

26 CFR 1.409A-3

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Code of Federal Regulations > Title 26 Internal Revenue > Chapter I — Internal Revenue Service, Department of the Treasury > Subchapter A — Income Tax > Part 1 — Income Taxes > Normal Taxes and Surtaxes > Deferred Compensation, Etc. > Pension, Profit-Sharing, Stock Bonus Plans Etc.

§ 1.409A-3 Permissible payments.

(a) In general. The requirements of section 409A(a)(2)(A) [26 USCS § 409A(a)(2)(A)] are met only if the plan provides that an amount of deferred compensation under the plan may be paid only upon an event or at a time set forth in this paragraph (a):

- (1) The service provider's separation from service (as defined in § 1.409A-1(h) and in accordance with paragraph (i)(2) of this section).
- (2) The service provider becoming disabled (in accordance with paragraph (i)(4) of this section).
- (3) The service provider's death.
- (4) A time or a fixed schedule specified under the plan (in accordance with paragraph (i)(1) of this section).
- (5) A change in the ownership or effective control of the corporation, or in the ownership of a substantial portion of the assets of the corporation (in accordance with paragraph (i)(5) of this section).
- (6) The occurrence of an unforeseeable emergency (in accordance with paragraph (i)(3) of this section).

(b) Designation of payment upon a permissible payment event. Except as otherwise specified in this section, a plan provides for the payment upon an event described in paragraph (a)(1), (2), (3), (5), or (6) of this section if the plan provides the date of the event is the payment date, or specifies another payment date that is objectively determinable and nondiscretionary at the time the event occurs. A plan may also provide that a payment upon an event described in paragraph (a)(1), (2), (3), (5), or (6) of this section is to be made in accordance with a schedule that is objectively determinable and nondiscretionary based on the date the event occurs and that would qualify as a fixed schedule under paragraph (i)(1) of this section if the payment event were instead a fixed date, provided that the schedule must be fixed at the time the permissible payment event is designated. In addition, a plan may provide that a payment, including a payment that is part of a schedule, is to be made during a designated taxable year of the service provider that is objectively determinable and nondiscretionary at the time the payment event occurs such as, for example, a schedule of three substantially equal payments payable during the first three taxable years following the taxable year in which a separation from service occurs. A plan may also provide that a payment, including a payment that is part of a schedule, is to be made during a designated period objectively determinable and nondiscretionary at the time the payment event occurs, but only if the designated period both begins and ends within one taxable year of the service provider or the designated period is not more than 90 days and the service provider does not have a right to designate the taxable year of the payment (other than an election that complies with the subsequent deferral election rules of § 1.409A-2(b)). Where a plan provides for a period of more than one day following a payment event during which a payment may be made, such as within 90 days following the date of the event, the payment date for purposes of the subsequent deferral rules under § 1.409A-2(b) is treated as the first possible date upon which a payment could be made under the terms of the plan. A plan may provide for payment upon the earliest or latest of more than one event or time, provided that each event or time is described in paragraphs (a)(1) through (6) of this section. For examples illustrating the provisions of this paragraph, see paragraph (i)(1)(vi) of this section.

(c) Designation of alternative specified dates or payment schedules based upon date of permissible event. Except as otherwise provided in this paragraph (c), for an amount of deferred compensation under a plan, the plan may designate

only one time and form of payment upon the occurrence of each event described in paragraph (a)(1), (2), (3), (5), or (6) of this section. For example, a plan does not satisfy the requirements of this paragraph (c) if it provides for one payment date or schedule of payments if a specified event occurs on a Monday, but another payment date or schedule of payments if the event occurs on any other day of the week. However, a plan that provides for a payment upon an event described in paragraph (a)(2), (3), (5), or (6) of this section may allow for an alternative payment schedule if the event occurs on or before one (but not more than one) specified date, provided that the addition or deletion of such a different time and form of payment applicable to an existing deferral is subject to § 1.409A-2(b) (subsequent deferral elections) and paragraph (j) of this section (accelerated payments). For example, a plan may provide that a service provider will receive a lump sum payment of the service provider's entire benefit under the plan on the first day of the month following a change in control event that occurs before the service provider attains age 55, but will receive 5 substantially equal annual payments commencing on the first day of the month following a change in control event that occurs on or after the service provider attains age 55. In the case of a plan that provides that a payment upon an event described in paragraph (a)(1) of this section (a payment upon a separation from service), a different time and form of payment may be designated with respect to a separation from service under each of the following conditions, provided that the addition or deletion of such a different time and form of payment applicable to an existing deferral is subject to § 1.409A-2(b) and paragraph (j) of this section:

- (1) A separation from service during a limited period of time not to exceed two years following a change in control event (as defined in paragraph (i)(5) of this section).
- (2) A separation from service before or after a specified date (for example, the attainment of a specified age), or a separation from service before or after a combination of a specified date, such as attaining a specified age, and a specified period of service determined under a predetermined, nondiscretionary, objective formula or pursuant to the method for crediting service under a qualified plan sponsored by the service recipient.
- (3) A separation from service not described in paragraphs (c)(1) or (c)(2) of this section.

(d) When a payment is treated as made upon the designated payment date. Except as otherwise specified in this section, a payment is treated as made upon the date specified under the plan (including a date specified under paragraph (a)(4) of this section) if the payment is made at such date or a later date within the same taxable year of the service provider or, if later, by the 15th day of the third calendar month following the date specified under the plan and the service provider is not permitted, directly or indirectly, to designate the taxable year of the payment. In addition, a payment is treated as made upon the date specified under the plan (including a date specified under paragraph (a)(4) of this section) and is not treated as an accelerated payment if the payment is made no earlier than 30 days before the designated payment date and the service provider is not permitted, directly or indirectly, to designate the taxable year of the payment. For purposes of this paragraph, if the date specified is only a designated taxable year of the service provider, or a period of time during such a taxable year, the date specified under the plan is treated as the first day of such taxable year or the first day of the period of time during such taxable year, as applicable. The payment with respect to a stock right generally occurs upon the exercise of the stock right, so that where a stock right designates a fixed exercise date, the stock right will be deemed to have been paid at such date if the exercise and payment occur on such date or a later date within the same taxable year of the service provider or, if later, by the 15th day of the third calendar month following the exercise date specified under the plan. If calculation of the amount of the payment is not administratively practicable due to events beyond the control of the service provider (or service provider's beneficiary), the payment will be treated as made upon the date specified under the plan if the payment is made during the first taxable year of the service provider in which the calculation of the amount of the payment is administratively practicable. For purposes of this paragraph, the inability of a service recipient to calculate the amount or timing of a payment due to a failure of a service provider (or service provider's beneficiary) to provide reasonably available information necessary to make such calculation does not constitute an event beyond the control of the service provider. Similarly, if the making of the payment at the date specified under the plan would jeopardize the ability of the service recipient to continue as a going concern, the payment will be treated as made upon the date specified under the plan if the payment is made during the first taxable year of the service provider in which the making of the payment would not have such effect.

(e) Designation of time and form of payment with respect to earnings. A nonqualified deferred compensation plan that provides for actual or notional earnings to be credited on amounts of deferred compensation may specify, in accordance with the requirements of § 1.409A-2(a) (initial deferral elections), that such earnings are treated separately from the right

to the other amounts deferred under the plan for purposes of designating the time and form of payments under such plan, provided that to satisfy the requirements of this paragraph (e), actual or notional earnings must be credited at least annually. For these purposes, a right to dividend equivalents may be treated analogously to a right to actual or notional earnings on an amount of deferred compensation. For purposes of this paragraph (e), the term dividend equivalents means the right to an amount equal to all or a specified portion of dividends declared and paid, if any, on a specified number of shares of stock.

(f) Substitutions. Except as otherwise provided under these regulations, the payment of an amount as a substitute for a payment of deferred compensation will be treated as a payment of the deferred compensation. A forfeiture or voluntary relinquishment of an amount of deferred compensation will not be treated as a payment of the compensation, but there is no forfeiture or voluntary relinquishment for this purpose if an amount is paid, or a legally binding right to a payment is created, that acts as a substitute for the forfeited or voluntarily relinquished amount. Whether a payment or a right to a payment acts as a substitute for a payment of deferred compensation is determined based on all the facts and circumstances. However, where the payment of an amount results in an actual or potential reduction of, or current or future offset to, an amount of deferred compensation, or if the service provider receives a loan the repayment of which is secured by or may be accomplished through an offset of or a reduction in an amount deferred under a nonqualified deferred compensation plan, the payment or loan is a substitute for the deferred compensation. In addition, where a service provider's right to deferred compensation is made subject to anticipation, alienation, sale, transfer, assignment, pledge, encumbrance, attachment, or garnishment by creditors of the service provider or the service provider's beneficiary, the deferred compensation is treated as having been paid. For the treatment of certain offsets, see paragraph (j)(4)(xiii) of this section. Even where there is no explicit reduction or offset, the payment of an amount or creation of a new right to a payment proximate to the purported forfeiture or voluntary relinquishment of a right to deferred compensation is presumed to be a substitute for the deferred compensation. The presumption is rebuttable by a showing that the compensation paid would have been received regardless of the forfeiture or voluntary relinquishment of the right to deferred compensation. Factors indicating that a payment would have been received regardless of such forfeiture or voluntarily relinquishment include that the amount paid is materially less than the forfeited or relinquished amount, or consists of a type of payment customarily made in the ordinary course of business of the service recipient to service providers who do not forfeit or relinquish deferred compensation (for example, a payment of accrued but unused leave or a payment for a release of actual or potential claims). See § 1.409A-1(b)(9)(i) with respect to certain separation pay plans.

