



JONES DAY  
**COMMENTARY**

## SECTION 409A RESPITE: IRS GRANTS ONE-YEAR DELAY

Reversing decisions announced just six weeks ago, the Internal Revenue Service issued earlier this week a one-year extension of time for full compliance with Section 409A of the Internal Revenue Code. The IRS also moved several key compliance dates from December 31, 2007, to December 31, 2008. Most important, the IRS postponed the necessity to make permanent decisions on the basic structure of many compensation arrangements. This is welcome news for companies and their advisors, who have been confronting many difficult issues raised by Section 409A.

The compliance extension was announced in IRS Notice 2007-86. The Notice also extends until December 31, 2008, most of the transition relief provisions that were set to expire on December 31, 2007, including the provision permitting a change in the time or form of payment. As is currently the case, however, operational compliance with Section 409A is still required. This is especially important for employment terminations, deferral elections, and distributions.

We urge companies and individuals to continue to identify their Section 409A issues and reach workable solutions. Many decisions involve important substantive changes to executive compensation arrangements. When made, the reasons for these changes will need to be explained in a public company's next proxy statement. As a result, a thorough process and careful thought are critical. Furthermore, due to the rigidity imposed by Section 409A, decisions will be hard to alter after December 31, 2008.

Some specific items of interest dealt with in Notice 2007-86 are as follows:

- Under the new transition relief, a change in the time or form of payment can be made during 2008, provided that the change does not accelerate a payment into 2008 or defer a payment that otherwise was due in 2008. Therefore, employers should consider before the end of 2007 whether changes should be made to deferred compensation that will or may be paid in 2008, or that could be accelerated into 2008.

- The transition relief provision that permits, generally for non-Section 16 officers, the substitution of nondiscounted stock options for discounted options has been extended through December 31, 2008.
- The ability to link a payment election under a nonqualified plan to a qualified plan has been extended through December 31, 2008.
- The deadline for altering a “good reason” provision of an employment agreement to comply with the final regulations, or qualify for the final regulations’ safe harbor, has been extended until December 31, 2008. The Notice, however, retains the requirement that the change in the “good reason” provision must occur at a time when the employee’s right to payment is subject to a substantial risk of forfeiture.
- To the extent an item is not addressed in Notice 2005-1 (the “Q&As”) or other applicable guidance, a good-faith interpretation of the statute is sufficient. For periods before January 1, 2008, compliance with the proposed regulations or the final regulations will constitute good-faith compliance. For periods after December 31, 2007, and before January 1, 2009, compliance with the final regulations (but not the proposed regulations) will constitute good-faith compliance.

## LAWYER CONTACTS

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