



DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

April 8, 2005

OFFICE OF  
CHIEF COUNSEL

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Reference: Correspondence from the Department of Labor

Dear \_\_\_\_\_ :

This is in response to your request for assistance from the Employee Benefits Security Administration of the Department of Labor which was forwarded to the Internal Revenue Service for response. Your request concerns the withholding rules applicable to Federal Insurance Contributions Act (FICA) taxes imposed on nonqualified annuities.

For purposes of the FICA tax, sections 3101 and 3111 of the Internal Revenue Code (Code) impose a tax on the wages paid by employers to employees with respect to employment. The FICA tax is comprised to two separate taxes. Code sections 3101(a) and 3111(a) impose Old-Age, Survivor's, and Disability Insurance (OASDI) taxes, and sections 3101(b) and 3111(b) impose Hospital Insurance (HI) taxes on employees and employers, respectively.

Qualified retirement benefits are not subject to FICA taxation. However, nonqualified retirement benefits are subject to FICA taxation.

Correspondence forwarded from the Department of Labor suggests you are receiving nonqualified retirement benefits in the form of an annuity from a nonqualified deferred compensation plan. Code section 3121(v)(2) and Employment Tax Regulation (regulation) section 31.3121(v)(2)-1 provide rules that govern the FICA tax treatment of certain nonqualified deferred compensation plans.

As a general rule, nonqualified deferred compensation must be taken into account as FICA wages as of the later of (i) the date on which the employee performs the services

that create the right to a deferral, or (ii) the date on which the amount deferred is no longer subject to a substantial risk of forfeiture.

Because you are receiving monthly benefits in the form of an annuity, a defined monthly benefit, the plan providing such benefits is a “nonaccount balance plan”. There is a special rule for “nonaccount balance plans” which permits an employer to delay taking a deferral under the plan into account for FICA tax purposes until the amount deferred is considered “reasonably ascertainable”, which is the first date on which the amount, form, and commencement date of the benefit are known, so that its present value can be computed. When the present value of a benefit becomes reasonably ascertainable, the present value amount is subject to FICA tax. Under some non-account balance plans retirements benefits become reasonably ascertainable at the time of retirement.

Correspondence included in the Department of Labor referral from your former employer indicates that your employer failed to correctly apply the FICA tax withholding rules to your nonqualified pension benefits when you retired. However, the correspondence also suggests that the employer has since taken actions to comply with the statute and regulations and that your benefit payments are being temporarily reduced to satisfy the withholding requirements for nonqualified deferred compensation.

If you have any further questions concerning this matter, please contact

of my staff.        can be reached to (202) 622-        .

Sincerely,

John B. Richards  
Senior Technician Reviewer  
Employment Tax Branch 2  
(Tax Exempt & Government Entities)