(g) Disputed payments and refusals to pay. If a service recipient fails to make a payment in whole or in part as of the date specified under a plan, either intentionally or unintentionally, other than with the express or implied consent of the service provider, the payment will be treated as made upon the date specified under the plan if the service provider accepts the portion (if any) of the payment that the service recipient is willing to make (unless such acceptance will result in a relinquishment of the claim to all or part of the remaining amount), makes prompt and reasonable, good faith efforts to collect the remaining portion of the payment, and any further payment (including payment of a lesser amount that satisfies the obligation to make the payment) is made no later than the end of the first taxable year of the service provider in which the service recipient and the service provider enter into a legally binding settlement of such dispute, the service recipient concedes that the amount is payable, or the service recipient is required to make such payment pursuant to a final and nonappealable judgment or other binding decision. For purposes of this paragraph (g), efforts to collect the payment will be presumed not to be prompt, reasonable, good faith efforts, unless the service provider provides notice to the service recipient within 90 days of the latest date upon which the payment could have been timely made in accordance with the terms of the plan and these regulations, and unless, if not paid, the service provider takes further enforcement measures within 180 days after such latest date. For purposes of this paragraph (g), a service recipient is not treated as having failed to make a payment where pursuant to the terms of the plan the service provider is required to request payment, or otherwise provide information or take any other action, and the service provider has failed to take such action. In addition, for purposes of this paragraph (g), the service provider is deemed to have requested that a payment not be made, rather than the service recipient having failed to make such payment, where the service recipient's decision to refuse to make the payment is made by the service provider or a member of the service provider's family (as defined in section 267(c)(4) [26 USCS § 267(c)(4)] applied as if the family of an individual includes the spouse of any member of the family), or any person or group of persons over whom the service provider or service provider's family member has effective control, or any person any portion of whose compensation is controlled the service provider or service provider's family member.

(h) Special rule for certain resident aliens. An agreement, method, program, or other arrangement that is, or constitutes part of, a nonqualified deferred compensation plan is deemed to meet the requirements of this section with respect to any amount payable in the first taxable year of the service provider in which a service provider is a resident alien, and with respect to any amount payable in a subsequent taxable year if no later than the last day of the first taxable year of the service provider in which the service provider is a resident alien, the plan is amended as necessary so that the times and forms of payment of amounts payable in a subsequent year comply with the provisions of this section. For any year after the first taxable year of an individual in which the individual is a resident alien, this paragraph (h) does not apply, provided that a taxable year may again be treated as the first taxable year in which an individual is a resident alien if such individual has not been a resident alien for at least three consecutive taxable years immediately preceding the taxable year in which the service provider is again a resident alien.

(i) Definitions and special rules —

(1) Specified time or fixed schedule —

(i) In general. Amounts are payable at a specified time or pursuant to a fixed schedule if objectively determinable amounts are payable at a date or dates that are nondiscretionary and objectively determinable at the time the amount is deferred. An amount is objectively determinable for this purpose if the amount is specifically identified or if the amount may be determined at the time payment is due pursuant to an objective, nondiscretionary formula specified at the time the amount is deferred (for example, 50 percent of a specified account balance). Except as otherwise provided in paragraph (i)(1) of this section, an amount is not objectively determinable if the amount of the payment is based all or in part upon the occurrence of an event, including the consummation of a transaction by, or a payment of an amount to, a service recipient. If an amount is payable in a service provider's taxable year (or pursuant to a fixed schedule of taxable years of the service provider) that is designated at the time the amount is deferred and that is objectively determinable, the amount is treated as payable at a specified time (or pursuant to a fixed schedule), provided that for purposes of the application of the subsequent deferral rules contained in § 1.409A-2(b), the specified time or fixed schedule of payments is deemed to refer to the first day of the relevant taxable year or years. A specified time or fixed schedule also includes the designation at the time the amount is deferred of a defined period or periods within the service provider's taxable year or taxable years that are objectively determinable, provided that no such defined period may begin within one taxable year and end within another taxable year, and provided further that for purposes of the application of the subsequent deferral rules contained in § 1.409A-2(b), the specified time or fixed schedule of payments is deemed to refer to the first day of the relevant period in which the payment will be made. A plan may provide that a payment upon the lapse of a substantial risk of forfeiture is to be made in accordance with a fixed schedule that is objectively determinable based on the date the substantial risk of forfeiture lapses (disregarding any discretionary acceleration of the lapse of the substantial risk of forfeiture), provided that the schedule must be fixed on the date the time and form of payment are designated, and any change in the fixed schedule will constitute a change in the time and form of payment. For example, a plan that provides for a bonus payment subject to the condition that the service provider complete three years of service, and subject to the further condition that such requirement of continued services will lapse upon the occurrence of an initial public offering, which condition if applied alone would constitute a substantial risk of forfeiture, may provide that a service provider is entitled to substantially equal payments on each of the first three anniversaries of the date the substantial risk of forfeiture lapses (the earlier of three years of service or the date of an initial public offering).

(ii) Payment schedules with formula and fixed limitations —

(A) Individual limitations. A schedule of payments does not fail to be a fixed schedule of payments where the amount of a payment or payments that may be paid at a specified time or during a specified period is limited by an objective nondiscretionary formula or a specified amount that is not under the effective control of the service provider and is not subject to the exercise of discretion by the service recipient, where such limitation is established on or before the date the time and form of payment is otherwise required to be set under these regulations, and the plan specifies the time and form of any payment that will be made or completed after its original payment date due to the application of the

limitation. A change in the limitation or a change in the time and form of any payment that exceeds the limitation is subject to the requirements of § 1.409A-2(b) (subsequent deferral elections) and paragraph (j) of this section (accelerated payments). For purposes of this paragraph, a plan provision that reduces a schedule of periodic payments on a dollar-for-dollar basis by the amount of Social Security payments received or receivable may be treated as a nondiscretionary, objective formula limitation, if such reduction does not otherwise affect the time of payment of the deferred compensation (other than a forfeiture due to the reduction), including changes based on the service provider's eligibility or elections related to Social Security benefits. Similarly, a plan provision that reduces a schedule of periodic payments on a dollar-for-dollar basis by the amount of bona fide disability pay (within the meaning of § 1.409A-1(a)(5)) received or receivable may be treated as a nondiscretionary, objective formula limitation, if the disability payments are made pursuant to a plan sponsored by the service recipient that covers a substantial number of service providers and was established before the service provider became disabled, and if such reduction does not otherwise affect the time of payment of the deferred compensation (other than a forfeiture due to the reduction). Whether an amendment to, or other change in the benefit payable under, such bona fide disability plan results in an acceleration of a payment for purposes of paragraph (j) of this section or a subsequent election to delay the time or change the form of payment for purposes of § 1.409A-2(b) is determined based on all of the relevant facts and circumstances.

(B) Limitations on aggregate payments to all participants in substantially identical plans. A schedule of payments does not fail to be a fixed schedule of payments where the amount of the aggregate payments that will be made during a specified period of time to all participants in substantially identical plans is limited by an objective nondiscretionary formula or specified amount that is not under the effective control of the service provider and is not subject to the exercise of discretion by the service recipient, where the limit is established on or before the date the time and form of payment of the amount deferred is otherwise required to be set under these regulations, the method of allocating payments among the participants where there is an overall limitation on the aggregate amount that may be paid to a group of service providers during a specified period is an objective nondiscretionary allocation method that is not under the effective control of the service provider and is not subject to the exercise of discretion by the service recipient, the method is established on or before the date the time and form of payment of the amount deferred is otherwise required to be set, and the plan specifies the time and form of any payment of any amount that will be paid after its original payment date due to the application of the limitation. A change in the limitation or a change in the time and form of payment of any payment that is not otherwise made at the scheduled payment date due to application of the formula limitation is subject to the requirements of § 1.409A-2(b) (subsequent deferral elections) and paragraph (j) of this section (accelerated payments).

(iii) Payment schedules determined by timing of payments received by the service recipient. A payment schedule determined by reference to the timing of payments received by the service recipient (not including payments from one entity to another entity where both entities are treated as part of a single service recipient), meets the requirements of a specified date or fixed schedule of payments if the following conditions are met:

- (A)** The payments due to the service recipient arise from bona fide and routine transactions in the ordinary course of business of the service recipient.
- (B)** The service provider does not have effective control of the service recipient, the person from whom such amounts are due, or the collection of any of the amounts due to the service recipient.
- (C)** The payment schedule provides an objective, nondiscretionary method of identification of the payments to the service recipient from which the amount of the payment from the service recipient to the service provider is determined.
- (D)** The payment schedule provides an objective, nondiscretionary schedule under which the payments will be made to the service provider.

