Office of Chief Counsel
Internal Revenue Service
memorandum

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subject: Matching Contributions 409A Substantial Risk of Forfeiture

This Chief Counsel Advice responds to your request for assistance. This advice may not be used or cited as precedent.

FACTS

On November 1, 2014, an employee entered into an agreement to defer $15,000 of the employee's salary that would otherwise have been paid during 2015, with payment of the deferred amount to be made as a lump-sum payment on January 1, 2018, but only if the employee continues to provide substantial future services until December 31, 2017. Under the agreement the employee's salary is reduced by $600 each biweekly pay period (so 26 x $600 or $15,600) and the employer credits matching amounts to the employee's deferred compensation account of 25% of each salary reduction (so 26 x ($600 / 4) or $3,900) for a total amount deferred of $19,500. The matching amounts are credited each time a salary reduction amount is credited, which is the time the salary reduction amount would otherwise be paid as salary.

ISSUE

May the salary that the employee could have elected to receive as compensation be treated as subject to a substantial risk of forfeiture under section 409A through December 31, 2017, if as part of the imposition of the service requirement through

December 31, 2017, the employer provides a matching contribution resulting in a 25% increase in the present value of the amount of deferred compensation?

CONCLUSION

Yes, an amount that an employee could have elected to receive as salary may be treated as subject to a substantial risk of forfeiture under section 409A if the employer provides a matching contribution resulting in a 25% increase in the present value of the amount deferred.

LAW AND ANALYSIS

Section 409A generally provides that if certain requirements related to the timing of elections, distributions, and funding are not met at any time during a taxable year, amounts deferred under a nonqualified deferred compensation plan for that year and all previous taxable years are currently includible in gross income to the extent not subject to a substantial risk of forfeiture and not previously included in gross income. Amounts includible in income under section 409A are also subject to two additional taxes under section 409A(a)(1)(B).

Treas. Reg. §1.409A-1(d)(1) provides that a substantial risk of forfeiture exists if the receipt of deferred compensation is conditioned on the performance of substantial future services or the occurrence of a condition related to a purpose of the compensation, and the possibility of forfeiture is substantial. In general, the addition of any risk of forfeiture after the legally binding right to the compensation arises, or any extension of a period during which compensation is subject to a risk of forfeiture, is disregarded for purposes of determining whether such compensation is subject to a substantial risk of forfeiture. However, an amount will be considered subject to a substantial risk of forfeiture beyond the date or time at which the recipient otherwise could have elected to receive the amount of compensation if the present value of the amount subject to a substantial risk of forfeiture is "materially greater" than the present value of the amount the recipient otherwise could have elected to receive absent such risk of forfeiture.

Generally, under Treas. Reg. §1.409A-1(d), the addition of a risk of forfeiture is disregarded. However, the addition of a substantial risk of forfeiture is respected if the present value of the amount subject to the substantial risk of forfeiture is "materially greater" than the present value of the amount the service provider otherwise could have elected to receive absent such risk of forfeiture. Under the facts here, the present value of the amount deferred by the employee is 25% greater than the amount the employee otherwise could have received absent the addition of the substantial risk of forfeiture. A 25% increase in the present value of the amount a service provider could have received absent the risk of forfeiture is a material increase. Accordingly, the combined deferred amount of 2015 salary ($15,600) plus the deferred amount of the employer's matching contribution ($3,900) is subject to a substantial risk of forfeiture for purposes of section 409A until December 31, 2017.

This writing may contain privileged information. Any unauthorized disclosure of this writing may undermine our ability to protect the privileged information. If disclosure is determined to be necessary, please contact this office for our views.

Please call if you have any further questions.

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