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An Employer's Practical Guide to 401(k) Plan Catch-Up Contribution Changes for 2026

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Under the SECURE 2.0 Act of 2022 (the Act), new rules apply to 401(k), 403(b), and governmental 457(b) plans regarding catch-up contributions – the additional elective deferrals (\$7,500 in 2025) that employees aged 50 or older can make above the regular annual individual contribution limit (\$24,500 in 2025). These new rules do not apply to SIMPLE IRAs or SIMPLE 401(k)s (separate rules apply there). In January 2025, the IRS issued proposed regulations on the Act's catch-up contribution provisions. Last month, the Treasury Department and the IRS issued joint final regulations, answering many looming questions after the proposed regulations were issued.

Key Rule Changes for Catch-Up Contributions

Catch-Up Contribution Requirement for "High Earners"

Beginning January 1, 2026, employees classified as "High Earners" – those whose prior-year Social Security wages exceed \$145,000 – must make catch-up contributions exclusively as Roth (after-tax) contributions, **but only if** the plan permits Roth contributions. If the plan does not permit Roth contributions, then High Earners cannot make catch-up contributions. This \$145,000 threshold amount is indexed annually for inflation and applies only to employees, excluding partners or self-employed individuals.

Catch-Up Contributions for Other Participants

Participants who are not High Earners in the prior year can continue to make pre-tax or Roth catch-up contributions, as permitted by the plan.

Determining the \$145,000 Threshold

The threshold is determined using the prior calendar year's W-2 wages, specifically Box 3 Social Security wages, and applies separately to each employer based on controlled group rules.

Practical Tips for Employers

Plan Design Changes

Employers who currently offer no Roth feature must amend their plans to permit Roth contributions by the end of the 2026 plan year and notify the plan's recordkeeper if they want to continue allowing catch-up contributions for High Earners. While the plan does not have to be amended to add the Roth contribution feature until the end of the 2026 plan year, employers should decide whether they want to add this feature before January 1, 2026, and notify the plan's recordkeeper of that decision. Alternatively, employers could suspend catch-up contributions, although this may be unfavorably received by employees.

Restrictions on Catch-Up Contribution Elections

Employers cannot require all catch-up contributions from all participants to be Roth contributions, as this conflicts with IRS rules that require employee elections for Roth designation.

Employers also cannot limit Roth catch-up contributions only to High Earners. If Roth catch-up contributions are allowed for any participant subject to the Roth catch-up rule, they must be available to all catch-up-eligible participants.

Impact on "Deemed" Catch-Up Contributions

Historically, when participants exceeded contribution limits or plans failed nondiscrimination tests, excess contributions were "deemed" catch-up contributions for participants aged 50 or older to avoid refunds. Under the final IRS regulations, "deemed elections" can only apply after a participant exceeds the individual contribution limit (\$24,500 in 2025) but not after exceeding the aggregate limit (\$72,000 in 2025).

Deemed Election vs. Affirmative Election

- **Deemed Election** simplifies plan administration and provides special correction methods that are more favorable to participants. If the plan provides for a deemed election, it must also provide the participant with an effective opportunity to make a new election that is different from the deemed election. Whether a participant has an effective opportunity will be based on the facts and circumstances. Further, the deemed election must cease within a reasonable period after a participant is no longer subject to the High Earner Roth catch-up requirement.
 - **"Spillover" Design Issue:** A plan may deem a "spillover" amount as Roth contributions without regard to any Roth contributions made earlier in the year. A plan may choose to apply the deemed election either (1) once the employee's year-to-date pre-tax deferrals *reach* the annual limit or (2) once the employee's year-to-date aggregate (pre-tax and Roth) deferrals *exceed* the annual limit.
- **Affirmative Election** requires participants to actively elect catch-up contributions separately from their deferral elections and is often used to avoid forcing unintended taxable Roth contributions or due to administrative constraints with the payroll and HR operating systems.

Correcting Errors in Administering the New Rules

Correction Methods

IRS regulations provide for two correction methods for instances when catch-up contributions should have been Roth but were made pre-tax. The correction methods cover elective deferrals exceeding (i) a statutory contribution limit or the aggregate contribution limit of \$72,000 for 2026, (ii) an employer-provided limit, or (iii) the Average Deferral Percentage (ADP) limit. The correction requirements differ depending on the underlying reason for the error.

- **Form W-2 Correction Method:** A plan may transfer the catch-up contribution (adjusted for earnings/losses) from the High Earner's pre-tax account to their designated Roth account and report the contribution (not adjusted for earnings/losses) as a designated Roth contribution on their Form W-2 for the year of deferral. This method is only available if the Form W-2 for that year has not yet been filed or furnished to the participant.
- **In-Plan Roth Rollover Correction Method:** A plan may directly roll over the elective deferral (adjusted for earnings/losses) from the participant's pre-tax account to their designated Roth account. This correction does not require a voluntary participant election under Code section 402A(c)(4)(E)(i).

