

November 12, 2004

**CHECKLIST FOR AMENDING VOLUNTARY DEFERRAL/401(K) MIRROR PLANS
TO COMPLY WITH NEW CODE SECTION 409A^{*/}**

Item	Plan Provisions	New Law Applies to Amounts Deferred after 12/31/04	Required and Optional Changes
Grandfathered Amount	N/A	The new law applies to any amounts not earned and vested as of December 31, 2004. Amounts earned and vested before January 1, 2005 are grandfathered, unless the plan is "materially modified" after October 3, 2004. A material modification includes the addition of an any benefit, right, or feature ("BRF"), such as adding a haircut provision or accelerating vesting. It does not include the exercise or reduction of an existing BRF, such as removing a haircut provision, changing the plan administrator, or freezing the plan as of December 31, 2004.	Determine grandfathered amount based on vested December 31, 2004 account balance (plus earnings thereon).
Initial deferral election	Most plans provide for initial elections to defer salary to be made by 12/31 of the prior year. However, bonus deferrals are	In general, initial participant elections to defer compensation must be made before the beginning of the taxable year in which the services are performed giving rise to the	A bonus election must either (1) be made prior to the year the bonus is earned, or (2) if the bonus is performance-based, comply with the

^{*/} Enacted by The American Jobs Creation Action of 2004 (Pub. L. No. 108-357, Oct. 22, 2004).

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	<p>sometimes delayed until well into the bonus period.</p> <p>"Mirror 401(k)" plans may, in practice, not require separate deferral elections and may implement participant changes in 401(k) deferral elections at the time they are made under the 401(k) plan.</p>	<p>compensation. However, for "performance-based compensation" earned over a period of at least 12 months, the initial election to defer may be made as late as six months prior to the end of such period. IRS guidance is pending on what is "performance-based compensation" and for fiscal-year bonus plans.</p> <p>Newly eligible participants have a 30-day election period.</p> <p>There are no special rules for mirror 401(k) plans.</p>	<p>6-month rule.</p> <p>Note: The 2004 bonuses and long-term bonuses with outstanding performance periods are subject to the new rule if not vested by 12/31/04. Because it is too late to comply in these cases, we anticipate IRS transition relief. Treasury has indicated, however, that elections for bonuses payable in 2005 should be made in 2004, even if non-compliant with the new rules.</p> <p>Separate deferral elections will be required for mirror 401(k) plans.</p>
Time and form of in-service distributions	<p>Most plans permit in-service distributions in the event of financial emergency or hardship.</p> <p>Plans also may permit an in-service distribution at any time for any reason, subject to a penalty – called a "haircut" (e.g., 10% of the benefit is forfeited).</p>	<p>Haircut provisions are not permitted. The time and form of distribution may be specified by the participant (or set forth in the plan) at the time of deferral. Distributions may occur upon a specified time or pursuant to a fixed schedule. Deferred amounts may also be distributed in-service in the event of an unforeseeable emergency, under standards similar to the "unforeseeable emergency" requirements under Code section 457.</p>	<p>A 401(k)-type hardship withdrawal provision must either be eliminated or modified to comply with the stricter unforeseeable emergency standards.</p> <p>General in-service withdrawal provisions (e.g., with a haircut) must be eliminated.</p>

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Investments	Some plans provide for a choice among designated investment options, including employer stock; others provide a fixed interest rate.	Investment provisions are generally not affected by the new law (other than possibly for "excessive" earnings rates resulting in new deferrals). However, any changes to the investment provisions after Oct. 3, 2004 may trigger a "material modification," resulting in the new rules applying to pre-2005 deferrals.	Revision of the investment provisions of the plan for pre-2005 deferrals could result in a material modification subjecting such deferrals to the new law.
Time and form of post-termination distributions	<p>Most deferred compensation plans provide for an employee election of the payment form and timing, and if no election, a default provision (e.g., lump sum or installments paid at termination of employment).</p> <p>Mirror 401(k) plans may simply tie form and time of termination distribution to the method of payment under the 401(k) plan.</p> <p>Death benefits are also an issue if the participant or beneficiary has a choice as to the form and timing of payment.</p>	<p>The time and form of distribution must be specified in the plan document or by the participant at the time of deferral. Distributions are limited to separation from service (from entire controlled group), disability, death, specified time or fixed schedule in the plan or at the time of deferral, a change in control, or an unforeseeable financial emergency.</p> <p>Generally, cannot tie timing/form to payment election under 401(k) plan.</p>	<p>Either:</p> <ol style="list-style-type: none"> 1. Require separate participant elections at time of deferral. (Newly eligible participants can have a 30-day election period.) 2. Designate the payment form and timing in the plan document.
Subsequent deferral elections	A plan that ties payments to the form and time elected under the 401(k) plan, or that permits changes to plan-designated (or	Any change in the form or date of payment that would result in an acceleration of payments is prohibited. The following plan provisions are prohibited:	Subsequent elections must comply with the new law.

