JOURNAL of PENSION BENEFITS

ISSUES IN ADMINISTRATION, DESIGN, FUNDING, AND COMPLIANCE
Volume 33 • Number 2 • Winter 2026

Catching Up on Catch-Up—(OK, That IS the Most Obvious Article Title EVER)

BY ILENE FERENCZY

This article provides a detailed discussion of the final regulations in September regarding the catch-up contributions for people ages 60-63 and those catch-up provisions related to Roth amounts.

It's long awaited. Or long dreaded. But, the new catch-up rules are effective January 1, 2026, and the final regulations are issued. Now, what do we do?

The final regulations (Final Regs), issued on September 16, 2025, contained two sections of note. The first dealt with the increased catch-up contribution availability for people ages 60-63. This uncontroversial section engendered a few open questions to be answered, and the Treasury endeavored to answer them. We'll discuss them below.

By far the more important, confusing, disadvantaging rules from the SECURE 2.0 Act of 2022 are those related to the need of some participants to have any catch-up contributions classified as Roth amounts. That was the guidance everyone awaited with dread, and that will be addressed in the bulk of this article.

Ilene Ferenczy, Esq. is managing partner of Ferenczy Benefits Law Center in Atlanta, GA and Co-Editor-in-Chief of the *Journal of Pension Benefits*.

The Final Regs are effective as of January 1, 2027, even though the Internal Revenue Code (Code) sections that they modified are changed as of earlier dates (discussed below). That means that practitioners can use a good faith interpretation of the law in the meantime. What does that mean? It is not definitive, so the safest course of action is to follow the Final Regs (or, at least, the proposed regulations) to the extent possible.

Age 60-63 Catch-Up Increase (SECURE 2.0 Section 109, Code Section 414(v)(2)(B))

This available larger catch-up contribution provision was effective as of January 1, 2025.

Under Code Section 414(v)(2)(B), individuals who are age 60-63 may contribute greater catch-up contributions than other participants, specifically 150 percent of the normal catch-up limit (60-63 Limit), which is an increase from the normal $7,500 limit to $11,250 for 2025 for 401(k), 403(b), and governmental 457(b) plans. [Treas. Reg. §1.414(v)-1(c)(2)(i)] (As usual, 457(b) plans sponsored by tax-exempt organizations are at a disadvantage and are not able to adopt this increased limit.) Catch-up contributions under Savings Incentive Match Plan for Employees (SIMPLE) Plans increased to $5,250. [Treas. Reg. §1.414(v)-1(c)(2)(ii)]

For a participant to qualify for the increased catch-up limit, two requirements must be met. First, the participant must attain age 60, 61, 62, or 63 on their birthday in the relevant calendar year. In other words, those who turn 64 during the year are not able to make the increased catch-up amount. [Treas. Reg. §1.414(v)-1(c)(2)(i)(B)] Second, and this was an open issue addressed by the Final Regs, the plan document must specifically authorize the increased catch-up. [FR Doc. 2025-17865 (filed Sept. 15, 2025), Summary of Comments and Explanation of Revisions (Preamble), Section II.A] This means that all plans that offer this to their participants must be amended as part of the SECURE amendments due (for most nongovernmental plans) by the end of 2026 to so permit. (They can permit the use of the 60-63 Limit in the interim, so long as the amendment is adopted timely.)

The other open question about these rules that was addressed by the Final Regs has to do with whether a plan allowing the additional catch-ups has to permit all participants between the ages of 60 and 63 to contribute an additional amount, and also whether the larger available amount has to be the full 150 percent of the normal limit. (Why a plan would want to limit the ability of people to defer to something less than the maximum available to them is a cypher to me, but if there is a possible variation on a plan design, it's axiomatic that someone out there will want to use it.) The Final Regs make it clear that limiting the additional catch-up contributions to certain people or an amount something less than the full 60-63 Limit would violate the Universal Availability Rule and potentially be discriminatory as to benefits, rights, and features. The Universal Availability Rule generally requires that catch-up contributions be made available to everyone if they are available at all. The Treasury interpreted this rule for purposes of both the 60-63 Limit and the Roth catch-up rules to provide that the Universal Availability Rule is met if:

> each catch-up eligible participant who participates under any applicable employer plan maintained by the employer is provided with an effective opportunity to make the maximum amount of catch-up contributions *permitted for that participant* under Section 414(v). [Preamble, Section II.C, Emphasis added]

Therefore, if a plan makes this higher limit available (and it may choose not to do so at all), it must permit each participant to make the highest contribution for which they are eligible. Furthermore, all plans of the employer must also so provide. The lowdown: can't limit the people; can't limit the limit.

The same concept applies under the Final Regs in relation to nondiscrimination. The Preamble provides that Code Section 401(a)(4) nondiscrimination rules are not violated if all participants can make the largest catch-up contribution affordable to them under the law, notwithstanding that the limit is greater for those aged 60-63 than for other participants. [*Id.*]

Roth Catch-Ups (SECURE 2.0 Section 603, Code Section 414(v)(7))

Enough of the opening act. Let's get to the real show.

SECURE 2.0, Section 603, added a new Code Section 414(v)(7), which requires that the catch-up contributions for certain individuals must be made as Roth contributions (Roth Catch-up Rules). The effective date of the statute was taxable years beginning on or after January 1, 2024. Internal Revenue Service (IRS) Notice 2023-62 provided that the first two years of applicability would not be enforced. Therefore, Code Section 414(v)(7) is first applicable for tax years beginning January 1, 2026.

To make proper sense of the new rules, one must understand the basic requirements for Roth contributions. These are:

- A participant must irrevocably designate a deferral as a Roth amount (as opposed to a pre-tax deferral) prior to payday. Such a designation cannot be made retroactively.
- The employer must treat the amount made as a Roth contribution as an after-tax amount, including it as income on the Form W-2 and determining tax withholding appropriately.
- The Roth amount must be deposited into a designated Roth account, not into the pre-tax account. [Code § 402A]

The conundrum this produces is that it may not be known at the time that a deferral is contributed to the plan that it will ultimately be a catch-up contribution. This is because a deferral becomes a catch-up contribution in one of four ways:

1. *It is a deferral in excess of the Code Section 402(g) deferral maximum*. In absence of an error, this is something that both the plan sponsor and the plan administrator should be able to identify at the point of deposit; all they need to know is how much was contributed to the plan during the calendar year before the excess is deferred.
2. *It is a deferral in excess of a limit outlined in the plan document*. Again, assuming that the limit is outlined prior to the deferral being made, the plan sponsor and the plan administrator should have all available information at the point of deferral to identify this.
3. *It is a deferral by a highly compensated employee (HCE) in excess of the Actual Deferral Percentage (ADP) Testing Limit*. As the ADP nondiscrimination test is performed after the end of the year—sometimes nearly a full year after the end of the year—it is commonly not possible to know that the deferral is a catch-up contribution until long after it is deposited to the plan.
4. *It is a deferral in excess of the available limit on annual additions under Code Section 415*. As annual additions include employer contributions, forfeiture allocations, and after-tax employee contributions in addition to the salary deferrals by participants, one cannot identify a Code Section 415 excess until after all deposits are made for the plan year—commonly not until the employer's tax return due date, occurring in the following year. Again, this is long after deferrals are made to the plan. [Code § 414(v)(5)]

The mission of the Treasury regulations, therefore, in addition to explaining how the Roth requirement works generally, was to find a way to make the Roth requirement work within a context that complies with the general Roth rules. As this is not objectively possible for the reasons outlined below, the Treasury had to promulgate regulations that were within the scope of the previously existing law while accommodating the practical needs of compliance. That mean feat may explain a lot of the complications embodied in the Final Regs.

