GuideStone®

409A

Deferred Compensation Plan Administration Manual

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This information should not be considered tax or legal advice. GuideStone stands ready to assist your organization as you work with your legal and tax advisors by providing resource information that you and your advisor may find beneficial.

DEFERRED COMPENSATION PLANS

In a typical employment arrangement, employers agree to provide compensation for services provided by their employees. In addition, employers offer certain benefits, such as insurance to help supplement the cost of health care and contributions to an employee's retirement plan to assist in building adequate savings for their employees' retirement income.

Deferred compensation plans have been developed to provide employers with a vehicle to set aside the additional funds for their employees. Examples of these arrangements include programs that reward loyal or outstanding service, the attainment of certain goals or service duration requirements with the employer. This manual will address 409A deferred compensation plans, which are offered by churches, qualified church-controlled organizations (QCCOs) that are exempt from the provisions of the Employee Retirement Income Security Act of 1974 (ERISA) and top-hat plans of employers subject to ERISA.*

PURPOSE OF MANUAL

GuideStone® has prepared this manual to provide plan administrators an overview of non-qualified deferred compensation (NQDC) arrangements a n d to help plan administrators better understand the intricacies of these types of arrangements. While we attempted to cover important points, there are many nuances in the regulations governing these plans, and it is impossible to cover every scenario. We recommend that you routinely review your plan to see if you are administering it accordingly. We also recommend that you consult your legal counsel regarding the operation and maintenance of the plan.

All employees of the employer involved in administering the NQDC arrangements should read through the *Basic Plan Document* and the employer's *Adoption Agreement* as well as any other documents related to plan provisions (such as policies or procedures). These documents are the key to proper administration of the employer's NQDC arrangement with GuideStone.

Failure to administer the plan properly could result in significant penalties for the participant.

*Note: For employers subject to ERISA, this manual will address only the top-hat exception to ERISA for non-qualified plans.

OVERVIEW OF 409A

Section 409A applies to NQDC arrangements. The IRS broadly defines compensation as deferred if the participant has a legally binding right during a taxable year to compensation that will be paid in a later taxable year. Deferred compensation is not restricted to plan contributions and can thus include other arrangements like separation pay or incentive pay.

These regulations specifically exclude certain arrangements:

- 403(b) plans and 401(k) plans
- Non-taxable benefits
- Vacation, sick leave and disability pay
- 457(b) arrangements
- Short-term deferrals
- Grandfathered deferred compensation plans — non-qualified plans that existed prior to the effective date of Code section 409A (i.e., the account was earned and vested as of December 31, 2004)

Section 409A makes all NQDC taxable in the year deferred unless it meets either of the following criteria:

- Subject to a substantial risk of forfeiture
- Meets the requirements set out in 409A

Section 409A does not limit the amount of compensation that the employer or participant can defer or who can be included in the arrangements. Nor does it require participation, vesting or nondiscrimination standards as are found in retirement plans.*

*Note: Top-hat plans must limit participation to a "select group of management or highly compensated employees." The Department of Labor (DOL) has not provided significant guidance on what constitutes a "select group of management or highly compensated employees."

NQDC arrangements must be in writing and must contain the appropriate provisions as required by the regulations. Upon establishing an NQDC plan with GuideStone, we will provide you with a *Basic Plan Document*, *Trust Agreement* (rabbi trust), *Adoption Agreement* and additional administrative forms you may need to put the arrangements in writing.

- The *Basic Plan Document* encompasses the foundational provisions.
- The *Adoption Agreement* reflects the specific provisions elected by the employer for the arrangement.

OVERVIEW OF 409A

(CONTINUED)

The *Basic Plan Document* and *Adoption Agreement* together with any other documents such as policies and procedures related to the plan constitute the basic provisions of the employer's NQDC arrangement. The administrative forms, if applicable, will document any deferral or payment arrangements that may be allowed in the *Adoption Agreement*. Because the forms contain options that may not be applicable to your particular arrangement, you should assist the participant in completing any forms. Contact GuideStone if you have any questions about how to complete the forms.

As a plan sponsor, it is your responsibility to keep all documents related to the plan since its inception, including any resolutions, exhibits and forms. You should verify that your files contain all current and historical plan documents. GuideStone reserves the right to retain only an electronic copy of the plan documents for a reasonable period of time as determined by GuideStone in its policies and procedures and to destroy or otherwise dispose of any original documents or other materials related to the plan.

