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**EBEC (Employee Benefits / Executive Compensation) Law Update**

December 6, 2010

**NOTICE 2010-80:  
RELIEF FOR PAYMENTS CONDITIONED ON EXECUTING  
RELEASES AND FOR § 409A CORRECTION PROGRAMS**

*Notice 2010-80 - Relief With Respect to Correction Methods and Payment Conditioned on Executing Release.* [Notice 2010-80](#), issued on Nov. 30, 2010, provides certain relief with respect to the correction methods described below, as well as with respect to payments conditioned on employment-related action of the employee such as executing a release, as summarized below.

- ❖ [IRS Notice 2008-113](#) described certain self-correction methods for Internal Revenue Code § 409A operational failures, provided the corrections are made in the year of failure or in certain cases in the first or second year following the year of failure. (The notice also provided certain transitional relief for operational failures occurring before 2008.) See Feb. 28, 2009 [client memo](#).
- ❖ [IRS Notice 2010-6](#) allowed taxpayers to voluntarily correct many documentary failures under IRC § 409A, including (i) impermissible definitions of payment events, (ii) impermissible payment periods, payment events or payment schedules, (iii) lack of six-month delay, (iv) impermissible initial deferrals, etc. This notice also provides certain transition rules for corrections on or prior to Dec. 31 2010 or for certain corrections on or prior to Dec. 31, 2011.
- ❖ Notice 2010-6 also provides relief for payments conditioned on employment-related action of the employee such as executing a release, non-solicitation agreement or non-compete agreement, that correction can be made before the permissible payment event occurs by removing the ability of the employee to delay or accelerate the timing of the payment as a result of his or her actions, and fixing the payment date at 60 (or 90) days after the payment event (with certain other conditions, as outlined below). See March 7, 2010 [client memo](#) for more information.

***Severance Conditioned on Executing Release – Expanded Relief.*** When payment of severance is conditioned on the employee's signing a release of claims (including age discrimination waivers), and the employee can sign the release at any time, this could cause the severance to fail to be a short-term deferral or to have or not have a fixed payment date as required by IRC § 409A.

One solution that practitioners have used is to provide a fixed deadline in which time to execute the release, e.g., the release must be executed and not revoked by the 60th (or 90th) day following termination, and

the terms of the release would be agreed upon in advance. This way, the ADEA 21-day period to consider the release, or the 45-day period in connection with an exit incentive program or other employment termination program, and the 7 days to revoke can be satisfied before the expiration of that period, and the payment is fixed to withdraw 60 (or 90) days after termination. In addition, in order to avoid an employee being able to control the year of payment, a provision would also need to be added that if the 60 (or 90) day period begins in one taxable year and ends in the next taxable year the payment will automatically be pushed to the next taxable year.

The IRS had indicated informally and in Notice 2010-6, however, that such a solution may not work, because there would be an impermissible toggle by being able to have a different pay option depending on whether the employee terminates before or after November 1. The solution the IRS suggested is to require is that regardless of whether the release is executed right away, the severance payment will only be made 60 (or 90) days after termination, provided an irrevocable release is in place by then. This solution is supported by Notice 2010-6 § VI.B, which provides a documentary correction that if payment is conditioned on the employee executing a release, correction can be made before the permissible payment event occurs by removing the ability of the employee to delay or accelerate the timing of the payment as a result of his or her actions, and fixing the payment date at 60 (or 90) days after the payment event.

- ❖ Note that much of the above requirements only apply if the severance arrangement is subject to § 409A, but if the severance can be paid within the short term deferral period (e.g., it has a safe harbor § 409A good reason definition) or within the two years two times pay exception for involuntary terminations, this would avoid application of § 409A and therefore it would not be subject to the toggle rule relating to § 409A payment events or the straddling of two years. The release would have a fixed deadline that must be executed and become irrevocable within e.g., 60 (or 90) days, and the severance would have to be paid in all events no later than 2-½ months (to ensure that it is a short-term deferral), or within two years if relying on that exception.