(E) The payments to the service recipient from which the amount of the payments from service recipient to the service provider are determined result from sales of a type that the service recipient is in the trade or business of making and makes frequently, and either all such sales by the service recipient are taken into account for purposes of determining the payment to the service provider, or there is a legitimate, non-tax business reason for identifying the specific sales taken into account.

(iv) Reimbursement or in-kind benefit plans —

(A) General rule. A plan that provides for reimbursements of expenses incurred by a service provider, or in-kind benefits, meets the requirements of a specified date or fixed schedule of payments with respect to such reimbursements or benefits if the following conditions are met:

- (1)** The plan provides an objectively determinable nondiscretionary definition of the expenses eligible for reimbursement or of the in-kind benefits to be provided.
- (2)** The plan provides for the reimbursement of expenses incurred or for the provision of the in-kind benefits during an objectively and specifically prescribed period (including the lifetime of the service provider).
- (3)** The plan provides that the amount of expenses eligible for reimbursement, or in-kind benefits provided, during a service provider's taxable year may not affect the expenses eligible for reimbursement, or in-kind benefits to be provided, in any other taxable year.
- (4)** The reimbursement of an eligible expense is made on or before the last day of the service provider's taxable year following the taxable year in which the expense was incurred.
- (5)** The right to reimbursement or in-kind benefits is not subject to liquidation or exchange for another benefit.

(B) Medical reimbursement arrangements. Notwithstanding the foregoing, an arrangement providing for the reimbursement of expenses referred to in section 105(b) [26 USCS § 105(b)] will not be deemed to fail to meet the requirements of paragraph (i)(1)(iv)(A)(3) of this section solely because the arrangement provides for a limit on the amount of expenses that may be reimbursed under such arrangement over some or all of the period in which the reimbursement arrangement remains in effect.

(v) Tax gross-up payments. A plan providing a right to a tax gross-up payment will be treated as providing for payment at a specified time or on a fixed schedule of payments if the plan provides that payment will be made, and the payment is made, by the end of the service provider's taxable year next following the service provider's taxable year in which the service provider remits the related taxes. For purposes of this paragraph (i)(1)(v), the term tax gross-up payment refers to a payment to reimburse the service provider in an amount equal to all or a designated portion of the Federal, state, local, or foreign taxes imposed upon the service provider as a result of compensation paid or made available to the service provider by the service recipient, including the amount of additional taxes imposed upon the service provider due to the service recipient's payment of the initial taxes on such compensation. In addition, a right to the reimbursement of expenses incurred due to a tax audit or litigation addressing the existence or amount of a tax liability, whether Federal, state, local, or foreign, satisfies the requirement of a fixed time and form of payment if the right to the reimbursement provides that payment will be made, and the payment is made, by the end of the service provider's taxable year following the service provider's taxable year in which the taxes that are the subject of the audit or litigation are remitted to the taxing authority, or where as a result of such audit or litigation no taxes are remitted, the end of the service provider's taxable year following the service provider's taxable year in which the audit is completed or there is a final and nonappealable settlement or other resolution of the litigation. Nothing in this paragraph (i)(1)(v) otherwise alters the application of section 409A [26 USCS § 409A] to the underlying compensation arrangement or other arrangement that results in the taxes subject to the right to the tax gross-up payment.

(vi) Examples. The following examples (in which each employee is an individual whose taxable year is the calendar year) illustrate the principles of paragraphs (a), (b), (c), (d), and (i)(1) of this section:

Example 1.

Employee A provides services as an employee of Employer Z, but is not a specified employee. Employee A participates in a nonqualified deferred compensation plan providing for a lump sum payment payable on or before December 31 of the calendar year in which Employee A separates from service. The plan provides for a payment upon a separation from service in compliance with this section.

Example 2.

Employee B provides services as an employee of Employer Y, but is not a specified employee. Employee B participates in a nonqualified deferred compensation plan providing for a lump sum payment payable on or before the 90th day immediately following the date upon which Employee B separates from service. Employer Y retains the sole discretion to determine when during the 90-day period the payment will be made. Although the plan does not specify a period during one calendar year in which the payment will be made, the plan provides for a payment upon a separation from service in compliance with this section because the period over which the payment may be made is not longer than 90 days.

Example 3.

Employee C provides services as an employee of Employer X, but is not a specified employee. Employee C participates in a nonqualified deferred compensation plan providing for a lump sum payment payable on or before the 180th day following the date upon which Employee C separates from service. Employer X retains the sole discretion to determine when during the 180-day period the payment will be made. Because the plan does not specify a period during one calendar year in which the payment will be made, and because the period over which the payment may be made is longer than 90 days, the plan does not provide for a payment upon a separation from service that complies with this section.

Example 4.

Employee D provides services as an employee of Employer W, but is not a specified employee. Employee D participates in a nonqualified deferred compensation plan providing for 10 installment payments payable on the first 10 anniversaries of the date Employee D separates from service, provided that no installment payment in any year may be more than 1% of Employer W's net income for the previous calendar year, and provided further that the excess over such limit that would otherwise be payable but is not paid due to application of the limit will become payable as of the first installment payment date at which time such amount, in combination with any installment payment otherwise due Employee D, does not exceed 1% of Employer W's net income for the previous calendar year. Provided that Employee D does not retain effective control of the calculation of Employer W's net income or the amount that Employee D will not be paid due to application of the limit, the plan provides for a schedule of payments upon a separation from service that complies with this section.

Example 5.

Employee E and Employee F provide services as employees of Employer V, but neither is a specified employee. Employee E and Employee F both participate in substantially identical nonqualified deferred compensation plans providing for 10 installment payments payable on the first 10 anniversaries of the date the respective employee separates from service, provided that the total amount of installment payments in any year may not be more than 1% of Employer V's net income for the previous year, that where any payments are not made due to application of the limit the determination of the amount not paid to a particular employee will be made by applying the overall limit proportionately based upon the installment payment due the employee that year, and that the excess over such limit that would otherwise be payable but is not paid due to application of the limit will become payable as of the first installment payment date at which time such amount, in combination with any installment payments otherwise due the participants, does not exceed 1% of Employer V's net income for the previous calendar year. Provided that neither Employee E nor Employee F retains effective control of the calculation of Employer V's net income or the amount that the respective employee will not be paid due to application of the limit, the plan provides for a schedule of payments upon a separation from service that complies with this section.

Example 6.

Employee G provides services as an employee of Employer U, but is not a specified employee. As a bona fide part of this employment relationship, Employee G provides professional services to clients of Employer U as part of the bona fide, ordinary course of Employer U's trade or business. Under an arrangement between Employee G and Employer U, Employer U agrees to pay Employee G upon Employee G's separation from service an amount equal to 5% of any amount collected from Company T, a client of Employer U for which Employee G performed services during his employment with Employer U, during the 36 months following Employee G's separation from service. Under the arrangement, the amounts due to Employee G based upon payments received by Employer U during any calendar year are payable to Employee G on April 1 of the subsequent calendar year. Provided that Employee G does not have effective control of Employer U, Company T, or the collection of any amounts due Employer Y from Company T, the arrangement provides for a schedule of payments upon a separation from service that complies with this section.

Example 7.

Employee H provides services as an employee of Employer S, but is not a specified employee. Under a plan sponsored by Employer S, Employee H has a legally binding right upon a separation from service to the reimbursement of country club dues paid in the calendar year of the separation from service and each of the next 3 calendar years following the separation from service in an amount not to exceed \$ 30,000 in any calendar year, provided that the amount of dues paid in any calendar year that are eligible for reimbursement equals only the amount actually expended during such calendar year, and the maximum amount available for reimbursement in any calendar year will not be increased or decreased to reflect the amount expended or reimbursed in a prior or subsequent calendar year. The plan further provides that any reimbursement must be paid to Employee H by December 31 of the calendar year following the year in which Employee H pays the country club dues. The reimbursement plan provides for a schedule of payments upon a separation from service that complies with this section.

Example 8.

Employee J provides services as an employee of Employer Q, but is not a specified employee. Under a plan sponsored by Employer Q, Employee J has a legally binding right upon a separation from service to the reimbursement of country club dues paid during the calendar year in which the separation from service occurs and the next 3 calendar years in a total amount not to exceed \$ 90,000. The plan further provides that any reimbursement must be paid to Employee J by December 31 of the calendar year following the year in which Employee J pays the country club dues. Because the reimbursement of a payment of country club dues in one calendar year may affect the amount of country club dues available for reimbursement in another calendar year, the plan does not provide for a schedule of payments upon a separation from service that complies with this section.

(2) Separation from service — required delay in payment to a specified employee pursuant to a separation from service —

(i) In general. In the case of any service provider who is a specified employee (as defined in § 1.409A-1(i)) as of the date of a separation from service, the requirements of paragraph (a)(1) of this section permitting a payment upon a separation from service are satisfied only if payments may not be made before the date that is six months after the date of separation from service (or, if earlier than the end of the six-month period, the date of death of the specified employee). For this purpose, a service provider who is not a specified employee as of the date of a separation from service will not be treated as subject to this requirement even if the service provider would have become a specified employee if the service provider had continued to provide services through the next specified employee effective date. Similarly, a service provider who is treated as a specified employee as of the date of a separation from service will be subject to this requirement even if the service provider would not have been treated as a specified employee after the next specified employee effective date had the specified employee continued providing services through the next specified employee effective date. Notwithstanding the foregoing, this paragraph (i)(2)(i) does not apply to a payment made under the circumstances described in paragraph (j)(4)(ii) (domestic relations order), (j)(4)(iii) (conflicts of interest), or (j)(4)(vi) (payment of employment taxes) of this section.

