



COMPLIANCE BULLETIN

October 2005

IRS Publishes Proposed Regulations for Nonqualified Deferred Compensation Plans

On October 4, 2005, the IRS published proposed regulations affecting nonqualified deferred compensation plans. These regulations provide guidance for implementing the Internal Revenue Code section 409A rules, which were enacted as part of the [American Jobs Creation Act of 2004 \(AJCA\)](#). Since these rules are only proposed, plan sponsors do not need to comply with them immediately. However, the rules do specify actions that plan sponsors may need to take before December 31, 2005. They also provide some important additional transitional period relief.

Immediate Action May Be Required

Some of the transition period relief that was available for 2005 is not available for 2006. As a result:

- Participants must make deferral elections on regular compensation to be received in 2006 by December 31, 2005.
- Participants who want to lower or cancel deferral elections or terminate their plan participation for 2006 must do so by December 31, 2005.
- Plan sponsors that want to terminate plans for reasons not allowed under the proposed rules must do so by the end of 2005.

In addition, plan sponsors that take advantage of any of the following transitional provisions in 2005, will ***need to document those actions*** (e.g., via plan amendment, Board of Directors resolution, election forms) ***by December 31, 2005***:

- Allowing participants to make new 2005 deferral elections after December 31, 2004, but by March 15, 2005;
- Allowing participants to cancel or revoke deferral elections;
- Terminating an individual's participation in a plan and distributing the amounts subject to the new rules by December 31, 2005; or
- Terminating a grandfathered plan and distributing all benefits by the end of 2005.

If you take advantage of any of these provisions in 2005, you should discuss plan documentation needs with your legal counsel.

Transition Period Extensions

On the other hand, the *good faith compliance period* has been *extended to December 31, 2006*.

As a result:

- Except as noted above, plans generally do not have to be amended to reflect these new rules until that date. Until then, plan sponsors must simply operate their plans in accordance with a good faith interpretation of the law and IRS guidance.
- Participants may be allowed to change the distribution provisions for amounts that are subject to the new rules until the end of 2006, within certain limits.
- Distributions paid by nonqualified plans may continue to be determined by the distribution option selected under a related qualified plan, through the end of 2006.

In general, these extensions provide plan sponsors with more time to make plan design decisions.

Additional Information Forthcoming

These proposed regulations are quite lengthy and somewhat complicated. In the near future, we will publish a *Washington Update* discussing the proposals in detail.

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