Note that a rabbi trust is an optional document which may offer some level of security to the employee with respect to their non-qualified benefits. This is especially true for an NQDC plan in which the employee defers compensation with only a promise of the employer to pay the benefits. Under the rabbi trust, the funds are reachable by the employer's creditors in the event of the employer's bankruptcy or insolvency. Thus, the rabbi trust will protect an employee's investments from the employer's reach in most cases. However, if insolvency or bankruptcy occurs, the plan participants stand in line with other employer creditors. The IRS has ruled that the establishment of a rabbi trust does not in itself cause an NQDC plan to be considered funded for tax purposes since NQDC plan assets are subject to the claims of creditors and are not set aside solely for the benefit of participants.

BASIC TYPES OF DEFERRAL ARRANGEMENTS

Various types of deferral arrangements are allowed in NQDC plans. However, it is up to the employer to determine how they want the plan structured, the types of deferrals they want to allow and if they are going to place certain restrictions on how and when the employee can receive the amount set aside for them in the plan.

Below are some of the more common arrangements, along with a brief explanation of any IRS conditions that must be satisfied.

1| Elective (employee deferral)

The employee agrees to set aside a certain amount from his or her salary into the plan to be paid at a later date or event as specified at the time of deferral.

Important things to remember:

- In general, forms must be signed by **December 31 of the year prior to the year** the deferrals are being made. If forms are not completed by such date, then deferrals cannot be made or changed for the following year (e.g., to make elective deferrals for 2021, the forms must be signed by December 31, 2020).
- For newly eligible employees, if forms are not signed and dated **within 30 days* of becoming eligible**, then deferrals cannot be made for the year of eligibility.
- Once forms are signed and dated and December 31 has passed, the amount of the deferral **cannot change** and must be contributed, or the participant could face taxes and penalties. Deferral elections can be made for a specific year (e.g., defer 10 percent of my compensation from my 2020 salary) or evergreen (e.g., defer 10 percent of my compensation every year until I make a timely election to change or stop the deferral amount).
- If the participant takes a distribution from the 409A plan because of an unforeseeable emergency or a hardship distribution from their 403(b) or 401(k) plan with the employer, they may cancel their election to defer into the 409A plan for the remainder of the year. The deferral elections for subsequent years will be subject to the general rules regarding deferral election (i.e., must be made by the end of the year to take effect in the subsequent year).

*Note: The payment election must be made at the same time as the deferral election. See the “Distributions” section for more information.

2| Non-elective (employer contribution)

The employer may desire to set aside a certain amount from its general assets for the employee. The employer has the ability to change the contribution amount within the taxable year if the employer contribution was discretionary or based on a percentage of compensation.

BASIC TYPES OF DEFERRAL ARRANGEMENTS

(CONTINUED)

3| Performance based

The employer may desire to set aside a certain amount to be paid at a time at which the employee has met certain performance requirements over a service period of at least 12 months (e.g., coaches having a winning season, increasing sales by 5 percent or increasing enrollment by 15 percent over a period of at least 12 months). This is different from a bonus that may be awarded without regard to meeting specific performance requirements. Participants must make elections to defer performance-based compensation **six months before the end of the performance period**, provided there is still some significant uncertainty regarding whether the performance requirements will be met. Performance-based bonuses cannot be discretionary and can only result if the participant completes specifically outlined objectives.

4| Recurring bonuses

For bonuses that do not meet the definition of “performance based” outlined above, the election to defer must meet the general requirement of being made by the end of the year before the year to which the bonus relates. For example, a participant must make an election to defer amounts from a bonus earned in 2020, but payable in 2021, no later than December 31, 2019.

5| Short-term deferral exception to 409A

Short-term deferral arrangements are an important exception to Code section 409A. Under a short-term deferral arrangement, the amount deferred must generally be received and/or taxed within two and one-half (2.5) months following the end of the calendar year in which the legally binding right to the compensation arises (i.e., the date the participant is assured of payment of the dollars) or within two and one-half (2.5) months following the end of the year in which the participant’s substantial risk of forfeiture lapses. Most short-term deferral arrangements are established with a substantial risk of forfeiture requiring the participant to remain employed through a specific date that is at least 24 months from the date the arrangement is established.

