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Executive Compensation and Benefits Alert

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Certain Deferred Compensation Plans Must Be Amended by December 31, 2020

Transition relief for amending nonqualified deferred compensation (NQDC) plans to reflect the 2017 amendments to Section 162(m) of the Internal Revenue Code will expire on December 31, 2020.

The $1 million deduction limitation under Section 162(m) applies to payments to "covered employees" of public companies. Prior to the 2017 amendments to this section of the code made by the Tax Cuts and Jobs Act (see our January 4, 2018, client alert "<u>After the Tax Cuts and Jobs Act: What to Do Now</u>"), a "covered employee" under Section 162(m) in one taxable year would not necessarily remain a covered employee in a subsequent taxable year. Accordingly, Section 409A of the Internal Revenue Code permitted an employer to delay payments under NQDC arrangements if the employer reasonably anticipated that the company's tax deduction would be limited due to Section 162(m). Typically, this provision meant that payment would be delayed until an employee ceased to be a covered employee, for instance, upon employment termination.

Following the 2017 amendments, however, a covered employee in any year remains a covered employee for all subsequent taxable years (including beyond employment termination and even death). As a result, if an employer's NQDC arrangements provide for delay until the limitation no longer applies, the payment may be delayed for a very long time or indefinitely. Because eliminating the included delay to provide for earlier payment normally would itself be a violation of Section 409A rules, a proposed Treasury Regulation issued under Section 162(m) in December 2019 provides companies with the ability to amend their plans by December 31, 2020, to eliminate any built-in delays.

In particular, the proposed regulations provide that if a plan requires the employer to delay payment until it is deductible under Section 162(m), the plan may be amended to eliminate this requirement without the amendment resulting in an impermissible acceleration of payment under Section 409A. However, **such an amendment must be made no later than December 31, 2020** (unless this deadline is extended). The amendment may be limited to amounts not grandfathered under Section 162(m), with payment of grandfathered amounts remaining delayed. In any event, if the company would have been required to make a payment before December 31, 2020, under the NQDC arrangement, the payment must be made not later than December 31, 2020.

Companies should review their NQDC arrangements to determine whether their plans contain this type of delay provision and, if so, adopt any appropriate amendments before the end of the year. Outside counsel can often prove useful with the required analysis and the drafting of amendments.

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