(ii) Application of payment rules to delayed payments. The required delay in payment is met if payments to which a specified employee would otherwise be entitled during the first six months following the date of separation from service are accumulated and paid on the first day of the seventh month following the date of separation from service, or if each payment to which a specified employee is otherwise entitled upon a separation from service is delayed by six months. A service recipient may retain discretion to choose which method will be implemented, provided that no direct or indirect election as to the method may be provided to the service provider. For an affected specified employee, a date upon which the plan or the service recipient designates that the payment will be made after the six-month delay is treated as a fixed payment date for purposes of paragraph (d) of this section once the separation from service has occurred.

(3) Unforeseeable emergency —

(i) Definition. For purposes of §§ 1.409A-1 and 1.409A-2, this section, and §§ 1.409A-4 through 1.409A-6, an unforeseeable emergency is a severe financial hardship to the service provider resulting from an illness or accident of the service provider, the service provider's spouse, the service provider's beneficiary, or the service provider's dependent (as defined in section 152 [26 USCS § 152], without regard to section 152(b)(1), (b)(2), and (d)(1)(B) [26 USCS § 152(b)(1), (b)(2), and (d)(1)(B)]); loss of the service provider's property due to casualty (including the need to rebuild a home following damage to a home not otherwise covered by insurance, for example, not as a result of a natural disaster); or other similar extraordinary and unforeseeable circumstances arising as a result of events beyond the control of the service provider. For example, the imminent foreclosure of or eviction from the service provider's primary residence may constitute an unforeseeable emergency. In addition, the need to pay for medical expenses, including non-refundable deductibles, as well as for the costs of prescription drug medication, may constitute an unforeseeable emergency. Finally, the need to pay for the funeral expenses of a spouse, a beneficiary, or a dependent (as defined in section 152 [26 USCS § 152], without regard to section 152(b)(1), (b)(2), and (d)(1)(B) [26 USCS § 152(b)(1), (b)(2), and (d)(1)(B)]) may also constitute an unforeseeable emergency. Except as otherwise provided in this paragraph (i)(3)(i), the purchase of a home and the payment of college tuition are not unforeseeable emergencies. Whether a service provider is faced with an unforeseeable emergency permitting a distribution under this paragraph (i)(3)(i) is to be determined based on the relevant facts and circumstances of each case, but, in any case, a distribution on account of unforeseeable emergency may not be made to the extent that such emergency is or may be relieved through reimbursement or compensation from insurance or otherwise, by liquidation of the service provider's assets, to the extent the liquidation of such assets would not cause severe financial hardship, or by cessation of deferrals under the plan. A plan may provide for a payment upon a specific type or types of unforeseeable emergency, without providing for payment upon all unforeseeable emergencies, provided that any event upon which a payment may be made qualifies as an unforeseeable emergency.

(ii) Amount of payment permitted upon an unforeseeable emergency. Distributions because of an unforeseeable emergency must be limited to the amount reasonably necessary to satisfy the emergency need (which may include amounts necessary to pay any Federal, state, local, or foreign income taxes or penalties reasonably anticipated to result from the distribution). Determinations of amounts reasonably necessary to satisfy the emergency need must take into account any additional compensation that is available if the plan provides for cancellation of a deferral election upon a payment due to an unforeseeable emergency. See paragraph (j)(4)(viii) of this section. However, the determination of amounts reasonably necessary to satisfy the emergency need is not required to take into account any additional compensation that is available from a qualified employer plan as defined in § 1.409A-1(a)(2) (including any amount available by obtaining a loan under the plan), or that due to the unforeseeable emergency is available under another nonqualified deferred compensation plan (including a plan that would provide for deferred compensation except due to the application of the effective date provisions under § 1.409A-6). The payment may be made from any plan in which the service provider participates that provides for payment upon an unforeseeable emergency, provided that the plan under which the payment was made must be designated at the time of payment.

(iii) Payments due to an unforeseeable emergency. A service provider may retain discretion with respect to whether to apply for a payment upon an unforeseeable emergency, and a service recipient may retain

discretion with respect to whether to make a payment available under the plan due to an unforeseeable emergency. A service provider who has experienced an unforeseeable emergency will not be treated as making a subsequent deferral election under § 1.409A-2(b) (subsequent deferral election rules) if the service provider does not apply for or elect to receive a payment available under the plan. A service recipient will not be treated as making a subsequent deferral election under § 1.409A-2(b) (subsequent deferral election rules) if the service recipient exercises its discretion not to make a payment otherwise available due to an unforeseeable emergency.

(4) Disability —

(i) In general. For purposes of §§ 1.409A-1 and 1.409A-2, this section, and §§ 1.409A-4 through 1.409A-6, except as otherwise specifically provided, a service provider is considered disabled if the service provider meets one of the following requirements:

(A) The service provider is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment that can be expected to result in death or can be expected to last for a continuous period of not less than 12 months.

(B) The service provider is, by reason of any medically determinable physical or mental impairment that can be expected to result in death or can be expected to last for a continuous period of not less than 12 months, receiving income replacement benefits for a period of not less than three months under an accident and health plan covering employees of the service provider's employer.

(ii) Limited plan definition of disability. A plan may provide for a payment upon any disability, and need not provide for a payment upon all disabilities, provided that any disability upon which a payment may be made under the plan complies with the provisions of this paragraph (i)(4).

(iii) Determination of disability. A plan may provide that a service provider will be deemed disabled if determined to be totally disabled by the Social Security Administration or Railroad Retirement Board. A plan may also provide that a service provider will be deemed disabled if determined to be disabled in accordance with a disability insurance program, provided that the definition of disability applied under such disability insurance program complies with the requirements of this paragraph (i)(4).

(5) Change in the ownership or effective control of a corporation, or a change in the ownership of a substantial portion of the assets of a corporation —

(i) In general. Pursuant to section 409A(a)(2)(A)(v) [26 USCS § 409A(a)(2)(A)(v)], a plan may permit a payment upon the occurrence of a change in the ownership of the corporation (as defined in paragraph (i)(5)(v) of this section), a change in effective control of the corporation (as defined in paragraph (i)(5)(vi) of this section), or a change in the ownership of a substantial portion of the assets of the corporation (as defined in paragraph (i)(5)(vii) of this section) (collectively referred to as a change in control event). To qualify as a change in control event, the occurrence of the event must be objectively determinable and any requirement that any other person or group, such as a plan administrator or compensation committee, certify the occurrence of a change in control event must be strictly ministerial and not involve any discretionary authority. The plan may provide for a payment on a particular type or types of change in control events, and need not provide for a payment on all such events, provided that each event upon which a payment is provided qualifies as a change in control event. For rules regarding the ability of the service recipient to terminate the plan and pay amounts of deferred compensation upon a change in control event, see paragraph (j)(4)(ix)(B) of this section.

(ii) Identification of relevant corporation —

(A) In general. To constitute a change in control event with respect to the service provider, the change in control event must relate to—

(1) The corporation for whom the service provider is performing services at the time of the change in control event;

(2) The corporation that is liable for the payment of the deferred compensation (or all corporations liable for the payment if more than one corporation is liable) but only if either the deferred compensation is attributable to the performance of service by the service provider for such corporation (or corporations) or there is a bona fide business purpose for such corporation or corporations to be liable for such payment and, in either case, no significant purpose of making such corporation or corporations liable for such payment is the avoidance of Federal income tax; or

(3) A corporation that is a majority shareholder of a corporation identified in paragraph (i)(5)(ii)(A)(1) or (2) of this section, or any corporation in a chain of corporations in which each corporation is a majority shareholder of another corporation in the chain, ending in a corporation identified in paragraph (i)(5)(ii)(A)(1) or (2) of this section.

(B) Majority shareholder. For purposes of this paragraph (i)(5)(ii), a majority shareholder is a shareholder owning more than 50 percent of the total fair market value and total voting power of such corporation.

(C) Example. The following example illustrates the rules of this paragraph (i)(5)(ii):

Example.

Corporation A is a majority shareholder of Corporation B, which is a majority shareholder of Corporation C. A change in ownership of Corporation B constitutes a change in control event to service providers performing services for Corporation B or Corporation C, and to service providers for which Corporation B or Corporation C is solely liable for payments under the plan (for example, former employees), but is not a change in control event as to Corporation A or any other corporation of which Corporation A is a majority shareholder unless the sale constitutes a change in the ownership of a substantial portion of Corporation A's assets (see paragraph (i)(5)(vii) of this section).

(iii) Attribution of stock ownership. For purposes of paragraph (i)(5) of this section, section 318(a) [26 USCS § 318(a)] applies to determine stock ownership. Stock underlying a vested option is considered owned by the individual who holds the vested option (and the stock underlying an unvested option is not considered owned by the individual who holds the unvested option). For purposes of the preceding sentence, however, if a vested option is exercisable for stock that is not substantially vested (as defined by § 1.83-3(b) and (j)), the stock underlying the option is not treated as owned by the individual who holds the option.

