

April 12, 2012



We continue to enrich our content with crucial updates and practical new articles and FAQs about key NQDC topics. Below are selected additions and updates from the past few months.



New Articles From NQDC Experts

- [Added Protections To Look For In Your Company's Nonqualified Deferred Compensation Plan](#), by **Michael Melbinger**. Participating in your company's NQDC plan can be an excellent way to defer taxes and save for retirement, among other benefits. However, as compensation and benefits attorney Michael Melbinger explains in this article, you need to recognize a few of the key differences between your company's nonqualified deferred compensation plan and its tax-qualified retirement plan.
- [How Bankruptcy Affects Your Nonqualified Deferred Compensation](#), by **Chad R. DeGroot**. One of the biggest risks you face with nonqualified deferred compensation (NQDC) is the possibility of your company's bankruptcy. Unlike 401(k) plans, NQDC plans do not receive ERISA protections, and the funds in the plans are at risk of being included in a company's bankruptcy estate. This article, by attorney Chad DeGroot, addresses some key issues that participants in these plans should know about corporate bankruptcy.
- [Ten Key Features Of Nonqualified Deferred Compensation](#), by **Kenneth A. Dayton**. For retirement savings, a nonqualified deferred compensation (NQDC) plan is one of the few choices for meaningful tax-deferred investing. When properly designed, financed, and administered, NQDC plans can also give your company a cost-effective way to retain and attract talented executives who maximize shareholder value. This article, by consultant Kenneth Dayton, encapsulates 10 compelling reasons in favor of NQDC plans, for both participants and companies.

409A Developments

Our readable collection of FAQs on the [rules of Section 409A](#) reflect the types of questions participants care about. The rules we explain also permeate all aspects of nonqualified deferred compensation. The following 409A developments will be of interest to both professionals and participants.

1. W-2 reporting for NQDC. As we explain in our [FAQ](#) on this topic, the amount of income deferred during the year may be indicated in Box 12 of the W-2 using Code Y once the IRS has issued more guidance on the point. (For income from a 409A violation, [Code Z](#) is currently used.) This guidance—and thus the required W-2 reporting—is not expected for some time, according to Bloomberg BNA's *Compensation Planning Journal*. It seems that the IRS is currently preoccupied with other proposed and final rules, including the [Income Inclusion Regulations](#) that relate to 409A and the penalty calculations

2. IRS audits. According to the newsletter *HRS Insight* by PricewaterhouseCoopers (Mar. 14, 2012), the IRS is "now stepping up its enforcement activity" in 409A compliance for nonqualified plans. Participants will get stuck with [substantial penalties](#) if plans do not comply. Areas of IRS attention include:

- incorrect reliance by companies on the [short-term deferral rule](#) to avoid 409A consequences
- inappropriate identification of [specified employees](#), a point that matters for various purposes, such as the six-month delay in payouts after [employment termination](#)

- documents that do not clearly specify the time and form of payment for deferred amounts, as with an employment agreement's [severance provision](#) allowing an employee to elect a lump-sum or installment distribution at termination

Bankruptcy & Nonqualified Plans

Although bankruptcy is the biggest risk with NQDC plans, there are ways to manage and limit it, as we explain in a thorough [FAQ](#) and [article](#). Below we present updates on two real-world examples of NQDC treatment in corporate bankruptcy.

1. Kodak. Soon after Kodak filed for Chapter 11 bankruptcy, we issued a [special alert](#) on what could happen to the amounts deferred into its nonqualified retirement plan, and on what actions the company and its executives have been taking in relation to the plan during the past several years. Since we published that alert, we have learned that the bankruptcy court has told Kodak to form a retirees' committee for purposes of working out of its large legacy costs, including that of its retiree health care and survivor welfare benefits, and its nonqualified retirement plans. The committee will have about 15 members selected by the trustee from the names submitted to it by Kodak and the independent Eastman Kodak Retirees Association (EKRA). We have heard that the former executives, as unsecured general creditors through their unfunded pensions and elective deferred compensation plans, are concerned that the extremely large health care costs for 30,000 retirees will overshadow the obligations due to 1,000 executives in the nonqualified plans. The bankruptcy court will probably allow only one retirees' committee, so the positioning for influence on it is intense.

