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Time to Act on New Deferred Compensation Rules

On April 10, 2007, the Treasury Department and the IRS issued long-awaited final regulations on the treatment of nonqualified deferred compensation plans and arrangements under Section 409A of the Internal Revenue Code ("Section 409A"). Section 409A imposes significant restrictions on nonqualified deferred compensation plans, including restrictions on the time and form of payment of deferred compensation.

"Nonqualified deferred compensation" is defined very broadly for purposes of Section 409A. In addition to traditional deferred compensation plans, such as SERP's and nonqualified retirement savings plans, Section 409A can also cover arrangements such as employment agreements, severance agreements, stock compensation plans and bonus programs.

Compliance with Section 409A is very important. Failure to comply would result in severe tax penalties, including a 20% excise tax, being imposed on service providers (e.g., employees, directors and consultants) who participate in the applicable deferred compensation program. In addition, service recipients (e.g., employers) have certain withholding and reporting obligations under Section 409A.

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Arrangements subject to Section 409A must be amended on or before **December 31, 2007**. To satisfy the requirements of Section 409A prior to the deadline, we suggest that you take the following steps now:

1. **Identify plans and arrangements that are or may be affected by Section 409A**. Determine whether your company maintains any (a) SERP's; (b) excess benefit plans; (c) deferred compensation plans; (d) employment agreements; (e) severance plans, policies, or arrangements, (f) stock-based compensation plans (e.g. stock options; restricted stock, etc); (g) bonus programs; (h) split dollar insurance arrangements; (i) rabbi trusts; or (j) change in control agreements.

2. **Determine the impact of Section 409A, if any, on affected plans and arrangements**.

3. **Administer affected plans and arrangements in good faith compliance with Section 409A and related guidance**.

4. **Identify "specified employees" under Section 409A**. The requirements under Section 409A are more burdensome for "specified employees" of publicly traded corporations. Therefore, it is important for those corporations to identify affected employees and the impact of Section 409A on them.

5. **Amend affected plans and arrangements to comply with Section 409A**. All affected plans and arrangements must comply, or be amended to comply, with documentation requirements established in the final regulations by **December 31, 2007**.

As you go through the process of making certain that your plans, programs and arrangements comply with Section 409A, please contact your Vorys attorney if you wish to discuss any of these issues further.

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EEOC Scrutinizing Criminal Background Checks

As part of its recently announced E-RACE initiative, the EEOC is examining the potentially discriminatory aspects of criminal background checks. E-RACE stands for Eradicating Racism and Colorism from Employment. The EEOC promises to use this initiative to "identify issues, criteria and barriers that contribute to race and color discrimination, explore strategies to improve the administrative processing and the litigation of race and color discrimination claims, and enhance public awareness of race and color discrimination in employment." Within these broad objectives, the EEOC will be focusing on criminal background checks. The EEOC notes that "some facially neutral employment criteria are significantly disadvantaging applicants and employees on the basis of race and color," and references unspecified "selection decisions based on names, arrest and conviction records, employment and personality tests, and credit scores, all of which may disparately impact people of color."

According to a study cited by the EEOC, a criminal history is more likely to keep an African-American applicant from being hired than a Caucasian applicant. In fact, the study (which used testers to apply for jobs in the Milwaukee area) found that, when compared to a Caucasian applicant with the same criminal offense, an African-American applicant was 40% more likely to have that record be a bar to securing entry-level employment.

The potential impact of the EEOC's initiative on the criminal background check policies of employers is significant. According to a study cited by the EEOC, the United States has the highest incarceration record in the world, and over half a million felons are released from U.S. prisons each year. Studies further indicate that "experience with the criminal justice system" is a major impediment to future employment, and that unemployment itself is a strong contributing factor to future recidivism. Thus, the EEOC's examination of criminal background check policies appears to be concerned both with racially discriminatory policies and with policies which, regardless of racial impact, may be a factor in recidivism.

In addition to being non-discriminatory, workplace background checks also must comply with the Fair Credit Reporting Act ("FCRA"), and, in some states (particularly New York, Hawaii, Pennsylvania and Wisconsin), with state law restrictions. The FCRA requirements include advance notification of the background check, written authorization by the individual, and prior notice to the individual of any "adverse action" the employer plans to take as a result of the background check's outcome.

What To Do?

In light of the EEOC's increased focus on background checks, and in order to comply with the EEOC's existing guidance on this issue, employers should review their policies and address the following issues:

1. Within broad policies on background checks, allow for exceptions based on such factors such as the nature of the conviction and the length of time between conviction and application.

2. Consider whether the conviction suggests conduct that is "substantially related" to the job at issue. For example, while a conviction for theft might be substantially related to the ability to work in a bank, a misdemeanor drug possession conviction might not be.

3. Focus on convictions, not arrests. While there may be circumstances where a history of arrests would be relevant in screening out an applicant, the EEOC takes the position that "a blanket exclusion of people with arrest records will almost never withstand scrutiny."

Please contact your Vorys attorney if you wish to discuss these issues further.

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