (212-728-8242, slindo@willkie.com), Frank A. Daniele (212-728-8216, fdaniele@willkie.com), David E. Rubinsky (212-728-8635, drubinsky@willkie.com), or the partner with whom you regularly work.

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IRS Circular 230 disclosure:

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