

One Minute Memo[®]



December 31 Deadline Approaching for Amending Employment and Severance Agreements with Release Requirements

Many severance and change in control agreements, and some deferred compensation plans, require the employee to sign a release of claims or other agreement, such as a non-compete, in order to receive payment. If the employee can affect the timing of payments (for example, because the agreement does not specify a time period during which the release must be signed), and the payments at issue are deferred compensation under §409A of the Internal Revenue Code, the IRS takes the position that the arrangement may not comply with §409A requirements.

As we discussed in our Management Alert dated December 1, 2010, to read click [here](#), in Notice 2010-80, the IRS provided a procedure for employers to bring such arrangements that were in effect on December 31, 2010 into compliance with Code §409A. However, action is required by December 31, 2012.

Notice 2010-80 provides rules that the arrangement must follow if payment is contingent upon the employee satisfying a release requirement. If the arrangement already has a permissible designated period for payment following the payment event (i.e., separation from service), but the employee's action could affect the year of payment depending on when the payment event occurs and when in the period the employee signs the release, the amendment must provide for payment to be made or begin either (a) on the last day of the designated period or (b) in the second taxable year if the period begins in one taxable year and ends in a second taxable year. If the arrangement does not provide for payment within a permissible designated period following the payment event, the amendment must provide for payment to be made or begin either (a) upon a fixed date either 60 or 90 days after the payment event, or (b) during a specified period no longer than 90 days after the payment event, provided that if the period extends into a later taxable year, the payment must be made in the later year.

One of the most unpopular features of the §409A correction procedures is the requirement that both the employer and the employee must attach statements to their respective tax returns notifying the IRS that they have relied on the correction procedures. Notice 2010-80 provides that the employee is not required to attach a statement to his or her tax return for any correction of the release timing rules that is completed by December 31, 2012, under the transition rule described above. However, the employer is still required to file the attachment to its return.

Note that not all severance arrangements that require a release of claims, non-compete or similar agreement will be subject to Code §409A, since the exceptions for short-term deferral and/or involuntary separation pay plans may exempt these arrangements from Code §409A. Nonetheless, employers who maintain arrangements that could be subject to Code §409A - whether traditional deferred compensation plans, severance plans or executive agreements - in which an employee may be required to provide a release of claims, non-compete or similar agreement should review these arrangements to confirm that they are §409A compliant. If a revision is necessary, it should be completed by December 31, 2012.

If you have any questions about the Code §409A release rules, please contact the Seyfarth attorney with whom you work or any Employee Benefits attorney on our website.

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