To Whom Do the Roth Catch-Up Rules Apply? Getting Hip about HPIs

It would have been nice if the Roth Catch-up Rules applied to HCEs. That would give us a usable definition with which we are familiar, and would also align the application of these rules well within the normal nondiscrimination requirements. However, it appears that this would not have produced enough taxable income for the Treasury to make SECURE 2.0 revenue neutral. As a result, a new category of employee has been created for the sole purpose of the application of the Roth Catch-up Rules … and then was not given a name at all. In our office, we have coined the phrase, "Highly Paid Individual" or "HPI" for these lost souls.

An HPI is someone who, in the prior calendar year (the Lookback Year), earned FICA wages in excess of the applicable limit, which is $145,000 for 2025, and will increase periodically for cost-of-living. [Code § 414(v)(7)(A), Treas. Reg. § 1.414(v)-2(a)(2)] FICA wages are those used to determine someone's taxes for the Old Age, Survivors, and Disability Insurance elements of Social Security payroll taxes. That information is found on Box 3 of a participant's Form W-2, as clarified under the Final Regs. [Preamble, Section III.A.1] Some have wanted to use Box 5 (Medicare Wages) instead. The difference between the two Form W-2 entries for nongovernmental employees is that Box 3 is limited to the Social Security Taxable Wage Base and Box 5 is not. The Final Regs permit one to use Box 5 for 2026 as a "good faith interpretation" of the Final Regs before they are officially effective. As the FICA wage limit for catch-up purposes is below the wage base, the limitation is of no practical effect for the Roth catch-up purposes. There are some other differences for some state and local workers, so Box 3 is the place to be in 2027 and later years.

It is noteworthy that there are people who do not have FICA wages, including some governmental workers and some scattered religious groups. However, the most important category of non-FICA people are self-employed individuals—generally sole proprietors and partners—who do not have W-2 income at all, but pay their Social Security taxes as part of the self-employment taxes reflected on their Forms 1040. The result: for unincorporated entities, the people whose "compensation" for plan purposes is Earned Income will not be HPIs and will be able to make full catch-up contributions, if permitted by their plan. [*Id.*]

When determining the HPIs for 2026, do we use the FICA limit for 2025 (that is, for the Lookback Year) or whatever the new limit is for 2026? It's not clear from the Final Regs, but it is reasonable to assume that the HPI rules will follow the HCE determination rules, which also use a lookback to the prior year's compensation. This assumption is also supported by language in IRS Notice 2025-67 (the notice that announced the cost of living adjustments for retirement plan limits for 2026), which states, "The Roth catch-up wage threshold for 2024, which under Section 414(v)(7)(A) is used to determine whether an individual's catch-up contributions to an applicable employer plan (other than a plan described in Sections 408(k) or (p)) *for 2026* must be designated Roth contributions, remains $145,000." [Emphasis added] Therefore, we assume that you will use the $145,000 limit in relation to the 2025-year FICA wages, for purposes of the HPI status of an employee in 2026.

More About HPI Compensation

Consistent with the previously proposed regulations, the Final Regs permit an employee's HPI status to be determined on a common-law-employer by common-law-employer basis. [Treas. Reg. § 1.414(v)-2(b)(4)]

This means that compensation earned by a participant from each adopting employer in a multiple employer plan, pooled employer plan, or multiemployer plan and the employee's HPI status is separately determined and applied. That makes perfect sense, and should not be particularly hard to administer, as the benefits earned in relation to each adopting employer in such plans are usually separately determined.

Things are more complex for related employers. Individuals who work for two or more companies that are related through a controlled or affiliated service group will have their HPI status determined separately for each such company. This means, for example:

- If Marjorie works for related Companies A and B, and earns $151,000 from Company A and $20,000 from Company B, she will be an HPI in relation to catch-up contributions made from her Company A pay but not for those made from her Company B pay, even if it's all part of one big plan.
- If Zachery also works for A and B earning $75,000 for each company, he is not an HPI at all for either company.