(iv) Special rules for certain delayed payments pursuant to a change in control event —

(A) Certain transaction-based compensation. Payments of compensation related to a change in control event described in paragraph (i)(5)(v) of this section (change in the ownership of a corporation) or paragraph (i)(5)(vii) of this section (change in the ownership of a substantial portion of a corporation's assets), that occur because a service recipient purchases its stock held by the service provider or because the service recipient or a third party purchases a stock right held by a service provider, or that are calculated by reference to the value of stock of the service recipient (collectively, transaction-based compensation), may be treated as paid at a designated date or pursuant to a payment schedule that complies with the requirements of section 409A [26 USCS § 409A] if the transaction-based compensation is paid on the same schedule and under the same terms and conditions as apply to payments to shareholders generally with respect to stock of the service recipient pursuant to a change in control event described in paragraph (i)(5)(v) of this section (change in the ownership of a corporation) or as apply to payments to the service recipient pursuant to a change in control event described in paragraph (i)(5)(vii) of this section (change in the ownership of a substantial portion of a corporation's assets), and to the extent that the transaction-based compensation is paid not later than five years after the change in control event, the payment of such compensation will not violate the initial or subsequent deferral election rules set out in § 1.409A-2(a) and (b) solely as a result of such transaction-based compensation being paid pursuant to such schedule and terms and conditions. If before and in connection with a change in control event described in paragraph (i)(5)(v) or (i)(5)(vii) of this section, transaction-based compensation that would otherwise be payable as a result of such event is made subject to a condition on payment that constitutes a substantial risk of forfeiture (as defined in § 1.409A-1(d),

without regard to the provisions of that section under which additions or extensions of forfeiture conditions are disregarded) and the transaction-based compensation is payable under the same terms and conditions as apply to payments made to shareholders generally with respect to stock of the service recipient pursuant to a change in control event described in paragraph (i)(5)(v) of this section or to payments to the service recipient pursuant to a change in control event described in paragraph (i)(5)(vii) of this section, for purposes of determining whether such transaction-based compensation is a short-term deferral the requirements of § 1.409A-1(b)(4) are applied as if the legally binding right to such transaction-based compensation arose on the date that it became subject to such substantial risk of forfeiture.

(B) Certain nonvested compensation. Notwithstanding the provisions of § 1.409A-1(d) (definition of a substantial risk of forfeiture) that disregard the extension or modification of a condition for purposes of determining whether a condition on payment constitutes a substantial risk of forfeiture, a condition that is a substantial risk of forfeiture that otherwise would lapse as a result of a change in control event described in paragraph (i)(5)(v) or (i)(5)(vii) of this section may be extended or modified before and in connection with such event to provide for a condition on payment that will not lapse as a result of such change in control event, and such extended or modified condition will be treated as continuing to subject the amount to a substantial risk of forfeiture, provided that the transaction constituting the change in control event is a bona fide arm's length transaction between the service recipient or its shareholders and one or more parties who are unrelated to the service recipient and service provider (applying the rules of § 1.409A-1(f)(2)(ii) and the modified or extended condition to which the payment is subject would otherwise be treated as a substantial risk of forfeiture under § 1.409A-1(d) (without regard to the provisions disregarding additions or extensions of forfeiture conditions). In such a case, the continued application of a fixed schedule of payments based upon the lapse of the substantial risk of forfeiture, so that payments commence upon the lapse of the modified or extended condition on payment, will not be treated as a change in the fixed schedule of payments for purposes of § 1.409A-2(b) (subsequent deferral elections) or paragraph (j) of this section (prohibition on the acceleration of payments).

(v) Change in the ownership of a corporation —

(A) In general. Except as provided in paragraph (i)(5)(vi)(C) of this section, a change in the ownership of a corporation occurs on the date that any one person, or more than one person acting as a group (as defined in paragraph (i)(5)(v)(B) of this section), acquires ownership of stock of the corporation that, together with stock held by such person or group, constitutes more than 50 percent of the total fair market value or total voting power of the stock of such corporation. A nonqualified deferred compensation plan may provide that amounts payable upon a change in the ownership of a corporation will be paid only if the conditions in the preceding sentence are satisfied but substituting a percentage specified in the plan that is higher than 50 percent for the words "50 percent" in the preceding sentence, but only if the provision is set forth in the plan no later than the date by which the time and form of payment must be established under § 1.409A-2. However, if any one person, or more than one person acting as a group, is considered to own more than 50 percent of the total fair market value or total voting power of the stock of a corporation (or such higher percentage specified in accordance with the preceding sentence), the acquisition of additional stock by the same person or persons is not considered to cause a change in the ownership of the corporation (or to cause a change in the effective control of the corporation (within the meaning of paragraph (i)(5)(vi) of this section)). An increase in the percentage of stock owned by any one person, or persons acting as a group, as a result of a transaction in which the corporation acquires its stock in exchange for property will be treated as an acquisition of stock for purposes of this section. This section applies only when there is a transfer of stock of a corporation (or issuance of stock of a corporation) and stock in such corporation remains outstanding after the transaction (see paragraph (i)(5)(vii) of this section for rules regarding the transfer of assets of a corporation). See § 1.280G-1, Q&A-27(d), Example 1, Example 2, Example 5, and Example 6.

(B) Persons acting as a group. For purposes of paragraph (i)(5)(v)(A) of this section, persons will not be considered to be acting as a group solely because they purchase or own stock of the same corporation at

the same time, or as a result of the same public offering. However, persons will be considered to be acting as a group if they are owners of a corporation that enters into a merger, consolidation, purchase or acquisition of stock, or similar business transaction with the corporation. If a person, including an entity, owns stock in both corporations that enter into a merger, consolidation, purchase or acquisition of stock, or similar transaction, such shareholder is considered to be acting as a group with other shareholders only with respect to the ownership in that corporation before the transaction giving rise to the change and not with respect to the ownership interest in the other corporation. See § 1.280G-1, Q&A-27(d), Example 3 and Example 4.

(vi) Change in the effective control of a corporation —

(A) In general. Notwithstanding that a corporation has not undergone a change in ownership under paragraph (i)(5)(v) of this section, a change in the effective control of the corporation occurs only on either of the following dates:

(1) The date any one person, or more than one person acting as a group (as determined under paragraph (i)(5)(v)(B) of this section), acquires (or has acquired during the 12-month period ending on the date of the most recent acquisition by such person or persons) ownership of stock of the corporation possessing 30 percent or more of the total voting power of the stock of such corporation. A nonqualified deferred compensation plan may provide that amounts payable upon an effective change in control of a corporation will be paid only if the conditions in the preceding sentence are satisfied but substituting a percentage specified in the plan that is higher than 30 percent for the word “30 percent” in the preceding sentence, but only if the percentage is set forth in the plan no later than the date by which the time and form of payment must be established under § 1.409A-2).

(2) The date a majority of members of the corporation’s board of directors is replaced during any 12-month period by directors whose appointment or election is not endorsed by a majority of the members of the corporation’s board of directors before the date of the appointment or election, provided that for purposes of this paragraph (i)(5)(vi)(A) the term corporation refers solely to the relevant corporation identified in paragraph (i)(5)(ii) of this section for which no other corporation is a majority shareholder for purposes of that paragraph. For example, if Corporation A is a publicly held corporation with no majority shareholder, and Corporation A is the majority shareholder of Corporation B, which is the majority shareholder of Corporation C, the term corporation for purposes of this paragraph (i)(5)(vi)(A)(2) would refer solely to Corporation A. A nonqualified deferred compensation plan may provide that amounts payable upon a change in the effective control of a corporation will be paid only if the conditions in the first sentence of this paragraph are satisfied substituting a portion of the members of the corporation’s board of directors that is higher than the words “a majority of the members of the corporation’s board of directors” in the first sentence of this paragraph, but only if the higher portion is set forth in the plan no later than the date by which the time and form of payment must be established under § 1.409A-2(a)).

(B) Multiple change in control events. A change in effective control may occur in a transaction in which one of the two corporations involved in the transaction has a change in control event under paragraph (i)(5)(v) or (i)(5)(vii) of this section. Thus, for example, assume Corporation P transfers more than 40 percent of the total gross fair market value of its assets to Corporation O in exchange for 35 percent of O’s stock. P has undergone a change in ownership of a substantial portion of its assets under paragraph (i)(5)(vii) of this section and O has a change in effective control under this paragraph (i)(5)(vi).

(C) Acquisition of additional control. If any one person, or more than one person acting as a group, is considered to effectively control a corporation (within the meaning of this paragraph (i)(5)(vi)), the acquisition of additional control of the corporation by the same person or persons is not considered to cause a change in the effective control of the corporation (or to cause a change in the ownership of the corporation within the meaning of paragraph (i)(5)(v) of this section).

