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Treasury and IRS Issue Proposed Rules for Roth Catch-up Contributions and Other Catch-up Contribution Changes Under SECURE 2.0 Act

[35991]January 20, 2025TO:ICI Members
Pension Committee
Pension Operations Advisory CommitteeSUBJECTS:Pension
TaxRE:Treasury and IRS Issue Proposed Rules for Roth Catch-up Contributions and Other Catch-up Contribution Changes Under SECURE 2.0 Act
The Department of Treasury (Treasury) and the Internal Revenue Service (IRS) recently issued proposed rules ("Proposal") to implement SECURE 2.0 Act changes to Code section 414(v).[1] Code section 414(v) permits a plan to allow participants aged 50 or over to make additional elective deferrals that are catch-up contributions, and also sets out the requirements for these contributions.

Background

SECURE 2.0 Act

Sections 109, 117, and 603 of the SECURE 2.0 Act amended section 414(v).

Section 109—Higher catch-up limit at ages 60, 61, 62, and 63. Effective for taxable years beginning after December 31, 2024, the limit on catch-up contributions for participants who turn 60, 61, 62, or 63 during a taxable year is increased to the greater of $10,000 ($5,000 in the case of SIMPLE plans) or 50 percent more than the regular catch-up amount in 2024 (2025 in the case of SIMPLE plans).[2] The SECURE 2.0 Act also instructs IRS to adjust these higher catch-up contribution limits annually for increases in the cost of living.

Section 117—Contribution limit for SIMPLE plans. Effective for taxable years beginning after December 31, 2023, section 117 increases the annual deferral limit for SIMPLE plans, and the catch-up contribution limit that applies at age 50 for SIMPLE plans, to 110 percent of the otherwise applicable limits in 2024 (and indexed thereafter). These increased limits are available to employers with no more than 25 employees; for employers with more than 25 employees and not more than 100 employees, the increased limits are available only to those employers who make enhanced employer contributions on behalf of employees (either a 4 percent matching contribution or a 3 percent non-elective contribution). Section 117 also requires Treasury to study and report to Congress on SIMPLE plans.[3]

Section 603—Roth treatment of certain "catch-up" elective deferrals. Effective for taxable years beginning after December 31, 2023, all future catch-up contributions by employees aged 50 or older to a 401(k), 403(b), or governmental 457(b) plan must be made as Roth contributions; unless the employee earned no more than $145,000 (indexed) from the from the employer sponsoring the plan in the prior taxable year.

Notice 2023-62

IRS in August 2023 issued Notice 2023-62, which provided interim guidance for implementing the Roth catch-up requirements of section 603.[4] Notice 2023-62 addressed some concerns expressed by ICI, along with many retirement service providers and other parties, as to the need for guidance to implement section 603.[5] To summarize, Notice 2023-62:

- Provided for a two-year delay of the requirements of section 603, until taxable years beginning after December 31, 2025;
- Clarified that during this two-year "administrative transition period" plans will be treated as complying with section 603, even if catch-up contributions by participants otherwise required to make Roth catch-up contributions are not made on a Roth basis;
- Clarified that during this administrative transition period plans need not add a Roth option to be considered as complying with section 603;
- Confirmed that the limitation on the permissible amount of elective catch-up contributions in a taxable year is aggregated across plans, notwithstanding associated changes to the Code in section 603 (specifically, the elimination of Code section 402(g)(1)(C));
- Noted that further guidance as to the implementation of section 603 is forthcoming, and indicates IRS and Treasury's positions on numerous issues; and
- Requested comments to assist with future guidance.

IRS and Treasury specifically noted that they anticipated issuing guidance addressing the following, among other issues.

- Guidance clarifying that if an eligible participant did not have FICA wages from the sponsoring employer in the prior year, the requirement to make Roth catch-up contributions would not apply to them.
- Guidance that a plan administrator/employer may treat an election by an affected participant to make catch-up contributions on a pre-tax basis as an election to make Roth catch-up contributions.
- Guidance addressing a number of issues for plans maintained by more than one employer (including multiemployer plans), including that each employer in the plan is treated as a separate employer for determining prior year FICA wages.

ICI submitted a comment letter in which we recommended these and other items be included in future guidance.[6] The Proposal is the future guidance contemplated by Notice 2023-62. We note below where the Proposal reflects an ICI recommendation.

Proposed Rules for Roth Catch-Up Contributions

The Proposal includes the following provisions (among others), many of which ICI recommended.