ADMINISTRATION OF PLAN

1| Prior to enrolling participants in the plan

A. Verify participant eligibility.* Refer to your *Adoption Agreement* to verify who is eligible to participate in the plan. Your *Adoption Agreement* may list categories of employees (for instance, all senior executives) who are eligible to participate, or it may refer to a separate *Exhibit B* where you indicate by name/category who is eligible to participate. If an *Exhibit B* is used, it may be necessary to update *Exhibit B* if a new participant is added or is no longer eligible to participate or if you decide to add or delete categories of employees eligible to participate.

*Note: Top-hat plans must limit participation to a "select group of management or highly compensated employees." The DOL has not provided significant guidance on what constitutes a "select group of management or highly compensated employees." Employers with a top-hat plan should consult with legal counsel regarding what constitutes a "select group of management or highly compensated employees."

B. Complete a deferral form — The purpose of this form is to:

- Meet the written deferral requirements of 409A.
- Communicate enrollment information.
- Assist in the communication of contribution expectations among the participant, employer and GuideStone.
- Allow the participant to make an investment election, if allowed by your plan. You will notice a box on the deferral form to allow the participant to elect to mirror his or her current investment allocation in an existing deferred compensation plan with GuideStone.

After completing this form, give a copy to the participant for their files and send a copy to GuideStone. You should maintain the original in your files. If at any time you have questions about completing the form, please call your GuideStone relationship manager.

2| Remitting employee deferrals and employer contributions

Below are several things you need to know regarding remitting deferrals/contributions to GuideStone:

- Remit deferrals/contributions correctly in reference to the amount, type (i.e., employee non- match or employer match) and pay period.
- Remit deferrals/contributions as soon as possible following the payroll(s) for which the deferrals are applicable and in accordance with the remittance method you use.
- A failure to defer the correct amount from a participant's compensation may be considered either an "acceleration" or "excess-deferred amount" under Code section 409A and could result in costly penalties to the participant and employment tax considerations for the employer.

ADMINISTRATION OF PLAN

(CONTINUED)

3 | Employment status

You should promptly notify GuideStone of changes in the employment status of participants. A change in employment status could trigger a payment under the NQDC plan. A failure to make a timely payment is an impermissible deferral that can result in significant penalties and taxes. Changes in employment status may include the following:

- Change from part-time to full-time status or vice versa if the status affects participant's eligibility in the plan or results in a separation from service. (Refer to the *Basic Plan Document* for the definition of "separation from service.")
- Rehire.
- Termination of employment. You can terminate a participant through Employer Access Program (EAP). If you are not set up for EAP, please contact your GuideStone Administrator.)
- Transfer within employer (i.e., when an employee switches from one employer number to another for contribution purposes). This is especially important if the employer has employees in both a not-for-profit entity and a for-profit entity and/or has multiple plans or multiple related employers.
- Disability.
- Death.

Important: It is especially important that plans with vesting schedules notify GuideStone promptly when a participant terminates so GuideStone may remove non-vested amounts from participant accounts. Not doing so can mislead participants regarding the value of their accounts.

4 | Employer changes

Notify GuideStone immediately of changes or possibilities of changes in the following:

- 501(c)(3) status
- Ability to offer a church plan (i.e., level of control or association with a church or a convention or association of churches)
- Organizational or corporate structure
- Employer name

Changes in any of the above can impact your plan or plans of related employers or other entities. Organizational or structural changes can include mergers, acquisitions, spin-offs, etc. Such changes frequently require plan amendments and can affect the administration of the plan. You need to submit a new *Status Certification Form* and *Church Plan Eligibility Form* in the event of any organizational changes so GuideStone will be informed of possible impacts to your plan. Additionally, newly related organizations that wish to participate in your plan may need to submit other information so GuideStone can determine their eligibility to participate.

In addition, if your plan permits a distribution on a change of control as defined in the *Adoption Agreement* and *Basic Plan Document*, such a change may result in a distribution event.

If you undergo a reorganization or restructuring, you should contact your relationship manager at GuideStone for more information.

*Note: If your organization is no longer able to offer a church plan and therefore becomes subject to ERISA, you must redesign the non-qualified plan in order to be exempt from ERISA. Contact your relationship manager to discuss your NQDC plan options. Likewise, if your organization's funding sources change to include a significantly higher ratio of funding from government sources or from goods and services offered to the general public, you may have other deferred compensation options available. Contact your relationship manager to discuss your situation.

