



HILL WARD HENDERSON
ATTORNEYS AT LAW
TAMPA | CLEARWATER

FICA Taxes on Nonqualified Deferred Compensation Plans

September 19, 2019

When is the appropriate time to withhold FICA (social security and Medicare) tax on amounts deferred under a Nonqualified Deferred Compensation Plan ("NQDC Plan")? The following briefly summarizes the primary two withholding rules (the special timing rule and general timing rule) that apply to amounts credited to a NQDC Plan.

Special Timing Rule for FICA Tax on Deferred Compensation

Wages are generally subject to FICA tax when they are paid, whether actually or constructively, to the employee. However, under the special timing rule for FICA tax withholding, amounts deferred under a NQDC Plan are subject to FICA tax upon the later of (1) when the services are performed to which the deferred amounts relate or (2) when there is no substantial risk of forfeiture for such amount (i.e. upon full vesting). Therefore, immediately vested amounts (e.g., salary deferrals) are subject to FICA tax at the time these amounts are withheld from pay. If an amount remains subject to a substantial risk of forfeiture, the amount (plus any earnings accruing prior to the date the amounts vest) will be subject to FICA tax at the time it is no longer subject to a substantial risk of forfeiture or vested. Any future earnings accruing on amounts that have been subjected to FICA withholding will not be subject to future FICA taxes.

If the NQDC Plan uses a deferral benefit type formula to determine a participant's benefit, FICA tax is not withheld on the amount until it is both vested and "reasonably ascertainable".

In addition to the potential FICA tax savings on future earnings, withholding FICA tax from deferred amounts under a NQDC Plan under the special timing rule may be favorable to the participant depending on their wages for the year of deferral (or, in the case of amounts that vest on a later date, the vesting date). The social security portion of FICA tax is only imposed on compensation amounts up to the social security taxable wage base. Therefore, if a participant has other, substantial compensation while still employed during the year of deferral or the year of vesting, some or all of the social security portion of the FICA tax on the deferred amount under the NQDC Plan may be eliminated.

General Timing Rule for FICA Tax on Deferred Compensation

If an employer does not withhold FICA tax on deferred amounts in accordance with the special timing rule, FICA tax will need to be withheld in accordance with the general timing rule. Under the general timing rule, FICA tax is withheld in the year of payment of the NQDC Plan benefits to the participant on all deferred amounts and any earnings that have accrued through the date of payment.

Correction of Missed Application of Special Timing Rule

If an employer fails to initially withhold FICA tax from deferred amounts under a NQDC Plan in accordance with the special timing rule, the employer generally may take steps to correct within 3 years by amending prior tax returns and paying any additional FICA tax plus interest resulting from application of the special timing rule.

In situations where the three-year period had passed, employers used to have the opportunity to enter into a closing agreement with the IRS to retroactively pay the additional FICA tax, according to the special timing rule, plus interest. Unfortunately, the IRS has stated it will no longer be entering into closing agreements with employers who request to fix the FICA tax error after the three-year period to amend their FICA tax reporting has passed.

Because of the potential tax savings, it is generally recommended that employers take advantage of the special timing rule.

If you have questions or would like additional information, please contact a member of our Employee Benefits and Executive Compensation Practice Group.



Al Ward
al.ward@hwlaw.com
813.222.8703



Kirsten Vignec
kirsten.vignec@hwlaw.com
813.222.8731



Melanie Hancock-Brown
melanie.hancock-brown@hwlaw.com
813.222.3138



Bret Hamlin
bret.hamlin@hwlaw.com
813.222.8717



Tim Zehnder
timothy.zehnder@hwlaw.com
813.222.3113

Hill Ward Henderson | www.hwlaw.com



Hill Ward Henderson | 101 East Kennedy Boulevard, Suite 3700, Tampa, FL 33602

[Unsubscribe {recipient's email}](#).

[About Constant Contact](#)

Sent by info@hwlaw.com