The IRS has retreated somewhat from its position requiring a fixed date, and has determined that the first solution – to set a 60 day (or 90 day) deadline for executing the release and payment and to push the payment date to the next year if this period begins in one calendar year and ends in the next year – would also work. This position is set forth in Notice 2010-80 that payment of severance can be set as not longer than 60 (or 90) days following the termination (the permissible payment event), provided that if such 60 (or 90) day period begins in the employee's first taxable year and extends into the employee's second taxable year, the payment must be made in the second taxable year (or alternatively the payment can be set for the last day of the period as per the method described above).<sup>1</sup>

***Transition Relief for Severance with Release through Dec. 31, 2012.*** Notice 2010-80 also modifies Notice 2010-6 by providing additional transition relief through December 31, 2012 for plans that contain failures involving payments dependent upon the employee executing a release (and the plan is eligible for correction by December 31, 2010 ), provided that any payments made after March 31, 2011 that could be paid during a period that begins in one taxable year and ends in the subsequent taxable year are made during the subsequent taxable year and provided further that to the extent any amounts remain deferred under the plan, the plan is amended to be compliant by no later than December 31, 2012.<sup>2</sup>

***Certain Linked Plans and Stock Rights are Included in Documentary Corrections.*** Notice 2010-80 amends Notice 2010-6 to provide that the documentary corrections can be utilized: (i) by linked plans (nonqualified plans linked with qualified plans) with document failures if the linkage does not affect the time and form of payment of amounts under the plans; and (ii) by stock rights (stock options and stock appreciation

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<sup>1</sup> Notice 2010-80 § III.B modifying § VI.B.2 of Notice 2010-6.

<sup>2</sup> Notice 2010-80 § III.C adding § VI.B.3 to Notice 2010-6.

rights) that were intended at the time of grant (or upon a modification pursuant to applicable transition relief) to be subject to and compliant with § 409A but that have a plan document failure.<sup>3</sup>

***Relief Regarding Information and Reporting Requirements for Operational Corrections.*** Notice 2008-113 provides information and reporting requirements by the employee and employer to make the operational corrections. For example, with respect to same year corrections, Notice 2008-113 provides that the employer must attach to its federal income tax return for its taxable year in which the failure occurred a statement entitled “Section 409A Relief under Section IV of Notice 2008-113” with specific information about the correction, and the employer must provide to each affected employee a similar statement by the W-2 due date.<sup>4</sup> Notice 2010-80 amends this provision so that notice to the employee is not required for corrections in the same year of payment.<sup>5</sup>

***Relief Regarding Information and Reporting Requirements for Documentary Corrections.*** An employer with respect to any of the corrections in the notice must attach to its corporate tax returns and to the W-2’s and 1099’s for the year of failure an exhibit entitled “409A Document Correction Under § \_\_\_ of Notice 2010-6,” which must include certain information about the correction.<sup>6</sup> The affected employees must also be provided with a statement that the employee is entitled to the relief provided in the applicable provision in Notice 2010-6 with respect to a failure to comply with § 409A, and containing the above information about the correction, and that the employee must attach a copy of the statement to his or her income tax return for the taxable year in which the failure was corrected.<sup>7</sup> Notice 2010-80 modifies Notice 2010-6 to provide that this statement is not required to be furnished by the employer to the employees and is not required to be attached by the employees to their tax returns with respect to transition relief corrections that may be made prior to Dec. 31, 2010, 2011 or 2012, as applicable,<sup>8</sup> although the employer is still required to attach the statement to its return.<sup>9</sup>

***Prompt Attention.*** If you are unsure if your documents or procedures need corrections, prompt attention is advisable, as certain of the transition rules for corrections end on December 31, 2010.

**IRS Circular 230 Disclosure:** To ensure compliance with requirements imposed by the IRS, we inform you that any U.S. federal tax advice contained in this communication is not intended or written to be used, and cannot be used, for the purpose of (i) avoiding penalties under the Internal Revenue Code or (ii) promoting, marketing or recommending to another party any transaction or matter that is contained in this document.

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<sup>3</sup> Notice 2010-80 § III.A.

<sup>4</sup> Notice 2008-113 § IX.

<sup>5</sup> Notice 2010-80 § III.H amending Notice 2008-113 § IX.

<sup>6</sup> Notice 2010-6 § XII.A. The attachment describing the documentary correction should set forth the name and tax identification number for each service provider affected by the failure, identification of the plan with the failure, a statement that the document failure is eligible for correction (and identifying the specific section of the notice) and stating the amount involved in the documentary error. Notice 2010-6 § XII.B.

<sup>7</sup> Notice 2010-6 § XII.C. The employee must attach to his or her tax return a copy of the above statement regarding the failure. § XIII.D.

<sup>8</sup> The transition relief corrections are in Notice 2010-6 § XI and in Notice 2010-6 § VI.B.3 (as added by Notice 2010-80).

<sup>9</sup> Sections III.E, F & G of Notice 2010-80 amending § XII of Notice 2010-6.