(D) Persons acting as a group. Persons will not be considered to be acting as a group solely because they purchase or own stock of the same corporation at the same time, or as a result of the same public offering. However, persons will be considered to be acting as a group if they are owners of a corporation that enters into a merger, consolidation, purchase or acquisition of stock, or similar business transaction with the

corporation. If a person, including an entity, owns stock in both corporations that enter into a merger, consolidation, purchase or acquisition of stock, or similar transaction, such shareholder is considered to be acting as a group with other shareholders in a corporation only with respect to the ownership in that corporation before the transaction giving rise to the change and not with respect to the ownership interest in the other corporation. See § 1.280G-1, Q&A-27(d), Example 4.

(vii) Change in the ownership of a substantial portion of a corporation's assets —

(A) In general. A change in the ownership of a substantial portion of a corporation's assets occurs on the date that any one person, or more than one person acting as a group (as determined in paragraph (i)(5)(v)(B) of this section), acquires (or has acquired during the 12- month period ending on the date of the most recent acquisition by such person or persons) assets from the corporation that have a total gross fair market value equal to or more than 40 percent of the total gross fair market value of all of the assets of the corporation immediately before such acquisition or acquisitions (or such higher amount specified by the plan no later than the date by which the time and form of payment must be established under § 1.409A-2). For this purpose, gross fair market value means the value of the assets of the corporation, or the value of the assets being disposed of, determined without regard to any liabilities associated with such assets.

(B) Transfers to a related person —

(1) There is no change in control event under this paragraph (i)(5)(vii) when there is a transfer to an entity that is controlled by the shareholders of the transferring corporation immediately after the transfer, as provided in this paragraph (i)(5)(vii)(B). A transfer of assets by a corporation is not treated as a change in the ownership of such assets if the assets are transferred to—

- (i)** A shareholder of the corporation (immediately before the asset transfer) in exchange for or with respect to its stock;
- (ii)** An entity, 50 percent or more of the total value or voting power of which is owned, directly or indirectly, by the corporation;
- (iii)** A person, or more than one person acting as a group, that owns, directly or indirectly, 50 percent or more of the total value or voting power of all the outstanding stock of the corporation; or
- (iv)** An entity, at least 50 percent of the total value or voting power of which is owned, directly or indirectly, by a person described in paragraph (i)(5)(vii)(B)(1)(iii) of this section.

(2) For purposes of this paragraph (i)(5)(vii)(B) and except as otherwise provided in this paragraph (i), a person's status is determined immediately after the transfer of the assets. For example, a transfer to a corporation in which the transferor corporation has no ownership interest before the transaction, but that is a majority-owned subsidiary of the transferor corporation after the transaction is not treated as a change in the ownership of the assets of the transferor corporation.

(C) Persons acting as a group. Persons will not be considered to be acting as a group solely because they purchase assets of the same corporation at the same time. However, persons will be considered to be acting as a group if they are owners of a corporation that enters into a merger, consolidation, purchase or acquisition of assets, or similar business transaction with the corporation. If a person, including an entity shareholder, owns stock in both corporations that enter into a merger, consolidation, purchase or acquisition of assets, or similar transaction, such shareholder is considered to be acting as a group with other shareholders in a corporation only to the extent of the ownership in that corporation before the transaction giving rise to the change and not with respect to the ownership interest in the other corporation. See § 1.280G-1, Q&A-27(d), Example 4.

(6) Certain back-to-back arrangements —

(i) In general. This paragraph (i)(6) applies where a service provider is providing services to a service recipient (the intermediate service recipient), who in turn is providing services to another service recipient (the ultimate service recipient), the services provided by the service provider to the intermediate service

recipient are closely related to the services provided by the intermediate service recipient to the ultimate service recipient, there is a nonqualified deferred compensation plan providing for payments by the ultimate service recipient to the intermediate service recipient (the ultimate service recipient plan), there is a nonqualified deferred compensation plan or other agreement, method, program, or other arrangement providing for payments of compensation by the intermediate service recipient to the service provider (the intermediate service recipient plan), and the intermediate service recipient plan provides for a payment upon the occurrence of an event described in paragraph (a)(1), (2), (3), (5), or (6) of this section. In such a case, notwithstanding the generally applicable limits on payments in paragraph (a) of this section, the ultimate service recipient plan may provide for a payment to the intermediate service recipient upon the occurrence of a payment event under the intermediate service recipient plan described in paragraph (a)(1), (2), (3), (5), or (6) of this section if the time and form of payment is defined as the same time and form of payment provided under the intermediate service recipient plan, the amount of the payment under the ultimate service recipient plan does not exceed the amount of the payment under the intermediate service recipient plan, and the ultimate service recipient plan and the intermediate service recipient plan otherwise satisfy the requirements of section 409A [26 USCS § 409A] (regardless of whether such plan is subject to section 409A [26 USCS § 409A]).

(ii) Example. The provisions of paragraph (i)(6)(i) of this section are illustrated by the following example:
Example.

Company B (intermediate service recipient) provides services to Company C (ultimate service recipient). Employee A (service provider) provides services to Company B that are closely related to the services Company B provides to Company C. Pursuant to a nonqualified deferred compensation plan meeting the requirements of section 409A [26 USCS § 409A], Employee A is entitled to a payment of deferred compensation upon a separation from service with Company B (the intermediate service recipient plan). Under an arrangement between Company B and Company C (the ultimate service recipient plan), Company C agrees to pay an amount of deferred compensation to Company B upon Employee A's separation from service with Company B, in accordance with the time, form and amount of payment provided in the intermediate service recipient plan. Provided that the intermediate service recipient plan and the ultimate service recipient plan otherwise comply with the requirements of section 409A [26 USCS § 409A] (regardless of whether such arrangements are subject to section 409A [26 USCS § 409A]), Company C's payment to Company B of the amount due under the ultimate service recipient plan upon the separation from service of Employee A from Company B may constitute a permissible payment event for purposes of paragraph (a) of this section.

(j) Prohibition on acceleration of payments —

(1) In general. Except as provided in paragraph (j)(4) of this section, a nonqualified deferred compensation plan may not permit the acceleration of the time or schedule of any payment or amount scheduled to be paid pursuant to the terms of the plan, and no such accelerated payment may be made whether or not provided for under the terms of such plan. For purposes of determining whether a payment of deferred compensation has been made, the rules of paragraph (f) of this section (substituted payments) apply. For purposes of this paragraph (j), an impermissible acceleration does not occur if payment is made in accordance with plan provisions or an election as to the time and form of payment in effect at the time of initial deferral (or added in accordance with the rules applicable to subsequent deferral elections under § 1.409A-2(b)) pursuant to which payment is required to be made on an accelerated schedule as a result of an intervening event that is an event described in paragraph (a)(1), (2), (3), (5), or (6) of this section. For example, a plan may provide that a participant will receive six installment payments commencing at separation from service, and also provide that if the participant dies after such payments commence but before all payments have been made, all remaining amounts will be paid in a lump sum payment. Additionally, it is not an acceleration of the time or schedule of payment of a deferral of compensation if a service recipient waives or accelerates the satisfaction of a condition constituting a substantial risk of forfeiture applicable to such deferral of compensation, provided that the requirements of section 409A [26 USCS § 409A] (including the requirement that the payment be made upon a permissible payment event) are otherwise satisfied with respect to such deferral of compensation. For example, if a nonqualified deferred compensation plan provides for a lump

sum payment of the vested benefit upon separation from service, and the benefit vests under the plan only after 10 years of service, it is not a violation of the requirements of section 409A [26 USCS § 409A] if the service recipient reduces the vesting requirement to five years of service, even if a service provider becomes vested as a result and receives a payment in connection with a separation from service before the service provider would have completed 10 years of service. However, if the plan in this example had provided for a payment at a fixed date, rather than at separation from service, the date of payment could not be accelerated due to the accelerated vesting. For the definition of a payment for purposes of this paragraph (j), see § 1.409A-2(b)(5) (coordination of the subsequent deferral election rules with the prohibition on acceleration of payments). For other permissible payments, see § 1.409A-2(b)(2)(iii) (certain immediate payments of remaining installments) and paragraph (d) of this section (certain payments made no more than 30 days before the designated payment date).

(2) Application to multiple payment events. Generally, the addition of a permissible payment event, the deletion of a permissible payment event, or the substitution of one permissible payment event for another permissible payment event, results in an acceleration of a payment if the addition, deletion, or substitution could result in the payment being made at an earlier date than such payment would have been made absent such addition, deletion, or substitution. Notwithstanding the previous sentence, the addition of death, disability (as defined in paragraph (i)(4) of this section), or an unforeseeable emergency (as defined in paragraph (i)(3) of this section), as a potentially earlier alternative payment event to an amount previously deferred will not be treated as resulting in an acceleration of a payment, even if such addition results in the payment being paid at an earlier time than such payment would have been made absent the addition of the payment event. However, the addition of such a payment event as a potentially later alternative payment event generally is subject to the rules governing changes in the time and form of payment (see § 1.409A-2(b)).

(3) Beneficiaries. The rules of this paragraph (j) apply to elections by beneficiaries with respect to the time and form of payment, as well as elections by service providers or service recipients with respect to the time and form of payment to beneficiaries. An election to change the identity of a beneficiary does not constitute an acceleration of a payment merely because the election changes the identity of the recipient of the payment, if the time and form of the payment is not otherwise changed. In addition, an election before the commencement of a life annuity to change the identity of a beneficiary does not constitute an acceleration of a payment if the change in the time of payments stems solely from the different life expectancy of the new beneficiary, such as in the case of a joint and survivor annuity, and does not change the commencement date of the life annuity.