5 General administrative responsibilities

Both the employer and the recordkeeper/trustee of a plan have administrative responsibilities. The *Recordkeeping Services Agreement* addresses specific administrative responsibilities of the employer and GuideStone that involve plan administration.

A. Employer responsibilities

Some examples of plan administration activities associated with these duties include, but are not limited to, the following:

- Explaining the plan to eligible participants and answering their questions about the plan.
- Having participants complete *Deferral Agreements* and *Payment Election Forms* and sending copies of the completed forms to GuideStone.
- Maintaining participants' *Deferral Agreements*, *Payment Election Forms* and other important papers relating to participation in the plan such as *Exhibit B* or documentation of the substantial risk of forfeiture for a short-term deferral arrangement.
- Withholding deferrals from participants' compensation as requested.
- Withholding employment taxes at the appropriate time (generally when deferrals/contributions are made to the plan).
- Verifying and adjusting deferral/contribution amounts.
- Cancelling deferrals for the remainder of the year in cases in which the participant takes an unforeseeable emergency distribution from the 409A plan or a hardship withdrawal from their 403(b) or 401(k) plan with the employer and elects to cancel 409A deferrals.
- Notifying GuideStone promptly in the event of a participant's death, disability, termination or occurrence of a specified time at which payment is due.
- Responding to requests for information from GuideStone about the plan or participants.
- Keeping plan practices consistent with plan provisions and making timely amendments.
- Notifying GuideStone prior to the date any amounts vest (whether incremental or cliff vesting) or a substantial risk of forfeiture lapses. If notification cannot be completed prior to the date, you must notify GuideStone within 10 days following the lapse or vesting date.
- Top-hat plans only: Filing a one-time notice with the DOL that the plan is exempt from ERISA reporting within 120 days of plan establishment.

ADMINISTRATION OF PLAN

(CONTINUED)

B. GuideStone services

Some examples of plan administration activities associated with these duties include, but are not limited to, the following:

- Establishing participant accounts
- Placing participant deferrals and employer contributions in plan funds, as directed
- Preparing and distributing quarterly accounting statements to participants and employers
- Preparing and distributing written information for participants, participants' spouses, beneficiaries and their attorneys in the event of death, divorce or bankruptcy
- Calculating benefits and communicating with participants and employers regarding benefit amounts
- Establishing procedures to administer distribution of participants' accounts (including in the event of death or divorce)
- Making administrative rules in accordance with the plan

6| Vesting

Vesting is the process by which a participant gains ownership, or rights, to the contributions made to the participant's account. Participants in plans that have vesting schedules forfeit non-vested amounts, including earnings, when they terminate service if they have not satisfied the service requirement to be fully vested. GuideStone then places forfeited amounts in the employer's non-qualified forfeiture account.

See the *Basic Plan Document* and your *Adoption Agreement* for plan provisions regarding vesting. Article III of your *Adoption Agreement* sets forth any vesting provisions that apply to your NQDC.

Regardless of whether amounts are distributable, for participants subject to FICA, each vesting increment subjects newly vested amounts to FICA employment taxes. You should contact GuideStone at each increment in a participant's vesting schedule to learn the amount subject to employment taxes and that you must report on the employee's IRS *Form W-2*. For participants subject to self-employment (SECA) taxes, SECA applies at distribution.

You must notify GuideStone prior to the date any amounts vest (whether incremental or cliff vesting) or a substantial risk of forfeiture lapses. If notification cannot be made prior to the date, you must notify GuideStone within 10 days following the lapse or vesting date.

Failure to notify GuideStone of a participant's termination causes non-vested amounts to remain in the participant's account. These amounts continue to accrue earnings. The participant can, therefore, easily be misled into thinking his or her accumulations are greater than they actually are when vesting is later applied. In addition, failure to notify GuideStone of any event that may constitute a vesting event can cause an operational failure that results in penalties and taxes for the participant and potential employment tax issues for the employer.

In addition to notification of termination, the plan sponsor shall promptly provide any related information necessary to enable GuideStone to (a) maintain accurate and up-to-date records of vested percentages and (b) process forfeitures of non-vested amounts on a timely basis, if vesting is applicable.