While this benefits the employees, giving them the maximum flexibility for making pre-tax deferrals, it can wreak havoc on the plan(s) administratively. Therefore, the Final Regs permit (but do not require) the plan to apply the HPI limits across all related employers if it chooses to do so. [Treas. Reg. § 1.414(v)-2(c)(4)(iii)] If one company acquires the assets of another, employees that follow the sale may be treated as working for one employer (even if two W-2 Forms are issued) if the buyer constitutes a "successor employer" under Treasury Reg. § 31.3121(a)(1)-1(b). [Treas. Reg. § 1.414(v)-2(c)(4)(iv)] In that case, the total FICA compensation paid by both of the companies may be counted for HPI purposes. You will need to talk to the accountant to know if this rule can apply. The third situation permitting aggregation is when the common law employer uses a common paymaster in accordance with Code Section 3121(s). The employee's compensation from the common law employer may be aggregated with that of one or more of the other companies using the common paymaster, if so specified. [Treas. Reg. § 1.414(v)-2(c)(4)(ii)]

There's one more aggregation situation of which you need to be aware, and this one is mandatory. The Final Regs require aggregation of compensation if the participant is paid by both a sole proprietor and a disregarded business that the sole proprietor owns. [Treas. Reg. § 1.414(v)-2(c)(4)(v)] (You will need to get the accountant's cooperation in this situation, too, to determine if this rule applies.)

The language of the Final Regs indicates that the common law employer method of determining compensation is the standard, and the "plan must provide" for any aggregation. Therefore, the SECURE amendment will need to provide for any aggregation of employers that is used. [Treas. Reg. § 1.414(v)-2(b)(4)]

All HCEs Are HPIs … Except When They're Not—Nondiscrimination Implications

As HCEs usually encompass people making more than $160,000 (in 2026) and the HPI compensation limit is $150,000, and they both increase for cost-of-living, all HCEs are HPIs, right?

Wrong. But nice try.

First, as we discussed earlier, not all compensation counts for HPI purposes. So, an HCE whose compensation derives from non-FICA wages such as self-employment income, will not be an HPI. Second, some people become HCEs due to stock ownership, particularly relatives of the bona fide owner. Compensation does not attribute to others in the way that ownership does. So, those HCE relatives will be HPIs only if their own compensation exceeds the HPI limit.

That means, of course, that some nonhighly compensated employees (NHCEs) will have to make their catch-up contributions as Roth and some HCEs won't. Is that discriminatory? No. As noted earlier, the Final Regs make it clear that, so long as everyone gets to make catch-up contributions of the same amount, we are in good shape, regardless of whether or not they need to be made as Roth.

But, there's more (of course there is). What if the plan does not make Roth contributions available? Now we have a circumstance where the dollar amount of catch-up contributions available to HCEs could exceed that available to similarly situated NHCEs (in that the catch-up contributions available to HPIs would be zero). While we do not have a Universal Availability Problem, as discussed above, we now have a potential benefits, rights, and features issue.

The Final Regs provide a "safe harbor" solution to the discrimination concern in plans that do not offer Roth contributions. Under this solution, the plan should provide that HCEs will be treated as HPIs if their plan compensation, regardless of whether it counts for FICA purposes, exceeds the $150,000 limit. [Preamble, Section III.B.2] By doing this, no HCE may make a catch-up contribution that is unavailable to a similarly situated NHCE, so there is no discrimination. Of course, the impact of this is to treat a non-HPI as if they were catch-up limited, but that's the breaks for the folks who sit in the big offices.

Many who reviewed the proposed regulations were concerned that a failure to provide for Roth contributions would create a discrimination or Universal Availability Rule problem in the plan, because HPIs in such situation cannot make catch-up contributions. Some of such companies adopted Roth provisions, anticipating this issue.

The Final Regs clarify that, except as discussed above in relation to NHCE HPIs, a plan will not fail either discrimination or Universal Availability if it does not permit Roth contributions. [Preamble, Section III.B.2] Therefore, plans that want to avoid making Roth available may simply decline to do so and, if they previously amended to add Roth, may now remove it from their plan prospectively.

Hey, I've Got an Idea ….

What if we make Roth available only to those people who are HPIs and who, without a Roth provision, would be prevented from making catch-up contributions?