(4) Exceptions —

(i) In general. Except as otherwise expressly provided, a plan may provide for the acceleration of a payment in accordance with paragraphs (j)(4)(ii) through (xiv) of this section, or may provide a service recipient discretion to accelerate payments in accordance with the provisions of paragraphs (j)(4)(ii) through (xiv) of this section. A plan may not provide a service provider discretion with respect to whether a payment will be accelerated, and a service recipient may not provide a service provider a direct or indirect election as to whether the service recipient's discretion to accelerate a payment will be exercised, even if such acceleration would be permitted under paragraphs (j)(4)(ii) through (xiv) of this section. Whether a service recipient has provided a service provider an election as to whether the service recipient's discretion to accelerate a payment will be exercised is determined based on all the facts and circumstances, including whether similarly situated service providers have been treated differently. Except as otherwise provided in paragraphs (j)(4)(ii) through (xiv) of this section, the plan need not set forth the exception in writing, and provided all other requirements of this section are met, the making of such a payment or the addition of a plan term permitting the making of such a payment will not constitute the acceleration of a payment, and the failure to make such a payment or the deletion or modification of a plan term permitting the making of such a payment will not be subject to the rules regarding a change in the time and form of payment under § 1.409A-2(b).

(ii) Domestic relations order. A plan may provide for acceleration of the time or schedule of a payment under the plan to an individual other than the service provider, or a payment under such plan may be made to an individual other than the service provider, to the extent necessary to fulfill a domestic relations order (as defined in section 414(p)(1)(B) [26 USCS § 414(p)(1)(B)]).

(iii) Conflicts of interest —

(A) Compliance with ethics agreements with the Federal government. A plan may provide for acceleration of the time or schedule of a payment under the plan, or a payment may be made under a plan, to the extent necessary for any Federal officer or employee in the executive branch to comply with an ethics agreement with the Federal government.

(B) Compliance with ethics laws or conflicts of interest laws. A plan may provide for acceleration of the time or schedule of a payment under the plan, or a payment may be made under a plan, to the extent reasonably necessary to avoid the violation of an applicable Federal, state, local, or foreign ethics law or conflicts of interest law (including where such payment is reasonably necessary to permit the service provider to participate in activities in the normal course of his or her position in which the service provider would otherwise not be able to participate under an applicable rule). A payment is reasonably necessary to avoid the violation of a Federal, state, local, or foreign ethics law or conflicts of interest law if the payment is a necessary part of a course of action that results in compliance with a Federal, state, local, or foreign ethics law or conflicts of interest law that would be violated absent such course of action, regardless of whether other actions would also result in compliance with the Federal, state, local, or foreign ethics law or conflicts of interest law. For this purpose, a provision of foreign law is considered applicable only to foreign earned income (as defined under section 911(b)(1) [26 USCS § 911(b)(1)] without regard to section 911(b)(1)(B)(iv) [26 USCS § 911(b)(1)(B)(iv)] and without regard to the requirement that the income be attributable to services performed during the period described in section 911(d)(1)(A) or (B) [26 USCS § 911(d)(1)(A) or (B)]) from sources within the foreign country that promulgated such law.

(iv) Section 457 plans [26 USCS § 457]. A plan subject to section 457(f) [26 USCS § 457(f)] may provide for an acceleration of the time or schedule of a payment to a service provider, or a payment may be made under such a plan, to pay Federal, state, local, and foreign income taxes due upon a vesting event, provided that the amount of such payment is not more than an amount equal to the Federal, state, local, and foreign income tax withholding that would have been remitted by the employer if there had been a payment of wages equal to the income includible by the service provider under section 457(f) [26 USCS § 457(f)] at the time of the vesting.

(v) Limited cashouts. A plan may require or provide a service recipient discretion to require (or be amended to require or to provide a service recipient discretion to require), a mandatory lump sum payment of amounts deferred under the plan that do not exceed a specified amount, provided that such plan term or amendment is executed and effective, and any required exercise of service recipient discretion is evidenced in writing, no later than the date of such payment, and provided that—

(A) The payment results in the termination and liquidation of the entirety of the service provider's interest under the plan, including all agreements, methods, programs, or other arrangements with respect to which deferrals of compensation are treated as having been deferred under a single nonqualified deferred compensation plan under § 1.409A-1(c)(2); and

(B) The payment is not greater than the applicable dollar amount under section 402(g)(1)(B) [26 USCS § 402(g)(1)(B)].

(vi) Payment of employment taxes. A plan may provide for the acceleration of the time or schedule of a payment, or a payment may be made under the plan, to pay the Federal Insurance Contributions Act (FICA) tax imposed under section 3101 [26 USCS § 3101], section 3121(a) [26 USCS § 3121(a)], and section 3121(v)(2) [26 USCS § 3121(v)(2)], or the Railroad Retirement Act tax imposed under section 3201 [26 USCS § 3201], section 3211 [26 USCS § 3211], section 3231(e)(1) [26 USCS § 3231(e)(1)], and section 3231(e)(8) [26 USCS § 3231(e)(8)], where applicable, on compensation deferred under the plan (the FICA or RRTA amount). Additionally, a plan may provide for the acceleration of the time or schedule of a payment, or a payment may be made under the plan, to pay the income tax at source on wages imposed under section 3401 [26 USCS § 3401] or the corresponding withholding provisions of applicable state, local, or foreign tax

laws as a result of the payment of the FICA or RRTA amount, and to pay the additional income tax at source on wages attributable to the pyramiding section 3401 [26 USCS § 3401] wages and taxes. However, the total payment under this acceleration provision must not exceed the aggregate of the FICA or RRTA amount, and the income tax withholding related to such FICA or RRTA amount.

(vii) Payment upon income inclusion under section 409A [26 USCS § 409A]. A plan may provide for the acceleration of the time or schedule of a payment, or a payment under such plan may be made, at any time the plan fails to meet the requirements of section 409A [26 USCS § 409A] and these regulations. Such payment may not exceed the amount required to be included in income as a result of the failure to comply with the requirements of section 409A [26 USCS § 409A] and these regulations.

(viii) Cancellation of deferrals following an unforeseeable emergency or hardship distribution. A plan may provide for a cancellation of a service provider's deferral election, or such a cancellation may be made, due to an unforeseeable emergency or a hardship distribution pursuant to § 1.401(k)-1(d)(3). The deferral election must be cancelled, not merely postponed or otherwise delayed. Accordingly, any later deferral election will be subject to the provisions governing initial deferral elections. See § 1.409A-2(a).

(ix) Plan terminations and liquidations. A plan may provide for the acceleration of the time and form of a payment, or a payment under such plan may be made, where the acceleration of the payment is made pursuant to a termination and liquidation of the plan in accordance with one of the following:

(A) The service recipient's termination and liquidation of the plan within 12 months of a corporate dissolution taxed under section 331 [26 USCS § 331], or with the approval of a bankruptcy court pursuant to 11 U.S.C. § 503(b)(1)(A), provided that the amounts deferred under the plan are included in the participants' gross incomes in the latest of the following years (or, if earlier, the taxable year in which the amount is actually or constructively received).

(1) The calendar year in which the plan termination and liquidation occurs.

(2) The first calendar year in which the amount is no longer subject to a substantial risk of forfeiture.

(3) The first calendar year in which the payment is administratively practicable.

(B) The service recipient's termination and liquidation of the plan pursuant to irrevocable action taken by the service recipient within the 30 days preceding or the 12 months following a change in control event (as defined in paragraph (i)(5) of this section), provided that this paragraph will only apply to a payment under a plan if all agreements, methods, programs, and other arrangements sponsored by the service recipient immediately after the time of the change in control event with respect to which deferrals of compensation are treated as having been deferred under a single plan under § 1.409A-1(c)(2) are terminated and liquidated with respect to each participant that experienced the change in control event, so that under the terms of the termination and liquidation all such participants are required to receive all amounts of compensation deferred under the terminated agreements, methods, programs, and other arrangements within 12 months of the date the service recipient irrevocably takes all necessary action to terminate and liquidate the agreements, methods, programs, and other arrangements. Solely for purposes of this paragraph (j)(4)(ix)(B), the applicable service recipient with the discretion to liquidate and terminate the agreements, methods, programs, and other arrangements is the service recipient that is primarily liable immediately after the transaction for the payment of the deferred compensation.

(C) The service recipient's termination and liquidation of the plan, provided that—

(1) The termination and liquidation does not occur proximate to a downturn in the financial health of the service recipient;

(2) The service recipient terminates and liquidates all agreements, methods, programs, and other arrangements sponsored by the service recipient that would be aggregated with any terminated and liquidated agreements, methods, programs, and other arrangements under § 1.409A-1(c) if the same service provider had deferrals of compensation under all of the agreements, methods, programs, and other arrangements that are terminated and liquidated;

- (3) No payments in liquidation of the plan are made within 12 months of the date the service recipient takes all necessary action to irrevocably terminate and liquidate the plan other than payments that would be payable under the terms of the plan if the action to terminate and liquidate the plan had not occurred;
- (4) All payments are made within 24 months of the date the service recipient takes all necessary action to irrevocably terminate and liquidate the plan; and
- (5) The service recipient does not adopt a new plan that would be aggregated with any terminated and liquidated plan under § 1.409A-1(c) if the same service provider participated in both plans, at any time within three years following the date the service recipient takes all necessary action to irrevocably terminate and liquidate the plan.

