

Legal News: Employee Benefits is part of our ongoing commitment to providing legal insight to our clients and our colleagues.

If you have any questions about this issue or would like to discuss these topics further, please contact your Foley attorney or any of the following individuals:

**Katherine L. Aizawa**  
San Francisco, CA  
415.438.6483  
kaizawa@foley.com

**Christopher S. Berry**  
Madison, WI  
608.258.4230  
cberry@foley.com

**Lloyd J. Dickinson**  
Milwaukee, WI  
414.297.5821  
lj Dickinson@foley.com

**Gregg H. Dooge**  
Milwaukee, WI  
414.297.5805  
gdooge@foley.com

**Robert E. Goldstein**  
San Diego, CA  
858.847.6710  
rgoldstein@foley.com

**Samuel F. Hoffman**  
San Diego, CA  
619.234.6655  
shoffman@foley.com

**Sarah Krause**  
Milwaukee, WI  
414.319.7340  
skrause@foley.com

**Harvey A. Kurtz**  
Milwaukee, WI  
414.297.5819  
hkurtz@foley.com

**Belinda Morgan**  
Chicago, IL  
312.832.4562  
bmorgan@foley.com

**Greg W. Renz**  
Milwaukee, WI  
414.297.5806  
grenz@foley.com

**Leigh C. Riley**  
Milwaukee, WI  
414.297.5846  
lriley@foley.com

**Michael H. Woolever**  
Chicago, IL  
312.832.4594  
mwoolever@foley.com

Thank you.

Harvey Kurtz  
Managing Editor

## Employee Benefits Developments for April 2007

### Executive Compensation

**Code Section 409A final regulations were released on April 10, 2007.** The link at the end of this sentence will take you to our special newsletter that describes the highlights of the final rules.  
[http://www.foley.com/publications/pub\\_detail.aspx?pubid=4065](http://www.foley.com/publications/pub_detail.aspx?pubid=4065)

**What should private, non-profit, and public employers do in response to the final Section 409A regulations?** The document compliance deadline is December 31, 2007, with no hint of extension. Treasury representatives have made clear that "savings clauses" will not be an effective means of compliance. The substantial penalties for noncompliance and the very short time to the compliance deadline, make immediate action vitally necessary. We suggest the following action steps:

- **Assemble All Possible Plans and Programs.** Section 409A compliance is emerging as a process similar to compliance programs for qualified retirement plans. We recommend compiling paper or electronic files that include any plans or programs that may have Section 409A issues, including administrative forms and award agreements. A partial listing of these includes: Options, stock appreciation rights, restricted stock units and other compensatory equity plans or programs; severance agreements; change in control agreements; long and short-term incentive pay plans; any kind of nonqualified deferred compensation plan; Supplemental Executive Retirement Plans; excess benefit plans; shadow or linked plans; Section 457(f) plans; and compensatory split-dollar life insurance plans. Do not overlook severance or other arrangements that may be "paid in full" before January 1, 2008, but may have provisions for later reimbursements or other payments.
- **Classify Each Plan or Program.** The exemptions in the final regulations from Section 409A coverage are substantial. It is well worth the effort now to determine definitively which plans or programs or provisions in contracts are exempt and which are not.
- **Assign Responsibility for Section 409A Compliance.** Plans and programs covered by Section 409A may be found at the board of directors level, in outside vendor (independent contractor) arrangements, under the auspices of the corporate secretary or general counsel in the case of some equity compensation arrangements, in the finance area, and/or in the human resources department. It is not practical for so many areas of a company to master Section 409A compliance in the short time available and, in many instances, coordination may be necessary between different types of programs. Overall responsibility for Section 409A compliance should be assigned to a specific person or persons who will have comprehensive access to all plans or programs that may be covered by Section 409A and who have the time and resources to secure compliance before year end.
- **Develop Compliance Plan and Execute.** The deadlines must be met and the deliverables must be completed on time, with effective follow through to completion, in order to satisfy the requirements of Section 409A by January 1, 2008. A comprehensive strategy and timetable need to be developed. For example, in many instances, the board of directors and/or its

## ABOUT FOLEY

The Employee Benefits attorneys of Foley & Lardner LLP counsel employers on employee benefits and executive compensation matters to reduce exposure to employee complaints, governmental agency actions, and union-related problems. We counsel on 401(k), profit sharing, employee stock ownership, pension and supplemental retirement plans as well as health, dental, disability, life insurance, severance, cafeteria, and flexible benefits plans. Our counsel also extends to Medicare and Social Security benefits, COBRA compliance, and post-retirement benefits issues. In addition, we advise clients in resolving benefits issues arising in mergers and acquisitions. We work closely with Foley trial lawyers who represent corporations and their benefit plans in litigation involving employment benefits and other obligations under ERISA.

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compensation committee will need to act to assure Section 409A compliance, and many boards and compensation committees do not meet in December.

- **Preserve Record of Interim Compliance and Grandfathering.** In the rush to comply with the requirements of the final regulations by January 1, 2008, it also will be very important to preserve the grandfathering available for pre-2005 plans and programs and to maintain sufficient records indicating compliance with Section 409A requirements during the interim period (January 1, 2005 – January 1, 2008).

Our recommended action plan emphasizes the need to assemble the library of potentially covered plans and programs and to classify them, first, and foremost, so that the scale of the necessary compliance effort can be assessed as soon as possible. Although there is a definite role in this process for expert legal counsel familiar with the law and regulations, a team effort, including a significant initial effort in-house to identify all possible plans and programs, is essential to getting the Section 409A compliance work accomplished by year end.

**IRS issued guidance regarding the application of Section 409A to split-dollar life insurance arrangements.** Notice 2007-34 provides guidance on how to identify the split-dollar life insurance plans that are subject to Section 409A, information on the application of the statutory effective date rules under Section 409A, and guidance on how to bring these arrangements into compliance.

**Limits on annual deferral amounts under nonqualified deferred compensation plans and expansion of the non-deductibility of certain executive compensation under Code Section 162(m) were dropped from the emergency supplemental bill sent to the President on May 1, 2007.** This kind of blunt attempt to limit “excessive” executive pay remains popular with some members of the U.S. Congress and seems likely to reappear in connection with future legislation.

## Qualified Retirement Plans

**Code Section 415 final regulations were issued April 4, 2007.** (Treasury Decision 9319) The final rules will apply to benefit limitation years (usually the plan year) beginning on or after July 1, 2007. Previous Section 415 final regulations were issued in 1981. The new rules incorporate the statutory changes since then and make other changes. A notable change from the proposed Section 415 regulations was made with reference to certain payments of compensation after a severance from service. The proposed rules only permitted certain post-severance compensation to be included as Section 415 pay if it was paid within two and a half months after the severance date. The final rules extended this period to the later of two and a half months after the severance from employment or the end of the limitation year that includes the date of severance from employment.

**Plan amendments to conform plans to the final Section 415 regulations qualify for the “remedial amendment period” applicable to the correction of disqualifying plan provisions.** That means, for example, for a calendar year employer with a calendar year plan, the period during which the necessary corrective amendments must be made ends on the date prescribed by law for the filing of the employer’s income tax return (including extensions) for the 2008 taxable year.

**Final rules on taxation of distributions from Roth 401(k) accounts.** (Treasury Decision 9324) The final rules redefine “designated Roth accounts” to include only those accounts under a plan to which designated Roth contributions are made in place of pretax 401(k) contributions. This change clarifies that a distribution from a designated Roth 401(k) account may only be rolled over to a Section 401(k) plan or Section 403(b) plan if the receiving account also may receive Roth 401(k) (or Roth 403(b)) contributions.