Deemed Roth election

The Proposal would add 26 C.F.R. § 1.401(k)-1(f)(5)(iii), which—for taxable years beginning after December 31, 2023—would permit a plan to provide that any participant subject to the Roth catch-up contribution requirement is deemed to have irrevocably designated any catch-up contributions as Roth contributions. Where a plan provides for deemed Roth catch-up elections, the plan must treat such deemed Roth catch-up contributions as not excludable from gross income and maintaining the contributions in a designated Roth account. The plan also must provide participants with an effective opportunity (as determined based on all relevant facts and circumstances) to make a different election, such as deciding to cease elective deferrals.

As requested by ICI, a plan may provide for deemed Roth catch-up contributions irrespective of whether the plan requires separate elections for catch-up contributions or uses a spillover design for catch-up contributions.[7]

Determining the $145,000 FICA wage threshold

The Proposal confirms that a participant must have prior calendar year FICA wages of more than $145,000 (as adjusted) *from the employer sponsoring the plan* in order to be subject to the Roth catch-up contribution requirements.[8] Other prior wages do not count towards this wage threshold, including FICA wages taken into account in a different year for tax purposes, self-employment income, non-FICA cash compensation, partnership income, and other types of wages.[9] Prior year FICA wages are based on actual FICA wages; if an employee was hired in the middle of the prior year their FICA wages are not prorated for that year.[10]

In a multi- or multiple employer plan, each employer is a separate common law employer. As such, a participant in such a plan who has more than $145,000 in prior year FICA wages from one participating employer may still be eligible to make non-Roth catch-up contributions if employed by a different participating employer in the current year.

Roth catch-up contributions may not be made selectively available

The Proposal requires, consistent with Code section 414(v)(7)(B), that if *any* catch-up eligible participant subject to the Roth catch-up requirement is permitted to make catch-up contributions as Roth contributions under an applicable plan for a given plan year, then *all* catch-up eligible participants must be allowed to make catch-up contributions as designated Roth contributions for that plan year. This requirement is still satisfied where a plan covers employees in both the US and Puerto Rico, and the plan permits catch-up eligible participants in Puerto Rico to make catch-up contributions as after-tax contributions under the Puerto Rico Internal Revenue Code.[11]

Designated Roth contributions later treated as catch-up contributions

The Proposal would permit plans to take into account designated Roth contributions that are made prior to an applicable limit being reached for purposes of determining whether the Roth catch-up requirement is satisfied.[12] In other words, if a catch-up eligible participant's total elective deferrals that are designated Roth contributions over the course of a calendar year or taxable year equal or exceed the total elective deferrals that are determined to be catch-up contributions, then the participant would satisfy the Roth catch-up requirement. ICI requested this flexibility.

Plans that do not include designated Roth contributions

Under the Proposal, if a plan does not have a qualified Roth contribution program, the plan may allow for catch-up contributions by participants not subject to the Roth contribution requirement, even though those who are subject to the Roth contribution requirement would not be able to make catch-up contributions. The Proposal indicates that this plan design would not violate the universal availability requirement.[13] The Proposal acknowledges that a plan operating pursuant to such an arrangement could risk failing non-discrimination testing because some non-highly compensated individuals would be precluded from making catch-up contributions (due to the $145,000 FICA wage limit being less than the wage threshold for being considered a highly compensated employee). In this context, the plan may address this testing failure by precluding one or more participants who are highly compensated employees and who are not subject to the Roth catch-up requirement (e.g., because the participant did not receive FICA wages for the preceding year) from making catch-up contributions, if such exclusions facilitate the plan's satisfying 26 C.F.R. § 1.401(a)(4)-4 as to the nondiscriminatory availability of benefits, rights, and features.[14]

Treasury and IRS declined to provide for an alternative plan design recommended by ICI and other commenters where all catch-up contributions would be made as designated Roth contributions.[15] Such as requirement would, in Treasury and IRS' view, be inconsistent with Code section 402A(b)(1).

Correction methods for violations of Roth catch-up contribution requirements

The Proposal provides multiples ways for a plan to correct violations of the Roth catch-up contribution requirements.[16] Absent correction, a plan would fail to be qualified.

