

IRC Section 409A plan aggregation issues

Under Internal Revenue Code Section 409A (IRC Section 409A), each nonqualified deferred compensation arrangement must be “aggregated” with other nonqualified arrangements of the same plan “type” in determining the application of various Code provisions.¹ Employers offering plans subject to IRC Section 409A need to be aware of the effect of the plan aggregation rules and how they can impact the operation of their deferred compensation plans, including provisions regarding:

- IRC Section 409A violations and penalty calculations
- Plan termination provisions
- Plan participant deferral elections upon initial eligibility
- Plan participant separation from service and re-hire issues
- Plan provisions for cash-out distributions

For the operation of these provisions, IRC Section 409A requires that certain types of plans be aggregated, meaning they are considered as one plan and must be aggregated with all other plans of that type. These plan types are.²

- Elective deferral account balance plans (employee deferral defined contribution plans)
- Non-elective deferral account balance plans (employer contributed defined contribution plans)
- Non-account balance plans (defined benefit plans)
- Split dollar life insurance plans
- Expense reimbursement plans
- Stock rights plans such as stock appreciation rights, discounted stock options or other equity-based arrangements
- Separation pay plans or severance arrangements
- Foreign plans
- Amounts deferred under any other type of plan

The **plan aggregation** rules apply in several circumstances under IRC Section 409A.²

- **IRC Section 409A violations.** If an employee is a participant in two nonqualified plans of the same type (as might occur when an employee is promoted to a new job level with a different plan), and an uncorrected IRC Section 409A violation occurs in one of the plans, the plan balances of both plans are aggregated to determine the amount of tax, penalties, interest, and income inclusion.
- **Plan terminations.** Another important application of the plan aggregation rules relates to plan sponsor plan terminations. Certain plan termination can be made only if **all** arrangements of the same plan type are terminated with respect to **all** participants. See the Applied Knowledge article titled, [“Plan Terminations under IRC Section 409A”](#) for more information on plan terminations.
- **Initial eligibility.** If a plan participant becomes newly eligible in a plan, the participant has 30 days to make deferral elections, which become effective immediately. If, however, the participant is eligible for another plan of the same type, the election would not become effective for the new plan until the next date when participation is allowed under the Code.

- **Re-hired participants.** If a plan participant separates from service and then is re-hired without a balance under the plan, the participant is allowed to make a new deferral election within 30 days of becoming eligible. However, if the participant has been eligible at any time over the past 24 months, the participant must wait until the next calendar year to begin participating in the plan.
- **Limited cash-out rules.** If the total due to the participant under all similar plans is less than the IRC Section 402(g) amount, the plan sponsor may distribute the balance to the participant, as long as the entire balance is paid.

Key points to remember with Section 409A plan aggregation

- Each deferred comp arrangement must be in documentary and operational compliance with 409A.
- A Section 409A violation in one plan may trigger taxes, penalties and interest due currently on all balances in all plans of like design subject to the plan aggregation rules. Taxes, penalties, and interest due on Section 409A violations are assessed on the plan participant, not the plan sponsor.
- Discretionary and Change in Control terminations of one plan may require the termination of all plans that are required to be aggregated as described above.
- Newly eligible participants in one plan already participating in other nonqualified plans with the plan sponsor may not be able to use the 30-day rule to make deferral elections for the new plan.

¹ IRC Section 409A(d)(6), Treas. Reg. Section 1.409A-1(c)(2).

² Treas. Regs. Section 1.409A-1(c)(2).



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