**TAX REPORTING FOR DISTRIBUTIONS FROM NQDC PLANS**

**Employee Tax Reporting (W-2)**

**Wage Reporting**

Distributions to employees from nonqualified deferred compensation plans are considered wages subject to income tax upon distribution. Since nonqualified distributions are subject to income taxes, these amounts should be included in amounts reported on Form W-2 in Box 1, Wages, Tips, and Other Compensation. Most states follow the federal rules for reporting distributions from deferred compensation plans, please consult local regulations.

**Income Tax Withholding**

Distributions from nonqualified deferred compensation plans are normally considered to be “supplemental wages” for income tax withholding purposes. Federal tax withholding rules require that taxes on supplemental wages are withheld at a flat rate of 25 percent. If the participant’s total supplemental wages from all sources exceeds $1 million, federal tax must be withheld at the flat rate of 35 percent. State rules vary, please consult local regulations.

**Social Security and Medicare Reporting**

Distributions are not normally subject to Social Security or Medicare taxes, since these have been collected during the plan participant’s service with the employer. However, any unvested amounts that become vested at distribution would be subject to Social Security and Medicare taxes at that time.

**Box 11 Reporting**

The purpose of Box 11 is for the Social Security Administration to determine whether any wages reported on Form W-2 were earned in prior years. Since distributions from a nonqualified deferred compensation plan are normally earned in prior years, these amounts should be included in Box 11.

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Tax reporting for distributions from nonqualified deferred compensation plans depends on the employment status of the plan participant. Tax information for employees is reported using Form W-2, while tax information for independent contractors (i.e., agents or members of the Board of Directors) is reported using Form 1099 MISC.

If you have any questions regarding this information, please contact:

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In a year when a plan participant has both nonqualified deferrals and nonqualified distributions, special reporting rules apply. Publication 957 has detailed instructions for reporting when this occurs:

- Do not complete Box 11 if both deferrals and distributions occur in the same year.
- Report to the Social Security Administration on Form SSA-131 the amount earned during the current year (typically the amount deferred). Current Form W-2 instructions specify, however, that a Form SSA-131 should not be filed if the employee will not be age 62 or older by the end of the year.

**Box 12 Reporting**

Nonqualified distributions are not reported in Box 12. Nonqualified amounts should only be reported using Code Z if the amount is subject to additional taxation and penalties due to a violation of Section 409A. Section 409A also requires reporting of “deferrals” in Box 12 using Code Y, but the Internal Revenue Service has suspended the Code Y reporting requirements until further regulations are issued.

**Distributions to Beneficiaries of Deceased Plan Participants**

Distributions to the beneficiaries of deceased nonqualified plan participants are reported on Form 1099-MISC.

**Independent Contractor Reporting (1099 MISC)**

Independent contractors subject to Form 1099 reporting, such as agents or members of the company’s Board of Directors, may be eligible to participate in a nonqualified deferred compensation plan. Nonqualified plan distributions are reported in Box 7 on Form 1099-MISC and are subject to income tax and self-employment tax (SECA) at the time of distribution. If the plan is in violation of Section 409A, then amounts subject to penalties would be reported in Box 15b.