2. General Motors. The court case *Tate v. General Motors* reveals some details about the way the company's executive retirement plan (ERP) was handled when the company faced financial difficulties. At GM, if a participant's combined yearly benefit under its qualified pension plan, plus nonqualified plan, was over \$100,000, the benefit under the ERP was reduced by two thirds. Calling it "implausible," the court rejected the executives' interpretation that only ERP benefits should be considered in reaching the \$100,000 threshold.

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The Editorial Team, myNQDC.com



Late October marks one year since the launch of myNQDC.com, the most comprehensive online resource on nonqualified deferred compensation plans. Thank you for your membership. We are honored by the [glowing testimonials](#) we have received about the value of our website and the guidance it has provided for both participants and professionals.

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Alert: Revised Limits For Qualified Plans Also Affect NQDC Plans

Last week, the IRS announced [increases](#) in the amounts that can be contributed during a calendar year to qualified retirement plans, such as 401(k) plans. These changes are the first in a few years. Among the increases taking effect in 2012, the annual maximum you can put into all qualified plans will rise from the current \$49,000 to \$50,000, and the ceiling on annual amounts of compensation that can be considered in the deferral calculation will go up from \$245,000 to \$250,000. The articles and FAQs on myNQDC.com have been updated for all of the [revised limits](#), which will become effective in 2012.

Anyone who wants to contribute or receive more than what is allowed by the revised IRS rules during a single year will need to use a nonqualified deferred compensation plan. One of the major [advantages](#) of NQDC is that you can contribute much higher amounts toward retirement than you can under qualified plans.

Exclusive Articles & FAQs: Selected New Content

With clear writing and independent, unbiased expertise, myNQDC.com will make you smarter about not only the basics of nonqualified deferred comp but also the related financial planning, taxation, risk, and legal issues. Our exclusive articles and FAQs can be found nowhere else. Below are a few of our recent additions.

[Nonqualified Plan Financing Strategies](#). How your company finances its NQDC plan is an important decision with long-lasting consequences. In this article, executive benefit consultants Richard DeVita and Scott Holton (The Todd Organization) evaluate the reasons and available alternatives for financing NQDC plans. They also analyze funding techniques and the related factors to consider.

[Keys To Successful NQDC Plans At Small Companies: A View From The Trenches](#). Nonqualified deferred compensation is not just for big corporations. Small companies can use NQDC plans to offer the same advantages of tax deferral and savings for any highly compensated executive or key employee. In this article, executive benefit consultants Cline Young and Mark Levitats (Gallagher Retirement Services) discuss the special issues a privately held company faces with an elective deferral NQDC plan. Drawing on their experience, they examine real-life challenges facing small employers.

[Rabbi Trusts: Benefits, Features, And Key Considerations.](#) While the use of a rabbi trust can furnish some security for NQDC participants against company insolvency or a corporate change of heart, it presents special concerns about design, administration, and the selection of a trustee/provider. In this article, NQDC expert Michael Hlavin (Wilmington Trust) looks at the rules and the practical considerations.

[My company plans to spin off my division. What can happen to my NQDC plan and my elections for deferrals and distributions?](#) Many of the contingencies for a nonqualified deferred compensation plan depend on the details of the spinoff and on the plan documents. For this new FAQ, we asked the compensation and benefits experts on the myNQDC.com Advisory Board for their input on this situation.

[How do I name a beneficiary who would receive my NQDC account balance if I were to die before getting it?](#) While the ability to name beneficiaries, and your company's rules for doing so, may be the same as in other benefit plans, differences in some areas (including tax treatment) probably exist. This FAQ explains.

[What is a QSERP?](#) A QSERP is one of the names given to the strategy of shifting accrued or future benefits from a SERP to a qualified retirement plan. This twist on the supplemental executive retirement plan (SERP) is explained by this new FAQ, which includes expert technical input from myNQDC.com Advisory Board member Michael Melbinger, an attorney at Winston & Strawn who specializes in executive compensation and benefits.

See myNQDC.com for these additions and other updates.

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Thank you for being a member of myNQDC.com, the most comprehensive online resource on nonqualified deferred compensation plans. The popularity of the website continues to grow among both NQDC professionals and participants. In recent weeks, we have enriched our content with crucial updates and exclusive new articles and FAQs on key NQDC topics.