First, the Proposal notes that as under existing rules, a plan may correct a pre-tax deferral in excess of an applicable limit by distributing the excess elective deferrals to the participant in accordance with a permitted correction method specific to the elective deferral limit that was exceeded (i.e., existing correction methods for elective deferrals exceeding the section 401(a)(30) limit, the section 415(c) limit, or the ADP limit).

The Proposal would permit two additional correction methods whereby a pre-tax elective deferral that exceeds an applicable limit could be treated as a designated Roth contribution in order to satisfy the Roth catch-up requirement. To use these new methods, the plan sponsor or plan administrator must have practices and procedures in place at the time the elective deferral is made that are designed to result in compliance with Code section 414(v)(7), which practices and procedures must include providing for deemed Roth catch-up elections. These additional correction methods are in response to comments, including ICI's recommendation to permit correction by in-plan Roth rollover.

Under the first new method, a plan could transfer the excess pre-tax contribution (adjusted for allocable gain or loss) to a designated Roth account in the plan and report the contribution (not adjusted for allocable gain or loss) as a designated Roth contribution on the participant's Form W-2 for the year of the deferral. Effectively, this method would include the contribution in gross income as if it had been correctly made as a designated Roth contribution. This correction method would not be available if the participant's Form W-2 for that year has already been filed or furnished to the participant.[17] The Proposal notes that this correction method generally will not be available for an elective deferral treated as a catch-up contribution because it exceeds the plan's applicable ADP limit.

Under the second new method, a plan could correct the excess pre-tax contribution through an in-plan Roth rollover where the excess deferral (adjusted for allocable gain or loss) is directly rolled over from the participant's pre-tax account to a designated Roth account, and the adjusted amount is reported as an in-plan Roth rollover on Form 1099-R.

The deadline for correction varies, depending on which limit is the basis for the pre-tax elective deferral being designated as a catch-up contribution.[18] An elective deferral that is a catch-up contribution because it exceeds the Code section 401(a)(30) limit on elective deferrals must be corrected by April 15 of the calendar year following the calendar year for which the elective deferral was made. If an elective deferral is a catch-up contribution because it resulted in a participant's annual additions exceeding the Code section 415(c) limit, the correction must be made by the deadline that applies for allocating amounts to the limitation year for which the elective deferral was made. Where a pre-tax catch-up contribution exceeds the ADP limit, the correction must be made within 2½ months (6 months for a plan that includes an eligible automatic contribution arrangement under Code section 414(w)) after the close of the plan year for which the excess contribution was made.

Proposed Rules Addressing Increased Catch-Up Contribution Limits for Participants Aged 60-63 and for SIMPLE Plans

The Proposal would (1) reflect the increased applicable dollar catch-up limits permitted under sections 109 and 117 of the SECURE 2.0 Act (along with updated cost-of-living adjustments) as discussed above,[19] including the different limits applicable to different SIMPLE plan structures; and (2) clarify that a plan would not fail to satisfy the universal availability requirement under Code section 414(v)(4) merely because the plan utilizes the permitted increased catch-up limit for participants attaining age 60 through 63. The Proposal, in footnote 6, also confirms that the enhanced catch-up contribution for participants aged 60 through 63 is optional, and a plan may limit catch-up contributions for those participants to the same dollar limit that applies to all other catch-up eligible participants.

Applicability Dates of the Proposal

The Proposal generally would apply with respect to taxable years beginning more than six months after the regulations are finalized. Taxpayers may elect to have certain provisions apply earlier, namely for taxable years beginning in 2024 for higher catch-up limits for certain SIMPLE plans, and for taxable years beginning in 2025 for higher catch-up contribution limits for individuals reaching 60-63 years old during a taxable year. **Note that the Roth catch-up requirement will become applicable in 2026 regardless of when the final regulations apply.**

Plans maintained pursuant to a collective bargaining agreement have potentially later applicability dates for the Roth catch-up regulations, which would apply to contributions to such plans in taxable years beginning after the later of (i) the first taxable year beginning six months after the date that final regulations are issued, or (ii) the first taxable year that begins after the termination of the last collective bargaining agreement in effect on December 31, 2025.[20] ICI had requested this flexibility in the applicability dates of the Proposal for multiemployer plans. Any plan (including a collectively bargained plan), however, may elect to apply the Roth catch-up regulations earlier, i.e., with respect to contributions in taxable years beginning after December 31, 2023.

Proposal Comment Period and Public Hearing

Treasury and IRS request comments on all aspects of the Proposal.[21] Comments on the Proposal are due March 14, 2025. Treasury and IRS also plan to hold a public hearing on the Proposal on April 7, 2025.