Nice try. Roth has to be available to everyone, not just HPIs with a catch-up contribution issue. [Preamble, Section III.B.2] You may, however, limit Roth availability to catch-up contributions, which means that any catch-up (even those of non-HPIs) could be made as a Roth amount. [Treas. Reg. § 1.414(v)-2(a)(5)]

So, How Does This Work in Practice?

In general theory, an HPI elects to make pre-tax salary deferrals. At some point during the year, the HPI hits a deferral limit. After that point, all deferrals are Roth. Easy peasy, right? (Pinch yourself on the cheek and say to yourself, "You are SO cute!")

Of course, it's not that easy! Are you new here?

Participants Must Irrevocably Designate Amounts as Roth Before the Relevant Payroll Date

Does an HPI need to affirmatively designate before they hit a pre-tax deferral limit that additional deferrals will be Roth?

The Final Regs confirm that the plan may contain a provision for a deemed Roth election by the participant. Under this provision, the HPI will be presumed to have elected that any pre-tax deferral that hits a limit and becomes a catch-up contribution will be made as Roth. Therefore, affirmative elections by HPIs are not needed. The deemed election *must be* elected by the plan in relation to excess deferrals if that failure is to be repaired in any manner other than through distribution to the participant. [Treas. Reg. § 1.414(v)-2(c)(3)(i)(B)]

The Final Regs, consistent with the original proposed regulations, require that HPIs be given an effective opportunity, however, to elect for the deemed election to not apply, that is, for any excess amount to be distributed to the participant as if they were not catch-up eligible. When and in what form must this effective opportunity be provided? The proposed regulations were silent, so some practitioners (our firm included) asked for clarification. The Treasury responded in the preamble to the Final Regs that it's a facts and circumstances analysis and declined to provide further guidance. [Preamble, Section I]

Looking at this logically, it seems that there are a few ways that effective opportunity could be provided:

- *The plan can notify the HPI as soon as a limit is hit that all future deferrals will be on a Roth basis, unless they take action to elect otherwise.* This gives the participant the greatest opportunity to know that the issue has arisen and to take action to decline the deemed election. It also has a terrifically high potential for error, requiring quick identification and notification to the participant. Any guesses how effective this would be for most plans to administer?
- *The plan can notify all participants in the SPD of the HPI potential and the deemed election*. This has the least likely chance of alerting the affected participant, because it requires reading the Summary Plan Description (SPD) and also remembering the issue before it actually arises.
- *The plan can put a disclosure about the HPI potential issue and the deemed election in one of the notices that go out at the beginning of the year in connection with the plan*. While some are cynical about people reading notices, it will be a recurring notice, and it will be provided at a time when a participant is likely to be considering the level of their deferral elections (or when automatic increases are likely to apply).

While none of these options is specifically sanctioned by the Treasury, we think that the last option makes the most sense, and recommend that the HPI notice be conspicuous (something in bold print, calling participants' attention to the information).

Of course, even plans with the election deemed must be administered in such a fashion as to ensure that it is effectuated when needed. That will require diligence on the part of the payroll provider, the employer, and the recordkeeper.

What About Situations Where the Catch-Up Nature of the Contribution Is Not Known at the Point of Deferral?

As discussed above, there are going to be situations, particularly ADP testing failures and excess annual additions, that require reclassification of pre-tax deferrals to be catch-up contributions and, for HPIs, Roth amounts. There is no way to know with any certainty before the end of the plan year that these amounts exist. Therefore, there is nothing preventative to ensure that no reclassification is needed.

Notwithstanding the general Roth rule about identifying the Roth before it is deposited and ensuring that it goes into a Roth account, the Final Regs permit a reclassification mechanism. This mechanism is available for both situations in which the catch-up contribution cannot be identified at the time that the deferral is deposited to the plan and when an error is made and the identification does not take place. For ease of wording, we will consider all three situations to be "corrections," and discuss how they can be handled.

Which Contributions Are the Catch-Up?

Both the proposed regulations and the Final Regs provide that any Roth deferrals made during the year can count as the catch-up contribution. [Treas. Reg. § 1.414(v)-2(b)(1); Preamble, Section III.B.1] This is most easily explained through an example.