7 | Distributions

One of the most important aspects of the 409A plan that administrators need to understand relates to the timing and method of distributions. In an effort to limit the ability of executives to access their deferred compensation plan assets before the designated time, Congress mandated that executives must elect how and when they will take distributions **before** deferring the compensation into the plan. Congress also prohibited acceleration of payments and restricted when and how often a participant may change distribution elections. Once the timing and method are set, there are complex rules to make changes. This makes it **imperative** that the participant understands the choices he or she is making.

Under Code section 409A, payment events are limited to:

- Separation from service (as defined by the plan)
- Death
- Disability
- A specified time or according to a fixed schedule (including following the lapse of a substantial risk of forfeiture, e.g., a vesting event)
- An unforeseeable emergency
- A change in the ownership or effective control of the corporation or a change in the ownership of a substantial portion of the assets of the corporation (as defined by the plan)

Refer to your *Adoption Agreement* to determine which payment events are applicable to your plan.

A. Time and method election

The participant must elect when he or she will (a) receive distributions from the plan and (b) in what form the distributions will be made (single sum withdrawal or installment):

- By December 31 of the year prior to the year for which salary is deferred or for which non-elective (employer) contributions are made to the plan or
- Within 30 days of becoming eligible to participate in the plan

This election applies to all contributions made to the plan until a timely election for a different time and method is made with respect to future accumulations.

If the plan allows the employer (instead of the participant) the right to elect the time and method of payment, the employer has until the later of the time the legally binding right arises or the employee's deferral election deadline. Note that the plan may dictate whether employee elections are allowed regarding the time and method of payment or can dictate the payment election with no elections allowed.

Rule of thumb: The participant must make elections by the end of the year prior to the year of the deferral/contribution unless an evergreen election is in place (i.e., an election that applies to all years until a timely election change is made (end of the year prior to the year of the deferral/contribution)).

ADMINISTRATION OF PLAN

(CONTINUED)

⚠ CAUTION: If a timely election is not made, the plan provides a default election, which may help to prevent taxes and penalties related to the failure to make a timely election. Under the plan default, if a timely election is not made, payment for contributions subject to the default will be made upon the earliest of **separation from service** or death. If the earliest payment event is separation from service, payment will be made 13 months after the event. If the earliest payment event is **death**, one-half the benefit will be paid 30 days following death and the remainder will be paid 15 months following death. Remember, for **future** contributions, if the plan provides, an election may be made for a different time and method of payment, i.e., it is possible some contributions may be subject to the default provision and some, for which a timely election has been made, may not.

If the plan allows the participant to make an election, the participant must choose from a list of approved events that are selected by the employer in the *Adoption Agreement*:

- Separation from service (as defined by the plan)
- Death
- Disability
- A specified time or according to a fixed schedule (including following the lapse of a substantial risk of forfeiture, e.g., a vesting event)
- An unforeseeable emergency
- A change in the ownership or effective control of the corporation or a change in the ownership of a substantial portion of the assets of the corporation (as defined by the plan)

These payment events are the only payment events allowed by Code section 409A and the related *Treasury Regulations*. If you want to have any or all of the events apply to your participants, it must be stated in your *Adoption Agreement*. You do not have to elect all the payment events that are available. If allowed in your plan, the participant can choose the earliest or latest of any or all of these events.

When choosing the timing/payment event, the participant must also choose the method of payment. The plan may allow for single sum withdrawals, installments or both. The installment option allows flexibility with respect to change elections (discussed later), but again, the decision must be made before the year in which the salary is deferred or for which employer contributions are made to the plan.

The participant can make a different election for each year or can make an election that will apply to all future contributions (evergreen election) until timely changed.

Remember, if the participant or employer fails to make a timely election, the plan default will be deemed the election for that year. Except in the case of death, the plan default is to pay the account in a single sum 13 months after separation from service.

B. Failure to pay in accordance with election

If payments are not made in accordance with the election, an operational failure will occur triggering penalties (see the "Consequences of violation" section of this manual). It is the employer's responsibility to notify GuideStone of the attainment of a payment event and request payment to be made, even if a specific date is chosen.

C. Anti-acceleration restrictions/change rules

Generally, participants are not allowed to accelerate payments (other than for an unforeseeable emergency, if it is allowed in the plan). Does this mean that participants are stuck with their timing and method elections? No. Although participants cannot accelerate payment, by following certain rules they may be able to change the timing and method of distribution with respect to accumulations in the plan. (Remember, the time and method of payment election with respect to future contributions is not subject to the following restrictions.)

