Section 409A Tax Code Deadline

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The American Jobs Creation Act of 2004 created Internal Revenue Code Section 409A, seen largely as a response to deferred compensation abuses at Enron, WorldCom and other companies in the early 2000s. Section 409A applies to nonqualified deferred compensation plans and permits employees to defer income, subject to specific conditions related to the election, timing and distribution of benefits. Employers must review and, if necessary, amend deferred compensation plans to ensure full compliance by Jan. 1, 2009, or be subject to punitive tax treatment and penalties. Failure to comply with 409A, or failure to operate a plan in compliance, will cause all monies previously considered to be deferred income to become immediately taxable.

To ensure Section 409A compliance, employers should identify and review all plans, practices and arrangements that deal in any way with the timing and form of employee compensation - even if they were not previously considered deferred compensation. If employers fail to review and amend affected plans and agreements to fully comply with Section 409A by Jan. 1, employees could pay the price. Penalties for non-compliance are primarily borne by plan participants, who would be subject to the immediate taxation on the full amount of deferred monies, plus an additional 20 percent penalty tax. So, it's important for employers to comply to avoid inadvertently exposing employees to a substantial tax liability that could wipe out what remains of an employee's retirement funds or cause other financial hardships for the people they depend on to sustain their businesses.

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