Selected New Content

[Participant Viewpoint: Tax Strategies With Options & Deferred Compensation.](#)

Having both nonqualified stock options and nonqualified deferred compensation gives you a tremendous amount of flexibility to optimize your financial planning and tax situation. In this article, CPA and NQDC participant Andy Wagner explains how he uses the two plans in concert with one another.

[College Financial Aid & Funding With Nonqualified Deferred Compensation \(Parts 1 and 2\).](#)

In line with our mission to cover all areas of NQDC-related financial planning, this new two-part article by Troy Onink explains the role of NQDC in preparing and paying for the costs of higher education. Mr. Onink, a college-funding expert and *Forbes* blogger, explains in [Part 1](#) the impact NQDC can have on eligibility for financial aid. In [Part 2](#), he discusses the use of the American Opportunity Tax Credit and financial-planning strategies to explore.

[Are there different types of services and fees for rabbi trusts?](#) These vary according to the service capabilities of the trustee and the provisions of the rabbi trust agreement. For this new FAQ, myNQDC.com asked Jeff McCarthy of Deferral.com and Mike Hlavin of Wilmington Trust for their input on this topic. As they explain, the nature of the trust agreement provides for various types of relationships between the trustee and the company, and there are some potential issues to watch for.

[Can I protect my NQDC plan when my company is acquired?](#) Change-in-control transactions (e.g. a merger or acquisition) do raise some risks for nonqualified deferred compensation. While they are not always as severe as the risks arising from corporate bankruptcy, they can create a situation in which your payout may not occur. This FAQ presents a few ways to protect yourself,

including recommendations provided by Winston & Strawn attorney Michael Melbinger, a member of the myNQDC.com advisory board.

[Has the likelihood of a tax audit increased?](#) Fluctuations of income, including sudden increases from NQDC distributions, can be a red flag triggering a dreaded audit by the IRS—especially now. The IRS Data Book has disclosed a large increase in audits among people with adjusted gross income of more than \$500,000 per year, and a particularly big jump for those with income over \$5 million. As this FAQ explains, normally the IRS can perform audits only within a three-year statute of limitations, but in some circumstances it can obtain a six-year statute of limitations for what it believes to be "substantial underreporting of income."

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Selected New Content

[Participant Viewpoint: My Investment And Risk Management Strategies For Nonqualified Deferred Compensation](#). An unusual and insightful perspective on NQDC plans enlivens our new article: **Andy Wagner**, a 25-year veteran of a Fortune 500 company, discusses his approach to NQDC plans and their investment choices, especially the crucial balance between risks and rewards.



[Plan Design Features To Increase Participation In Nonqualified Deferred Compensation Plans](#). Why are some NQDC plans more successful than others? What goes into a winning formula? **William B. MacDonald**, the founder and CEO of Retirement Capital Group in San Diego, shares his extensive experience of NQDC plans in a thoughtful white paper. Learn about NQDC plan features that encourage participation by executives and pay off for the company in the long term by the enhancement of executive loyalty and retention.

[Are severance payouts subject to the same six-month delay as other NQDC payments?](#) Winston & Strawn attorney **Michael Melbinger**, a noted compensation expert, lent us his technical acumen in this crucial new FAQ about [severance plans](#). If the severance plan or agreement provides for compensation that is earned in one year and payable in a later year, it could be subject to the rules of IRC Section 409A. However, Mr. Melbinger points out that the 409A regulations provide several exceptions to payments made upon an involuntary separation from service.

Our editorial team works hard to keep all of our content current. In addition to recent new content, **FAQs with important updates** include:

- [What happens to my NQDC plan in a merger or acquisition?](#) This FAQ explores the recent case involving the asset sale of Rand McNally and ways to protect NQDC in M&A.
- [What if I have a financial or medical hardship? Can I get a distribution?](#) This FAQ examines the newest IRS guidance that applies to NQDC plans.
- [Does ERISA apply to and protect my NQDC plan?](#) Learn the ways in which NQDC plans can and cannot be subject to ERISA rules, and read about a recent court case on this topic.

See the site for these updates and many more.

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