In general, a participant is allowed to change the time and method of the payment if the election is filed with the employer at least 12 months prior to the date the first payment would come due and the payment is pushed out for at least five years. If the participant chose the installments, you will need to review your *Adoption Agreement* to see if your plan treats installment distributions as a series of payments or as a single payment for purposes of the change elections.

Changing the time and method of payment (i.e., payment elections) with respect to money already accrued requires following these general rules:

- For payment elections based on death or disability — Election changes cannot be effective until 12 months have elapsed from the date the change is elected.
- For payment elections based on separation from service or change in control — Election changes cannot be effective until 12 months after the election is made, and payment must be delayed for five years beyond the originally scheduled payment date.
- For payment elections based on a specified time or fixed schedule — Election changes cannot be effective until 12 months after the election is made, and the participant must make the election at least 12 months before the first scheduled payment and must delay payment for at least five years beyond the originally scheduled payment date.

D. Installments as a series or single payment

The decision in the plan as to how to classify the installments only matters if the participant wishes to change an election and is thus subject to the anti-acceleration and change rules of 409A. This is not an election regarding the frequency of the installment payments.

If the participant wishes to make a change, the following apply:

Installments treated as a single payment

- If elected 12 months prior to a payment event, the participant can elect to push out the beginning of the stream of payments by five years or can take a single sum withdrawal five years from the original payment event.
    - For example: If a participant elected 12 months before separation to receive installment payments over 20 years starting at separation from service, the participant can elect to (a) take a single sum withdrawal five years after separation or (b) start receiving the installment payment stream five years after separation.
- Once distributions begin, neither the participant nor the beneficiary may change the election (i.e., the installment payments will continue). In general, the only exception to this rule is where the participant elected at the time of the initial payment election to allow an intervening event (such as death, disability, etc.) to modify the payment election and specified the new payment option.

ADMINISTRATION OF PLAN

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Installments treated as a series of payments

- If elected 12 months prior to each year's payment, a participant can elect to push out any of the annual installment payments by five years, or the participant can take a single sum withdrawal five years after the last payment would have been paid.
    - For example: If a participant chose the installment over five years starting in 2020, then, if elected 12 months prior to January 1, 2020 (i.e., no later than January 1, 2019), the participant could delay the 2020 payment until 2025, but the other installment payments would continue to be made as scheduled (unless a timely election is made to push those payments).
    - Assume the same facts as above. If the participant wished to elect a lump sum payment, he or she would have to wait until 2030, i.e., five years after the last payment.
- Since this is seen as a series, the participant and beneficiary can delay payments after installments begin.
- The employer can make different elections for different individuals, but it may be easier to administer if the plan sponsor makes one election for all. You will need to determine if your *Adoption Agreement* allows this flexibility.

E. Requesting distributions

GuideStone relies on the plan sponsor to send notification when a triggering event has occurred. Once the event occurs, the participant will need to complete a form requesting distribution. GuideStone will not track payment events. If timely payments are not made, the participant may face penalties (see the "Consequences of violation" section of this manual).

8 | Withholding and reporting

The following is general information regarding the taxation of NQDC arrangements. More information can be found on the IRS website at *irs.gov/Businesses/Corporations/Nonqualified-Deferred-Compensation-Audit-Techniques-Guide*. While GuideStone cannot provide tax or legal advice, GuideStone is pleased to provide this information as a resource for your organization's NQDC plan. You should consult with your Payroll department or benefit counsel for more information and for the specific taxation rules applicable to your plans and organi-zation. In addition, participants are urged to seek counsel from their own tax advisors regarding these compli-cated issues.

A. FICA — (contributions to the plan)

NQDC amounts are taken into account for FICA tax purposes at the later of when the services are performed or when the substantial risk of forfeiture lapses. Vesting schedules are considered to be a substantial risk of forfeiture, and FICA is due at each increment in the vesting schedule. Thus, both employee deferral and employer contribution amounts are subject to FICA taxes at the time of deferral unless the employee is required to perform substantial future services in order for the employee to have a legal right to the future payment.