Let's say that Maria defers $7,500 to the Plan in the first part of the year as Roth contributions and then changes her deferral election to contribute for the rest of the year on a pre-tax basis. Total deferrals are $31,000, more than the 402(g) limit, so that $7,500 of these amounts must be considered to be catch-up contributions. The amount Maria already contributed as Roth amounts can be considered to be the catch-up amount, so that no reclassification of other amounts is required.

This is a nice feature for the participant and allows HCEs who want to avoid having ADP excesses reclassified after the year end (and surprise additional taxable income) to avoid after-the-year reclassifications by making assumed catch-up amounts as Roth earlier in the year. It may be that such individuals will end up with more Roth than needed, but they will know what their taxable income is with no reclassification surprises.

This gift to participants, however, may not be so pleasant for the employer. Allowing earlier Roth contributions to count as catch-ups requires more sophisticated administration. Rather than instructing the payroll department that every deferral over the Code Section 402(g) limit is to be classified as Roth for HPIs, the plan administrator must now examine earlier-in-the-year deferrals for any Roth amounts to identify whether and how much of any future deferrals need to be classified as Roth. The risk of error here is high. As a result, it may be that many employers take advantage of the fact that the plan may provide that they do *not* allow earlier Roth contributions to count as catch-up amounts. [Preamble, Section III.B.1] That way, no one has to look back to earlier deferral classifications to determine what is and what is not a catch-up contribution.

When Things Don't Work … Corrections and the Mechanisms by Which They Happen

If an HPI's deferral is deposited as a pre-tax amount but is actually a catch-up contribution that is required to be Roth, there are three possible correction mechanisms:

1. The Distribution Method
2. The Form W-2 Method
3. The In-Plan Roth Rollover Method

There are some deadlines and timing issues for these methods, but let's discuss the methods, themselves, first.

The Distribution Method

This method applies in the absence of any deemed Roth deferral or if the participant has elected not to have the deemed Roth deferral apply. In this circumstance, the participant is treated as someone who is not eligible for catch-up contributions. The excess amount is, therefore, distributed to the participant with applicable earnings and is considered to be taxable income to the participant. [Preamble, III.C.1]

The Form W-2 Method

If it is discovered that there are excess amounts for an HPI that must be treated as catch-up contributions and converted to Roth, and that discovery occurs before the Form W-2 is issued to the participant or sent to the IRS (generally, therefore, in early- to mid-January), the deferral amount and earnings may be transferred from the pre-tax account to the participant's Roth account in the plan, and the deferral amount at issue (but not the earnings) may be reflected on the Form W-2 as a Roth contribution. In that case, it's almost like the pre-tax deposit never happened … [Treas. Reg. § 1.414(v)-2(c)(2)(ii), Preamble, III.C.2.a]

The In-Plan Roth Rollover Method

Under this method, the amount of the catch-up contribution and the earnings thereon are transferred from the pre-tax account to the Roth account. The plan then issues a Form 1099-R in the year of the transfer, showing both the contribution and the earnings as taxable income for that year. This method is available even if the plan does not generally permit in-plan Roth rollovers, and does not require amendment to so permit. If this is the first Roth contribution made to the account, the five-year Roth period for a qualified distribution begins as of January 1 for the year in which the amount is includable in the participant's income. [Treas. Reg. § 1.414(v)-2(c)(2)(iii); Preamble, Section III.C.2.b]

Deemed Roth Election Required

If the plan wants to use any correction method other than the Distribution Method for an excess deferral correction, it must provide for the deemed Roth election. [Treas. Reg. § 1.414(v)-2(c)(3)(i)(B)]

Correction Timing

Failing to properly limit salary deferrals is a violation of Code Section 401(a)(30), and that is a plan qualification requirement. So, from a plan standpoint, the most important thing is to protect the plan's qualification status.