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	<p>employee-elected) benefit form or payment date is providing a subsequent deferral election. For example, many plans permit an employee to elect or change the form of payment 12 months prior to retirement.</p>	<ul style="list-style-type: none"> • haircut provision, • change from installments to lump sum, • acceleration of payments on plan termination (e.g., lump sum distributions on plan termination), or • committee or company discretion to establish or override a distribution form. <p>It is expected that IRS rules will permit acceleration for (1) automatic cashout of less than \$10,000, (2) court-approved divorce settlements, (3) withholding of employment taxes, and (4) choices among life annuity choices.</p> <p>A subsequent election to delay the timing or change the form of payment must generally (1) not take effect until at least 12 months after the date of the election, (2) provide an additional deferral for a period of at least 5 years from the date payment would have otherwise been made, and (3) if related to a payment at a specified time or pursuant to a fixed schedule, be made at least 12 months prior to the date of the first scheduled payment.</p>	

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Change of Control Provision	Many plans provide for accelerated payout upon a change of control.	Accelerated payout is permitted in the event of a change in control under future IRS guidance.	Conform to future guidance.
Disability Provision	Many plans provide for distribution in the event of a disability.	Distribution in the event of a disability is permitted; however, the new rules provide a specific definition of disability – (1) disabled under the Social Security definition, or (2) participant is receiving income replacement benefits for at least 3 months under an employer's accident or health plan by reason of medically determined physical or mental impairment which is expected to result in death or last for at least 12 months.	Conform plan definition of disability to new law.
Vesting	Employees are typically fully vested in their deferrals of salary and bonus. Employer contributions (e.g., matching contributions under mirror 401(k) plans) may be subject to a vesting schedule.	Unvested deferrals (and earnings) at 12/31/04 will be subject to the new rules.	N/A
Special Rule for "Key Employees" of Public Companies	Plans do not have distribution restrictions on key employees.	Separation from service distributions to key employees (as defined in the top-heavy pension rules under Code § 416(i)) of public companies cannot commence until 6 months after the separation date (or, if earlier, the date of death of the employee).	Identify "key employees" or impose a blanket 6-month wait for all participants (or a group of more than 50 possible "officers") to simplify administration.

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Plan amendments	Nearly all plan documents have provisions on amending or terminating the plan.	Operational compliance is required as of January 1, 2005, but plan amendment language will not be required until the end of the amendment period to be provided by IRS (likely sometime in 2005). Treasury has 60 days after enactment to provide transition guidance.	Review the plan amendment provisions, as well as approval/filing procedures (in-house, SEC, etc.) for amending a plan or establishing a new plan. Either amend the plan or freeze it and create a new plan (when required).
Reporting and Withholding	No W-2/1099-MISC reporting or wage withholding generally until paid. However, FICA is generally paid when the amount is vested and reasonably ascertainable.	Accruals must be reported on Form W-2 when earned and distributions must be reported on Form W-2 (and subject to wage withholding) when includable in income. For non-employees, accruals must be reported on Form 1099-MISC when earned and distributions must be reported on Form 1099-MISC when includable in income. IRS reporting guidance pending.	Establish procedures to comply with new reporting requirements.
Penalties for Failure to Comply	N/A	Failure to comply with the new rules results in all post-2004 deferrals subject to current taxation, plus (1) interest (IRS underpayment rate plus 1%) from the later of the date of deferral or vesting, (2) 20% of the taxable amount. The penalty is imposed on an individual basis; however, a plan document failure could adversely affect all participants covered by the prohibited provision.	

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