- If the employee is required to perform future services (either through a substantial risk of forfeiture or a vesting schedule) in order to have a vested right to the future payment, the deferred amount (plus earnings up to the date of vesting) is subject to FICA taxes when all the required services have been performed. You should contact GuideStone at the lapse of substantial risk of forfeiture or at each increment in the vesting schedule so that GuideStone can provide you with the account balance that is vesting and subject to FICA. Amounts must be reported correctly on IRS *Form W-2*.
- FICA taxes apply up to the annual wage base of $137,700 for 2020 and $142,800 for 2021, which may adjust annually for Social Security taxes and without limitations for Medicare taxes.
- If no substantial risk of forfeiture exists, a participant subject to FICA may already be earning above the Social Security wage base and thus no Social Security taxes are due on the amount deferred. However, unless a substantial risk of forfeiture exists, the amount deferred will be subject to Medicare taxes each year, which should be reported on the participant's annual *Form W-2*. For participants earning below the taxable wage base, contributions to the plan should be added to compensation from the employer to determine the FICA due.

B. SECA

SECA generally applies when amounts are received. Income tax and SECA taxes generally apply at the time of distribution. A special rule allows retirement benefits received by a minister from a church plan after the minister retires not to be subject to SECA taxes. Ministers should consult a tax advisor regarding reporting distributions.

C. Non-duplication rule

Once contributions are taken into account for FICA as described above (i.e., at the later of a lapse of substantial risk of forfeiture or when the services are performed), the non-duplication rule in the regulations provides that the earnings on the contributions are not subject to FICA. However, if the earnings are not reasonable, the non-duplication rule does not apply. In general, if the earnings are based on actual earnings on an investment, such as a mutual fund, the earnings will not be considered unreasonable.

D. Income tax withholding

When amounts become payable, they are includable in income and are reported as such on *Form W-2* for participants or *1099-MISC* for beneficiaries. If deferrals/contributions have not already been taken into account for FICA, employers should report the income for FICA. Employees subject to SECA should check with their tax advisor regarding the proper reporting.

E. *W-2* reporting requirements (special 409A reporting requirements)

As of the printing of this manual, the IRS has not yet finalized the 409A reporting requirements for annual deferrals/contributions, including earnings. The IRS has indicated that when regulations are effective, amounts deferred in a given year (including earnings) for an employee must be reported in Box 12 of the participant's *W-2* with a code of "Y."

ADMINISTRATION OF PLAN

(CONTINUED)

However, the IRS has not deferred the reporting of failures to comply with Code section 409A with a "Z." If there is a failure under Code section 409A and amounts must be taken into income, those amounts must be reported on the participant's *W-2* in Box 12 with a "Z." There are also additional penalties that must be reported by the participant on *Form 1040*.

*Note: The timing of when there is a payment of wages for FICA tax purposes is not affected by whether an arrangement is funded or unfunded.

F. Special reporting for ERISA employers

Employers who are subject to ERISA but who file a notice with the DOL within 120 days of the plan's inception are exempt from ERISA's annual *Form 5500* reporting requirements.

9| Consequences of violation

Code section 409A contains harsh tax penalties for non-compliance. The IRS imposes penalties on the participant, and employment taxes may be due from the employer. This fact makes it **imperative** that both the employer and the participants understand the plan and the requirements of 409A.

A. Violations

Violations may be due to the plan documents not being in compliance (documentation failure) or because certain actions violated both the plan and 409A (operational failure). In either case, the participant will be responsible for the penalties, although the employer may be responsible for certain employment tax issues. GuideStone will work with you to provide compliant documents.

B. Taxes and penalties

In the case of either violation, the penalties could include:

- Taxation — Immediate taxation for the amount of the deferred compensation in question that is fully vested to the participant. May require filing amended tax returns.
- Penalty — An additional 20 percent penalty tax on the deferred compensation in question.
- Interest — Underpayment interest penalties plus 1 percent for each year in which there was an underpayment.

C. Application of the penalties

Penalties will be applied differently depending on the type of violation. For documentation failures, all participants will be affected. For operational failures, only the participant(s) involved will be penalized.