The Final Reg provides that the qualification status may be preserved by correcting the catch-up issue by the end of the plan year following the plan year in which the excess amount arose. So, if there is any deferral that is made on a pre-tax basis that ends up being identified as a catch-up contribution, the correction must take place by the end of the following plan year. [Treas. Reg. § 1.414(v)-2(c)(3)(iii)(A)]

Unfortunately, there are other Code sections that may be violated by not properly classifying the amount at issue as a catch-up contribution. And the correction timing for those other sections may be earlier, requiring faster resolution.

Situation #1: Excess Deferrals

Excess deferrals occur when the Code Section 402(g) limit (that is, $24,500 for 2026) is exceeded.

Under Code Section 402(g), an excess deferral failure must be corrected by April 15 following the end of the calendar year in which the excess arose. Failure to do so subjects the amount to taxation in the year deferred, plus taxation again when the amount is distributed. [Code § 402(g)(2)]

If the catch-up correction for an excess deferral is not made until after April 15, this problem arises. Let's look at an example:

> Dan, an HPI participant in the XYZ Plan, hit his deferral maximum of $24,500 in November of 2026. Nonetheless, an additional $5,000 of deferrals were deposited to the Plan on a pre-tax basis by the end of 2026. The problem was discovered when the Plan Administrator provided data to the third-party administrator in May 2027. The Plan Administrator immediately invoked the deemed Roth election and had the excess $5,000 and applicable earnings transferred to Dan's Roth account in late May. Because the correction occurred after April 15, Dan needs to claim the $5,000 as taxable income in 2026. But, when Dan leaves the company and takes a distribution of his entire account two years later, the $5,000 comes out of the plan as taxable income *again*, notwithstanding that it is a Roth amount. This result is not avoided if Dan waits to take his money until he has a qualified distribution.

It's important to note here that the person who suffers if the correction is late is not the Plan Sponsor, but the affected employee. Therefore, it behooves HPIs to watch their Code Section 402(g) limits carefully.

Situation #2: Excess Contributions

Excess contributions occur when deferrals by HCEs exceed the amount that can be contributed to the plan under the ADP test. This generally happens after the year end, and sometime before the Form 5500 is due. If the participant is catch-up eligible, the excess contribution may be reclassified to be a catch-up contribution to the extent that the catch-up limit is not exceeded.

Code Section 4979 provides, however, that if excess amounts are not distributed or reclassified as Roth within 2½ months of the end of the plan year (six months for plans with certain Eligible Automatic Contribution Arrangements), an excise tax applies that is equal to 10 percent of the amount distributed. Therefore, if an ADP failure is corrected later than that, the excise tax will apply.

The other two correction reasons—for annual additions in excess of the Code Section 415 limits or the deferrals in excess of a plan-provided limit—do not have special deadlines for correction. As long as they are corrected by the last day of the following plan year, the plan remains qualified, and no ramifications apply to either the participant or the plan.

If the participant terminated employment prior to correction being made and took a full distribution of his or her account, the plan will be considered to have been corrected by virtue of the distribution without further ado. However, the portion of the distribution attributable to pre-tax catch-up contributions would not be eligible for rollover. The Final Regs do not address what notification (if any) must be provided by the plan sponsor in such a situation. It makes sense that the sponsor should prepare a revised Form 1099-R and advise the participant of the tax issue, consistent with the requirement to do so found in the Employee Plans Compliance Resolution System. [*See,* Preamble, Section III.D.4, Rev. Proc. 2021-30, § 6.06]

Which Correction Method to Use?

Assuming that the plan contains the deemed election provision, any of the three methods may be used for any excess correction. However, the regulations provide that similarly situated employees must be corrected in the same fashion. There is no definition of what "similarly situated" means, but it appears to refer to employees who suffer the same type of excess that is discovered at more-or-less the same time, so that it is feasible to correct them in the same fashion. [Treas. Reg. § 1.414(v)-2(c)(2)(i)]

> *Example*. Suppose that an employer discovers in early January that two employees, Moe and Larry, have exceeded the Code Section 402(g) limit for the prior year. If the problem for either of these two similarly situated employees is corrected using the Form W-2 method, the correction must apply to the other. However, in April, the employer realizes that Curly also had a Code Section 402(g) limit violation. It is now too late to use the Form W-2 correction method for Curly. This later discovery means that Curly is not similarly situated to Moe and Larry and Curly's excess can be corrected using the In-Plan Roth Rollover method.