The final regulations confirm that a plan may utilize this correction method even if it does not permit participant-elected in-plan Roth rollovers because the transfer is being made by the plan and not at the election of the participant, and that it is an administrative detail and not a benefit, right, or feature subject to Code section 401(a)(4) nondiscrimination testing. A plan may use either of the preceding methods, but it must apply the same correction method to similarly situated participants.

The final regulations do not require a plan amendment, but the plan must have "practices and procedures" in place to utilize the correction methods. If the excess contribution is due to exceeding the annual individual contribution limit, then the plan's practices and procedures must include the deemed Roth catch-up election.

Correction Deadline

The deadline to correct a failure using these correction methods depends on which limit is the basis for the recharacterizing the pre-tax deferrals as Roth catch-up contributions:

- ***Correction for Exceeding Individual or Aggregation Annual Contribution Limit:*** A plan must generally correct failures relating to a statutory limit by the end of the taxable year following the year the contribution was made. However, a plan must still comply with correction deadlines that have other tax consequences. For example, if the deferral is a catch-up contribution because it exceeds the individual deferral limit, the applicable correction deadline to avoid penalty taxes is to recharacterize the deferral by April 15 of the calendar year following the calendar year for which the deferral was made.
- ***Correction for ADP Failure:*** The correction must be made by the end of the plan year following the plan year the excess contribution was made.

De Minimis Exception Rule

There are de minimis exceptions to the correction rules. Correction is not required: (1) if the pre-tax deferrals that should have been Roth do not exceed \$250, or (2) if the employee's FICA wages are determined to exceed \$145,000 on account of adjustments made after the correction deadline. The adjusted W-2 exception is particularly useful, as it allows a plan to avoid making corrections when the employer discovers a payroll error requiring an amended W-2 after the correction deadline.

Tax and Distribution Considerations for Roth Catch-Up Contributions

The Five-Year Rule

- For purposes of determining whether a distribution from a designated Roth account can be made tax-free (qualified distribution), the five-taxable-year period begins with the first taxable year for which the individual made a designated Roth contribution to the plan. For contributions corrected via the Form W-2 or rollover methods, the five-year period begins with the taxable year the amount is included in gross income. Early distributions (e.g., distributions made before the participant attains age 59½) within this period are subject to a 10 percent penalty under Code section 72(t).
- It can be confusing if a participant retires before the end of the five-year period. If amounts from a Roth account are withdrawn before the fifth anniversary of the participant's initial Roth contribution, the earnings on the funds will be subject to income tax (plus a 10 percent penalty if taken before age 59 ½). High Earners should be sure to take the five-year rule into consideration when planning retirement.

- The good news is that the five-year period is measured retroactively through January 1 of the year of the first contribution. So, for a contribution made in December 2026, it is treated as made on January 1, 2026 for purposes of the five-year rule.
- For participants who have Roth contributions and did not begin those contributions at least five years prior to retirement, to avoid the 10 percent penalty tax and allow the five-year period to run, the participant can leave their Roth contributions in the plan (if the plan permits) or roll over their Roth contributions to a Roth IRA and delay distribution until they have met the five-year requirement.

Special Considerations for Tax-Exempt or Governmental Plans

403(b) Plans

Special 15-year service catch-up contributions are always pre-tax; only age-50 catch-ups are subject to the Roth Catch-Up Rule.

Governmental 457(b) Plans

The special 457(b) catch-up allowed in the three years before normal retirement is pre-tax; age-50 catch-ups beyond this are subject to the Roth Catch-Up Rule. Non-governmental 457(b) plans do not permit age-50 catch-ups.

Plan Amendment Deadlines and Next Steps

Amendment Deadlines

SECURE 2.0 amendments are generally due by December 31, 2026, with extensions to 2028 for collectively bargained plans and 2029 for governmental plans. Unless there is future IRS guidance to the contrary, we recommend that employers adopt the requisite plan amendment by these deadlines.

Coordinate with Payroll and Recordkeepers

These steps should be taken by December 31, 2025:

- Ensure systems will identify "High Earners" – participants whose prior-year wages exceeded \$145,000.
- Confirm payroll is set to withhold catch-up contributions for High Earners as after-tax contributions.
- Determine whether the plan will administer catch-up contributions as deemed elections or require affirmative election.
- Confirm payroll and plan recordkeeping systems communicate wage data correctly and can segregate contribution types.

Communicate with Participants

Develop clear participant communications explaining:

- Who is affected (employees earning over \$145,000 in the prior year);
- What changes (catch-ups must be Roth);
- When it takes effect (2026); and
- The impact on take-home pay and tax treatment.

We will continue to monitor the agencies for further issuance of clarifying guidance, potential delays in implementation, model plan amendments, and regulations. If you have any questions or concerns regarding this alert, please reach out to [Andrea Bailey Powers](#), [Elverine "Rena" F. Felton](#), [William E. Robinson](#), or any member of Baker Donelson's [Tax](#) Group.