ANNUAL CHECKLIST FOR 409A PLAN SPONSORS

Sponsoring a 409A plan is a good way to supplement retirement savings for your employees. As a sponsor of a 409A plan through GuideStone, you should be aware of the following important operational aspects of this type of plan:

Plan administration

- □ The plan must be operated in accordance with the terms of the 409A plan document and/or the internal policies and procedures (such as eligibility and contributions).
- □ Everyone involved in the day-to-day operation of the 409A plan should read the *Deferred Compensation Plan Administration Manual – 409A* and know how the plan should be operated.
- □ Failure to operate the plan in compliance with its terms may subject the participants to immediate taxation and penalties.

Eligibility to participate

- □ Review your eligibility schedule (*Exhibit B* of plan documents or, if the plan provides, in your internal policies and procedures) to ensure the names, positions or categories of employees are current. Be sure to delete outdated information.
- □ All appropriate paperwork must be filed (for example, copies of the *Enrollment Application and Payment Election Form* are filed with GuideStone and the originals are kept in your records).

Elections to defer compensation (as permitted in plan)

- □ Plan participants must meet the following deadlines to defer compensation from future salary:
  - □ New participants must complete the *Deferral Agreement* **within 30 days of becoming eligible to participate**; otherwise, compensation cannot be deferred until the upcoming tax year.
  - □ Existing participants must complete the *Deferral Agreement* **by December 31 of the current tax year** to defer compensation for the upcoming tax year unless an election for all future years is already in place (an evergreen election).
- □ All participants who elect to **defer discretionary, non-performance-based, bonus income** earned in the upcoming tax year (but payable in a subsequent tax year) must complete a *Deferral Agreement* by **December 31 of the current year.**
- □ Participants who elect to defer all or a portion of **performance-based compensation*** earned in the upcoming tax year must complete a *Deferral Agreement* at least **six months prior to the end of the performance-based service period.**

Elections regarding time and method of distribution (as permitted in plan)

- □ All plan participants must meet the following deadlines to elect the time and method of payments for future deferrals:
  - □ New participants must complete the *Payment Election Form* **within 30 days of becoming eligible** to participate, or distributions for the current year's contributions will be subject to the plan's default.
  - □ Existing participants must complete the *Payment Election Form* **by December 31of the current tax year** elections with respect to contributions made in the upcoming tax year unless there is an evergreen election in place.

ANNUAL CHECKLIST FOR 409A PLAN SPONSORS

(CONTINUED)

Notification of payment events

- □ Notify GuideStone immediately when a payment event** occurs in the current tax year for any participant. Ensure those participants who reach a payment event contact GuideStone promptly to request a distribution.

Elections to change the time or method of distribution (as permitted in plan)

- □ Participants who wish to change the time or method of distribution for prior years' accumulations must complete the appropriate form at least 12 months in advance of the first scheduled distribution. (Most requests to delay distributions must be for a minimum of five years after the originally scheduled payment date.)

Proper withholding and reporting

- □ Ensure the following:
  - □ FICA employees:
    - □ Taxation of contributions: All contributions to the plan (employee and employer) are subject to FICA at the time of deferral unless there is a risk of forfeiture (including a vesting schedule). FICA is due each time amounts vest. Contact GuideStone at each vesting event so GuideStone can provide you with the account balance that is vesting and subject to FICA. Amounts must be reported correctly on IRS *Form W-2*.
    - □ Taxation of distributions: Federal income tax withholding should be at the supplemental wage tax rate (refer to *IRS Publication 15*).

- □ SECA employees:
  - □ SECA employees should consult a tax advisor regarding proper reporting and can reference the *Nonqualified Deferred Compensation Plan Special Tax Consequences*.

Return forms to GuideStone

- □ Copies of all completed forms must be sent to GuideStone so that the participant's records may be updated. Be sure to keep originals of the completed forms for your records.

If you have any questions, please contact your GuideStone relationship manager.

This information should not be considered tax or legal advice. GuideStone stands ready to assist your organization as you work with your legal and tax advisors by providing resource information that you and your advisor may find beneficial.

*Generally, performance-based compensation is bonus compensation (1) based on services performed over a period of at least 12 months, (2) contingent upon the satisfaction of individual or organizational performance criteria that are not substantially certain to be met at the time the deferral election is permitted and (3) payable based on subjective performance criteria that relate to the employee's service and is not awarded based on a determination by the employee or any member of the employee's family.

**Payment events may include death, disability, attainment of a specific age, termination and other predetermined dates. Payment events can be located on your copy of the participant's *Payment Election Form* or in the plan documentation.

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