

April 12, 2007

Action Steps on Final Section 409A Regulations

On April 10th, the IRS issued long-awaited final regulations under Code section 409A. The regulations primarily finalize rules contained in the October 2005 proposed regulations on the scope of section 409A, as well as the rules for deferral elections and distributions under plans subject to section 409A. As expected, the regulations do not extend the transition relief for section 409A compliance. ***Thus, full documentary and operational compliance is required as of December 31, 2007.*** We describe below steps that employers will need to take by the end of 2007 to ensure compliance with section 409A.

1. Identify Potentially Affected Plans and Arrangements – In addition to typical nonqualified retirement plans like elective deferral and SERP plans, section 409A may apply to:

- options, restricted stock units, and other equity compensation awards
- severance arrangements
- post-retirement reimbursements/in-kind benefits
- annual bonus plans
- long-term incentive plans

2. Examine Plans for Directors Too - Arrangements of the types described above covering non-employee directors and other independent contractors also should be analyzed, as the reach of section 409A is not limited to plans for employees.

3. Determine Which Plans May Fit in Exemptions – The final regulations provide several exemptions that could remove the items listed above from section 409A coverage. Employers should determine which of their arrangements already fit within these exemptions and which could fit with limited modifications. The exemptions for short-term deferrals, severance arrangements, and equity compensation awards should be particularly useful. For example, certain discounted options can still be revised in 2007 and made exempt from section 409A.

4. Determine Changes Required for Covered Plans – An employer will need to determine the changes to deferral election and distribution rules that the regulations require for its nonqualified retirement and other plans that are covered by section 409A.

5. Preserve Grandfathered Benefits – Most employers have already decided whether to "grandfather" benefits that were vested at the end of 2004. Grandfathered benefits remain exempt from the section 409A rules provided they are not "materially modified." Employers who wish to preserve grandfathered treatment should make sure plan amendments do not result in a material modification.

6. Consider Contractual Restraints on Amendments – Because nonqualified retirement plans are typically exempt from most substantive requirements of ERISA, they are analyzed as contracts between the employer and plan participants. Thus, an employer should

consider contractual restraints on its ability to amend an existing plan (e.g., to remove distribution rights), particularly with respect to vested amounts.

7. Approve Necessary Amendments – Employers will need to have amendments required for section 409A compliance approved (typically by their Board of Directors or a Board committee) by the end of 2007.

8. Draft Administrative Procedures and Participant Communications – Once plan design changes have been developed, these materials should be prepared.

9. Consider Securities Law Issues for Public Companies – The establishment or material amendment of an executive compensation arrangement by a public company will generally need to be reported to the SEC on a Form 8-K within four business days. The new plan or amendment will typically need to be included with the next Form 10-Q or Form 10-K filed by the company.

10. Revise Service Provider Agreements – An employer should review service provider agreements, such as rabbi trust agreements, for any changes required for section 409A compliance by the end of 2007 or otherwise desirable (e.g., responsibility for new Form W-2 reporting requirements).

* * *

Please call one of the following, or the Groom attorney you regularly contact, if you have any questions about the new regulations or their impact on your executive compensation arrangements.

Eric Cotts.....	(202) 861-6616
Liz Dold	(202) 861-5406
Jeff Kroh	(202) 861-5428
Lou Mazawey.....	(202) 861-6608
John McGuiness	(202) 861-6625
David Powell.....	(202) 861-6600
Bill Sweetnam.....	(202) 861-5427
Brigen Winters	(202) 861-6618