



To Our Clients and Friends:

November 23, 2010

Use of IRS Notice 2010-6 to Correct Deferred Compensation Plans

Internal Revenue Code (“Code”) section 409A regulates the deferral of compensation under nonqualified deferred compensation arrangements. The arrangements covered by section 409A (“nonqualified plans”) include not only traditional retirement arrangements that are not qualified employer plans described in section 401(a) of the Code, but also other arrangements such as employment agreements, equity incentive plans, and severance arrangements that include a deferral of compensation.

After an extended transitional period, the requirements set forth in Treasury regulations under section 409A became fully effective on January 1, 2009. Other IRS guidance under section 409A includes two important notices relating to the correction of nonqualified plans that have been documented or operated in a manner not compliant with section 409A: Notice 2008-113, which addresses certain failures to operate a nonqualified plan in accordance with section 409A; and Notice 2010-6, concerning the correction of nonqualified plan documents that do not comply with section 409A.

Notice 2010-6 in particular describes various specific situations involving documentary noncompliance with section 409A and provides guidance as to (i) how a nonqualified plan may be corrected and (ii) whether and to what extent the adverse consequences of noncompliance with section 409A, including the acceleration of income and an additional 20% tax, may be avoided through correction in the manner described in the notice.

Notice 2010-6 also includes a transitional relief provision under which, if a nonqualified plan eligible for correction under the notice is corrected by December 31, 2010, it may be treated as having been corrected as of January 1, 2009, for purposes of applying the relief provisions set forth in the notice. Thus, correction of a nonqualified plan by December 31, 2010, combined with compliance with Notice 2008-113 by the same date with respect to any needed correction of any related operational failure under section 409A, may mitigate or eliminate any adverse consequences that would otherwise result from the nonqualified plan’s not having been in compliance with section 409A. Although Notice 2010-6 will remain in effect after 2010, this transitional relief provision will not apply with respect to corrections made after 2010.

IRS officials have indicated that the IRS is preparing guidance that will combine and expand upon the corrective procedures described in Notice 2008-113 and Notice 2010-6. However, the timing and details of this further guidance is unclear at this time.

The relief otherwise provided under Notice 2010-6 with respect to voluntary correction of documents is subject to various restrictions and limitations. In particular, the notice does not apply if, at the time of the correction, the employer's federal tax returns are under examination with respect to any taxable year during which the nonqualified plan documents were not in compliance with section 409A. In general, however, under the two notices referred to above, employers that correct plan documents and operational failures on their own initiative, rather than after being contacted by the IRS, may be able to avoid some of the adverse tax consequences that may otherwise be imposed under section 409A.

Taking into account all the above, employers with nonqualified plans that are potentially not compliant with section 409A should give serious consideration to taking corrective action before the end of this year to avoid adverse consequences under section 409A.

If you have any questions regarding the above, please contact David E. Kahen at (212) 903-8763, Norman J. Misher at (212) 903-8733, or Allen J. Erreich at (212) 903-8769.