The fact that a violation is discovered in time to use the Form W-2 correction method does not mean that the employer must use that method. It may choose to use either the Distribution method or the In-Plan Roth Rollover method.

Times When No Correction Is Needed

You can avoid making any correction at all under two circumstances:

1. If the amount of the deferral that needs correction is $250 or less. Leave it as pretax, and back away slowly.
2. If the Form W-2 for the participant reflecting their FICA compensation is amended after the expiration of the end-of-the-following-plan-year deadline to reflect that the participant is an HPI, when the unamended form showed that they were not. (Again, back away, but leave things as they were before the amended Form W-2 was filed.) [Treas. Reg. § 1.414(v)-2(c)(4)]

Additional Issues and Questions

Off-Calendar Year Plans

The Final Regs do not contain a lot of language outlining how to handle plan years other than calendar years. However, it does have one example that shows how to correct failures for such plans. [*See,* Treas. Reg. § 1.414(v)-2(d)(4)] That example indicates, when determining whether a participant is an HPI, you should refer to the FICA compensation earned in the calendar year preceding the calendar year in which the excess amount occurred. For example, if an ADP testing failure arose for a June 30 year end plan as of June 30, 2028, the 2027 FICA compensation for the participant is used to determine whether the participant is an HPI.

Note that the relevant timing is when the excess arises and not when it is discovered. For example, suppose that the ADP testing for the June 30, 2028, plan year is not performed until June 1, 2029 (29 days before the correction deadline), the HPI status of an employee with excess contributions is still determined based on 2027 FICA compensation, that is, the year before the plan year in which the excess arose, *not* the year before the excess is identified. This means that the HPI status cannot be manipulated by the administrator by rushing or delaying the determination of the excess.

Dual Qualified Plans

Plans that cover both mainland and Puerto Rican employees face a conundrum, because the Puerto Rican Tax Code does not provide for Roth contributions. The proposed regulations provided a complex reclassification for Puerto Rican employees using after-tax employer contributions. The Final Regs eliminate this complication, simply providing that the Roth contribution conversion rules do not apply to employees subject to the Puerto Rican Tax Code. [Treas. Reg. § 1.414(v)-2(a)(6)]

Code Section 403(b) Plans Subject to Special Catch-Up Availability

Certain Code Section 403(b) plans permit special catch-up contributions under Code Section 402(g)(7), in addition to the normal catch-up contributions under Code Section 414(v). The Final Reg clarifies that the Code Section 403(b) catch-up amounts may be made on behalf of an HPI on a pre-tax basis, with only amounts in excess of those contributions (and up to the Code Section 414(v) catch-up limit) needing to be Roth amounts. [Treas. Reg. §1.414(v)-2(c)(3)(i)(C)]

Conclusion

While the Age 60-63 increased catch-up limit appears relatively easy to navigate, it is clear that Congress's activities in relation to Roth catch-up contributions has created quite the hornet's nest of issues. While all this may be completely avoided by eliminating either Roth or catch-up contributions from the plan, either step would have an unfortunate impact on the accumulation of savings for certain participants' retirement.

Just about every statute that modifies retirement plan rules is greeted by practitioners with cries of "how are we going to do this?" that are ultimately silenced by procedures and computer programs, but this rule may be the most challenging yet. If the plan will be subject to these rules, the employer should take immediate action to:

1. Adopt policies and procedures that address Roth catch-ups that adopt the deemed Roth election, to preserve the ability to freely correct errors that may be inevitable.
2. Talk to their third-party administrator or recordkeeper about how the plan notices should address the deemed Roth election.
3. Discuss with the payroll provider and the recordkeeper how best to identify excess amounts before they occur, to the extent possible, and what to do once an excess arises.
4. Confirm whose responsibility it is to oversee the development of these plan processes before they are needed.

It will be interesting to see how all this progresses in the industry. ■