

## SPECIFIED EMPLOYEES CHECKLIST

Use this checklist to guide you through the choices you will need to make regarding specified employees among the variables set out in the regulations under Section 409A. In some cases, we provide recommendations to help you along the way.

### Variables necessary to determine “specified employees” under Section 409A of the Internal Revenue Code

#### COMPENSATION

You have various options for defining the compensation that you will consider in identifying your specified employees. There are two core definitions of compensation you can use, with the most significant difference being whether equity compensation amounts (restricted stock vesting and nonqualified stock option exercises) are included in compensation. There are other differences between the definitions, but the differences are less significant. (Within each core definition, there are two alternative definitions that very likely would not have an impact on the specified employee determination.)

We wish to use ...

- A definition that excludes income recognized upon vesting of restricted stock or exercise of a non-qualified stock option from compensation.
- A definition that includes income recognized upon vesting of restricted stock or exercise of a non-qualified stock option in compensation—specifically, we wish to use ...
  - W-2 pay
  - Withholding pay

Compensation always includes amounts excluded from income as a result of an election under a cafeteria plan, qualified transportation fringe benefit or qualified plan.

The definition of compensation can be changed, but it cannot be changed once the specified employee group becomes effective.

(The “default” is the definition that excludes income recognized upon vesting of restricted stock or exercise of a non-qualified stock option from compensation.)

**Recommendation:** The definition that excludes income recognized upon vesting of restricted stock or exercise of nonqualified stock options leads to a more stable list of specified employees from year to year because stock option exercises and restricted stock vesting do not impact the determination. However, a W-2 definition is easier to obtain. Thus, there

is a tradeoff between stability and ease of administration.

**IDENTIFICATION  
DATE (OR  
MEASURING  
PERIOD**

You may choose the 12-month period over which compensation is measured for purposes of determining your specified employees. This can be any period you select that applies uniformly for all nonqualified deferred compensation plans.

Our measuring period is the ...

- Calendar year
- 12-month period ending \_\_\_\_\_

The last day of the measuring period is referred to as the “specified employee identification date.”

The measuring period can be changed but the change cannot be effective for a period of at least one year.

(The “default” measuring period is the calendar year.)

**Recommendation:** Use calendar year unless there is a compelling reason to do otherwise.

**EFFECTIVE  
DATE**

A specified employee continues in that status for a full year, and then a new specified employee group comes into place. While many specified employees may carry over from one year to the next, some employees may drop off the specified employee list and others may be added to the specified employee list. The new specified employee group comes into place as of the first day of the month following the specified employee identification date. (For example, if the identification date is Dec. 31, the new group comes into place the following April 1.) You can elect a different effect date.

Our specified employee effective date is ...

- The first day of the fourth month following the specified employee identification date
- Other: \_\_\_\_\_

(The “default” specified employee effective date is the first day of the fourth month following the specified employee identification date.)

**Recommendation:** Use the first day of the fourth month following the identification date unless there is a compelling reason to do otherwise.

**NONRESIDENT  
ALIEN  
EMPLOYEES  
ELECTION**

In the case of a nonresident alien, you may choose to include or exclude compensation that is excludable from gross income in the U.S. and that is not effectively connected with the conduct of a trade or business in the U.S. (generally, compensation for services rendered outside the U.S.). Including foreign compensation earned by nonresident aliens may result in certain nonresident alien employees being considered “specified employees,” and thus reducing the total number of employees subject to the six-month delayed payment rule. However, including foreign compensation earned by nonresident aliens may add administrative complexity.

We wish to ...

- include
- exclude

... foreign compensation earned by nonresident alien employees.

The foreign employee elections can be changed, but cannot be changed once the specified employee group becomes effective. (The “default” is that foreign compensation is included.)

**Recommendation:** There is a tradeoff between ease of administration and limiting the number of employees who are affected by the six-month delayed payment rule. Including foreign compensation earned by nonresident alien employees may result in some specified employees being foreign workers not covered by deferred compensation—thus, the group affected by the six-month delay is limited. However, foreign compensation needs to be converted to U.S. dollars and tracked in a way that may be difficult from an administrative standpoint.

**OFFICERS**

It is necessary to identify your “officers,” which are not determined by title necessarily, but are defined as any “administrative executive who is in regular and continued service.”

We will determine officers as follows:

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**ALTERNATIVE  
METHOD OF  
COMPLIANCE**

You can use an alternative method of identifying service providers if the alternative method is reasonably designed to include all specified employees (determined under the normal rule), is objective and results in no more than 200 employees (or all employees) being treated as specified employees as of a given date.