Brownstein

Catch-Up Contributions: Breathe a Sigh of Relief

BROWNSTEIN CLIENT ALERT, Aug. 30, 2023

On Friday, Aug. 25, 2023, the IRS released Notice 23-62, which (i) clarifies that plan sponsors may continue to allow participant "age 50" catch-up contributions after Dec. 31, 2023, and (ii) delays implementation of the mandatory Roth-ification of catch-up contributions for certain high-paid participants until the first taxable year after Dec. 31, 2025.

Take a Deep Breath: Catch-Up Contributions Can Continue After Dec. 31, 2023

Background: As many tax and benefits practitioners were quick to point out, Section 603 of the SECURE 2.0 Act completely eliminated Section 402(g)(1)(C) of the Internal Revenue Code (the "Code"), which was the statutory authority for catch-up contributions to be made. Plan administrators were concerned that they would have to terminate catch-up contributions after Dec. 31, 2023. In a May 23, 2023 letter to Treasury Secretary Janet Yellen and IRS Commissioner Daniel Werfel, the chairs and ranking members of the House Ways and Means Committee and the Senate Committee on Finance stated that it was the U.S. Congress' intent to require catch-up contributions by certain high-paid participants to be made on a Roth after-tax basis and to permit other participants to make catch-up contributions on either a pre-tax or a Roth after-tax basis. In other words, Congress did not intend to completely eliminate catch-up contributions.

Relief: Notice 23-62 now provides reliance on Congress' intention and states that 401(k) plans, 403(b) plans and governmental 457(b) plans may continue to operate as if Code Section 402(g)(1)(C) had not been deleted.

Take Another Deep Breath: Two-Year Delay for the Required Roth-ification of Catch-Up Contributions for Certain High-Paid Participants

Background: Section 603 of the SECURE 2.0 Act provides that catch-up contributions in 401(k) plans, 403(b) plans and governmental 457(b) plans made by an eligible participant whose preceding calendar year's FICA wages exceed $145,000 (as annually adjusted in $5,000 increments) are required to be made as designated Roth (after-tax) contributions. This change is effective for taxable years beginning after Dec. 31, 2023.

Plan administrators were concerned about their ability to implement this provision in less than 12 months (the SECURE 2.0 Act was enacted on Dec. 29, 2022, and actual implementation was required by Jan. 1, 2024), considering all of the plan amendments, administration systems changes, participant election processes and participant communications activities this change requires.

Relief: In Notice 23-62, the IRS announces that the first two taxable years after Dec. 31, 2023, will be treated as an administrative transition period for this purpose. This means that catch-up contributions for the affected group of high-paid participants are not required to be designated as Roth contributions until the first taxable year beginning after Dec. 31, 2025 (that is, Jan. 1, 2026, for a calendar year plan). ***Brownstein Comment***: With respect to this transition period, Notice 23-62 references "taxable years." It's unclear whether this reference is to plan years or participants' taxable years, but a clarification would be welcomed as this impacts how the two-year transition period applies to non-calendar year plans.

Brownstein Comment: We expect that the IRS will issue model plan language to help with amendments to address the transition period. If a plan has the wherewithal to implement the Roth-ification of catch-up contributions before the end of the transition period, it would seem that the plan would need to be amended *before* implementing that change, given the IRS guidance.

Exhale: Comments Please!

The Treasury Department and the IRS are expected to issue additional guidance regarding catch-up contributions to help plans implement the requirements under the SECURE 2.0 Act. Interested parties are to comment on any aspect of catch-up contributions. ***Comments are requested by Oct. 24, 2023***.

Some of the specific topics for which comments are sought include:

- ♦ May a pre-tax election be treated as an election to make Roth catch-up contributions or is a separate election required (for example, if there are excess deferrals as a result of ADP testing in a non-safe harbor plan and those are automatically recharacterized as catch-up contributions)? If a separate election is required, how should that election be administered and what is its timing?

- ♦ How should the wage limit apply to participants who do not have FICA wages (for example, partners in a partnership, or sole proprietors, or state or local government employees whose services are excluded from the definition of FICA employment)?

- ♦ Section 603 of the SECURE 2.0 Act states that prior-year FICA wages are taken into account only "from the employer sponsoring the plan." How should the FICA wage threshold apply if an employee is paid wages by more than one participating employer in the plan (even if the employers are in the same controlled group)? Should the FICA wage threshold apply separately to each employer or should it be an aggregate? What if an employee works for two or more unrelated employers with separate retirement plans?

- ♦ May a plan be designed to limit the ability to make Roth catch-up contributions to solely the affected group of high-paid participants who are required by law to do so or must the plan allow all eligible participants to designate some or all of their catch-up contributions as Roth contributions?

    - ◊ Alternatively, may a plan be designed to allow catch-up contributions to be made only by participants who are not subject to the Roth-ification provision?

Comments may be submitted electronically or in writing. We would be delighted to discuss any of your comments or concerns with the rules and assist with the drafting and filing of your comments.

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If you have questions or would like assistance on issues affecting your benefit plans, please contact us:

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