

IRS Announces Administrative Transition Period for SECURE Act 2.0 Catch-Up Contribution Provisions

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Catch-up contributions permit participants age 50 and older to make additional elective deferral contributions to their employer-sponsored defined contribution plan. While offering catch-up contributions is not a legal requirement, they are a popular feature of many 401(k), 403(b), and 457(b) plans.

Under prior law, all participants could make catch-up contributions on a pre-tax basis, and participants in a plan that offered both catch-up and Roth contributions could also designate catch-up contributions as Roth contributions, *i.e.*, after-tax. Plans are not required to offer a Roth option, and the feature is more common in 401(k) plans than in 403(b) or 457(b) plans.

These rules changed pursuant to the SECURE Act of 2022 (“SECURE 2.0”), enacted as part of the Consolidated Appropriations Act of 2023. Effective for taxable years beginning after December 31, 2023, catch-up contributions of participants with wages of \$145,000 or greater for the preceding calendar year must be made on a Roth basis.^[1] Wages are determined with reference to wages for purposes of FICA withholding, as adjusted for cost-of-living increases.

This new Roth catch-up rule has raised a number of legal and implementation concerns for affected plans.

- Plans that offer catch-up contributions but do not currently provide for Roth contributions must be formally amended to add a Roth feature. In the case of governmental plans, the plan amendment process may require contractual revisions and legislative approval.
- Plans that already offer both catch-up and Roth contributions also require amendment to add the new rule, including a reference to FICA wages. This is not one of the existing IRS safe harbor definitions of compensation, and few plans currently reference it. Further, some types of remuneration for employment are not considered wages subject to FICA withholding, and SECURE 2.0 is silent on the treatment of catch-up contributions in that scenario.
- The interaction of the various statutory revisions to the Internal Revenue Code (“Code”) adding the new Roth catch-up rule actually appears to eliminate all catch-up contributions effective December 31, 2023. While this is undoubtedly an unintended drafting error contrary to the clear purpose of the rule, it is nonetheless how SECURE 2.0 literally reads.

The retirement industry has been coordinated and vocal in identifying these concerns and asking for formal guidance or transition relief in advance of the January 1, 2024 statutory compliance deadline. On May 23, 2023, the Chairmen and Ranking Members of the Senate Finance and House Ways and Means Committees publicly stated in a “four corners” letter to Treasury Secretary Janet Yellen and IRS Commissioner Daniel Werfel that Congress did not intend to disallow catch-up contributions and intended to introduce technical corrections legislation to correct that and possibly other erroneous statutory language.

That legislation has not been introduced as of the date of this client alert. However, on Friday, August 25, 2023, the IRS issued Notice 2023-62 (“Guidance on Section 603 of the SECURE 2.0 Act with Respect to Catch-Up Contributions”). Notice 2023-62 provides as follows.

- Employer plans will not be treated as failing to meet any Code requirement solely because the plan permits an eligible participant to make catch-up contributions in any plan year. This effectively acknowledges the drafting error that appeared to eliminate the ability to make catch-up contributions altogether.
- The first two taxable years beginning after December 31, 2023 will be regarded as an administrative transition period with regard to the new Roth catch-up rule. This means that:
 - until taxable years beginning after December 31, 2025, catch-up contributions that otherwise satisfy the applicable requirements will be treated as catch-up contributions even if they are not designated as Roth contributions; and
 - a plan that does not provide for Roth contributions will nonetheless be treated as satisfying the requirement to do so.

Notice 2023-62 also states that the Treasury Department and the IRS intend to issue further guidance to assist taxpayers with the implementation of Section 603 of SECURE 2.0, which is expected to include (1) clarification that the new Roth catch-up rule would not apply to a participant who does not have FICA wages, (2) permission for an employer to treat a participant election to make pre-tax catch-up contributions as an election to make Roth catch-up contributions, *i.e.*, that the new Roth catch-up rule will apply automatically to affected participants, and (3) guidance that a plan maintained by more than one employer will not aggregate wages from more than one employer when applying the new Roth catch-up rule.

Notice 2023-62 is welcome and timely. Plan sponsors and service providers can proceed with their 2023 fourth quarter activities without uncertainty about how to implement and operationalize the new Roth catch-up rule. Further, the two-year administrative transition period should provide sufficient time for Congressional action before or after the 2024 elections, and for the IRS to issue more comprehensive guidance.

For further assistance with these and the many other retirement plan provisions of SECURE 2.0, as well as retirement plan design and compliance more generally, please contact Ronald G. Cluett or Richard W. Skillman.

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[1] SEPs and SIMPLE retirement accounts are exempt from the requirement.

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