David Cohen
Associate General Counsel, Retirement Policy

Notes

[1] The Proposal was published in the Federal Register January 13, 2025. 90 Fed. Reg. 2645 (2025), available at https://www.federalregister.gov/documents/2025/01/13/2025-00350/catch-up-contributions. For a summary of the SECURE 2.0 Act, see ICI Memorandum No. 34795, dated January 12, 2023, available at https://www.ici.org/memo34795.

[2] The discrepancy in the base year of adjustment for SIMPLE plans and other plans could be addressed in technical corrections to the SECURE 2.0 Act. Section 101(e) of the SECURE 2.0 Act Technical Corrections Discussion Draft released in December 2023 would amend subparagraph (E) of section 414(v)(2) by striking "2024" in clause (i)(II) and inserting "2025". See announcement dated December 6, 2023, available at https://waysandmeans.house.gov/2023/12/06/secure-2-0-act-technical-corrections-discussion-draft-released/.https://waysandmeans.house.gov/2023/12/06/secure-2-0-act-technical-corrections-discussion-draft-released/.

[3] While the report was due by the end of 2024, as of the date of this memorandum we find no record that it has been provided.

[4] Notice 2023-62, available at https://www.irs.gov/pub/irs-drop/n-23-62.pdf. For a summary of Notice 2023-62, see ICI Memorandum No. 35426, dated August 30, 2023, available at https://www.ici.org/memo35426.

[5] See Letter to IRS and Treasury from ICI and other signatories, dated July 19, 2023, see ICI Memorandum No. 35380, dated July 20 2023, available at https://www.ici.org/memo35380; Letter to US Congress from ICI and other signatories, dated June 29, 2023, see ICI Memorandum No. 35365, dated July 3, 2023, available at https://www.ici.org/memo35365; Letter to IRS and Treasury from Elena Chism and Shannon Salinas, dated March 23, 2023, see ICI Memorandum No. 35218, dated March 28, 2023, available at https://www.ici.org/memo35218 ("SECURE 2.0 Letter").

[6] Letter to IRS from Elena Chism and David Cohen, dated October 24, 2023, see ICI Memorandum No. 35496, dated October 24, 2023, available at https://www.ici.org/memo35496 ("Notice 2023-62 Comment").

[7] In a spillover design for catch-up contributions, elective deferrals are automatically considered to be catch-up contributions once a participant reaches the plan's limit on non-catch-up elective deferrals.

[8] Code section 414(v)(7) does not define "employer sponsoring the plan." The Proposal looks to the definition of "employer" for FICA purposes in determining that "employer sponsoring the plan" in this context refers to an individual's common-law employer, and not to other entities treated as a single employer under Code section 414 (b), (c), (m), or (o).

[9] Other types of wages that do not count for purposes of determining the applicability of the Roth catch-up requirement include wages under section 3131 of the Railroad Retirement Tax Act, and State or local government employees whose services were

excluded under the definition of employment under Code section 3121(b)(7). 90 Fed. Reg. at 2649.

[10] 90 Fed. Reg. at 2650.

[11] The Puerto Rico Code does not provide for designated Roth contributions.

[12] 90 Fed. Reg. at 2650.

[13] *Id.* n.9.

[14] *Id.* at 2651.

[15] See *Id.* at 2653 n.16.

[16] 90 Fed. Reg. at 2652-54.

[17] The Proposal does not address why an amended Form W-2 could not be provided to a participant.

[18] 90 Fed. Reg. at 2654.

[19] For a taxable year beginning after 2024, the enhanced catch-up limit for those aged 60 through 63 is $11,250 for a plan other than a SIMPLE plan, and $5,250 for a SIMPLE plan (and these limits are adjusted in subsequent years for changes in the cost of living). For a taxable year beginning after 2023, the higher catch-up limit for certain SIMPLE plans under section 117 of the SECURE 2.0 Act is $3,850, adjusted in subsequent years for changes in the cost of living.

[20] 90 Fed. Reg. at 2652. The timeframe relative to the termination of collective bargaining agreements applies without regard to any extension of such collective bargaining agreements.

[21] In addition to the general request for comments, the Proposal specifically requests comments in certain areas, including on the application of catch-up contribution limits to an employee who performs service for an employer in both the US and Puerto Rico in the same year. 90 Fed. Reg. at 2649.