(D) Such other events and conditions as the Commissioner may prescribe in generally applicable guidance published in the Internal Revenue Bulletin (see § 601.601(d)(2) of this chapter).

(x) Certain distributions to avoid a nonallocation year under section 409(p) [26 USCS § 409(p)]. A plan may provide for an acceleration of the time and form of a payment, or a payment may be made under such plan, to prevent the occurrence of a nonallocation year (within the meaning of section 409(p)(3) [26 USCS § 409(p)(3)]) in the plan year of an employee stock ownership plan next following the plan year in which such payment is made, provided that the amount distributed may not exceed 125 percent of the minimum amount of distribution necessary to avoid the occurrence of a nonallocation year. Solely for purposes of determining permissible distributions under this paragraph (j)(4)(x), synthetic equity (within the meaning of section 409(p)(6)(C) [26 USCS § 409(p)(6)(C)] and § 1.409(p)-1(f)) granted during the plan year of the employee stock ownership plan in which such payment is made is disregarded for purposes of determining whether the subsequent plan year would result in a nonallocation year.

(xi) Payment of state, local, or foreign taxes. A plan may provide for an acceleration of the time and form of a payment, or a payment may be made under such plan, to reflect payment of state, local, or foreign tax obligations arising from participation in the plan that apply to an amount deferred under the plan before the amount is paid or made available to the participant (the state, local, or foreign tax amount). Such payment may not exceed the amount of such taxes due as a result of participation in the plan. Such payment may be made by distributions to the participant in the form of withholding pursuant to provisions of applicable state, local, or foreign law or by distribution directly to the participant. Additionally, an arrangement may provide for the acceleration of the time or schedule of payment, or a payment may be made under such arrangement, to pay the income tax at source on wages imposed under section 3401 [26 USCS § 3401] as a result of such payment and to pay the additional income tax at source on wages imposed under section 3401 [26 USCS § 3401] attributable to such additional section 3401 [26 USCS § 3401] wages and taxes. However, the total payment under this acceleration provision must not exceed the aggregate of the state, local, and foreign tax amount, and the income tax withholding related to such state, local, and foreign tax amount.

(xii) Cancellation of deferral elections due to disability. A plan may provide for a cancellation of a service provider's deferral election, or a cancellation of such election may be made, where such cancellation occurs by the later of the end of the taxable year of the service provider or the 15th day of the third month following the date the service provider incurs a disability. For purposes of this paragraph, a disability refers to any medically determinable physical or mental impairment resulting in the service provider's inability to perform the duties of his or her position or any substantially similar position, where such impairment can be expected to result in death or can be expected to last for a continuous period of not less than six months.

(xiii) Certain offsets. A plan may provide for the acceleration of the time or schedule of a payment, or a payment may be made under such plan, as satisfaction of a debt of the service provider to the service recipient, where such debt is incurred in the ordinary course of the service relationship

between the service recipient and the service provider, the entire amount of reduction in any of the service recipient's taxable years does not exceed \$ 5,000, and the reduction is made at the same time and in the same amount as the debt otherwise would have been due and collected from the service provider.

(xiv) Bona fide disputes as to a right to a payment. A plan may provide for the acceleration of the time or schedule of one or more payments, or a payment may be made under such plan, where such payments occur as part of a settlement between the service provider and the service recipient of an arm's length, bona fide dispute as to the service provider's right to the deferred amount. Discretion to accelerate payments, other than due to an arm's length settlement of a bona fide dispute as to the service provider's right to the deferred amount, is not permitted under this paragraph (j)(4)(xiv).

Whether a payment qualifies for the exception under this paragraph is based on all relevant facts and circumstances. A payment will be presumed not to meet this exception unless the payment is subject to a substantial reduction in the value of the payment made in relation to the amount that would have been payable had there been no dispute as to the service provider's right to the payment. For this purpose, a reduction that is less than 25 percent of the present value of the deferred amount in dispute generally is not a substantial reduction. In addition, a payment will be presumed not to meet this exception if the payment is made proximate to a downturn in the financial health of the service recipient.

(5) Nonqualified deferred compensation plans linked to qualified employer plans or certain other arrangements. If a nonqualified deferred compensation plan provides that the amount deferred under the plan is the amount determined under the formula determining benefits under a qualified employer plan (as defined in § 1.409A-1(a)(2)), or a broad-based foreign retirement plan (as defined in § 1.409A-1(a)(3)(v)) maintained by the service recipient but applied without regard to one or more limitations applicable to the qualified employer plan under the Internal Revenue Code or to the broad-based foreign retirement plan under other applicable law, or that the amount deferred under the nonqualified deferred compensation plan is determined as an amount offset by some or all of the benefits provided under the qualified employer plan or broad-based foreign retirement plan, a decrease in amounts deferred under the nonqualified deferred compensation plan that results directly from the operation of the qualified employer plan or broad-based foreign retirement plan (other than service provider actions described in paragraphs (j)(5)(iii) and (iv) of this section) including changes in benefit limitations applicable to the qualified employer plan or the broad-based foreign retirement plan under the Internal Revenue Code or other applicable law does not constitute an acceleration of a payment under the nonqualified deferred compensation plan, provided that such operation does not otherwise result in a change in the time or form of a payment under the nonqualified deferred compensation plan, and provided further that the change in the amounts deferred under the nonqualified deferred compensation plan does not exceed such change in the amounts deferred under the qualified employer plan or the broad-based foreign retirement plan, as applicable. In addition, with respect to such a nonqualified deferred compensation plan, the following actions or failures to act will not constitute an acceleration of a payment under the nonqualified deferred compensation plan even if in accordance with the terms of the nonqualified deferred compensation plan, the actions or inactions result in a decrease in the amounts deferred under the plan, provided that such actions or inactions do not otherwise affect the time or form of payment under the nonqualified deferred compensation plan, and provided further that with respect to actions or inactions described in paragraphs (j)(5)(i) and (ii) of this section, the change in the amount deferred under the nonqualified deferred compensation plan does not exceed the change in the amounts deferred under the qualified employer plan or the broad-based foreign retirement plan, as applicable:

(i) A service provider's action or inaction under the qualified employer plan or broad-based foreign retirement plan with respect to whether to elect to receive a subsidized benefit or an ancillary benefit under the qualified employer plan or broad-based foreign retirement plan.

(ii) The amendment of a qualified employer plan or broad-based foreign retirement plan to increase benefits provided under such plan, or to add or remove a subsidized benefit or an ancillary benefit.

(iii) A service provider's action or inaction under a qualified employer plan with respect to elective deferrals and other employee pre-tax contributions subject to the contribution restrictions under section 401(a)(30) [26 USCS § 401(a)(30)] or section 402(g) [26 USCS § 402(g)], including an adjustment to a deferral election under such qualified employer plan, provided that for any given taxable year, the service provider's action or inaction does not result in a decrease in the amounts deferred under all nonqualified deferred compensation plans in which the service provider participates (other than amounts described in paragraph (j)(5)(iv) of this section) in excess of the limit with respect to elective deferrals under section 402(g)(1)(A), (B), and (C) [26 USCS § 402(g)(1)(A), (B), and (C)] in effect for the taxable year in which such action or inaction occurs.

(iv) A service provider's action or inaction under a qualified employer plan with respect to elective deferrals and other employee pre-tax contributions subject to the contributions restrictions under section 401(a)(30) [26 USCS § 401(a)(30)] or section 402(g) [26 USCS § 402(g)], and after-tax contributions by the service provider to a qualified employer plan that provides for such contributions, that affects the amounts that are credited under one or more nonqualified deferred compensation plans as matching amounts or other similar amounts contingent on such elective deferrals, pre-tax contributions, or after-tax contributions, provided that the total of such matching or contingent amounts, as applicable, never exceeds 100 percent of the matching or contingent amounts that would be provided under the qualified employer plan absent any plan-based restrictions that reflect limits on qualified plan contributions under the Internal Revenue Code.

(6) Changes in elections under a cafeteria plan. A change in an election under a cafeteria plan (as defined in section 125(d) [26 USCS § 125(d)]) does not result in an accelerated payment of an amount deferred under a nonqualified deferred compensation plan to the extent that the change in the amount deferred under the nonqualified deferred compensation plan results solely from the application of the change in amount eligible to be treated as compensation under the terms of the nonqualified deferred compensation plan resulting from the election change under the cafeteria plan, to a benefit formula under the nonqualified deferred compensation plan based upon the service provider's eligible compensation, and only to the extent that such change applies in the same manner as any other increase or decrease in compensation would apply to such benefit formula.

Statutory Authority

Authority Note Applicable to 26 CFR Ch. I, Subch. A, Pt. 1

History

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