SECURE 2.0 ALLOWS ROTH EMPLOYER CONTRIBUTIONS IN 401(K) PLANS

Monday, February 06, 2023

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Up to now, employer contributions to 401(k) (and other plans) had to be made to pre-tax accounts. One of the SECURE 2.0 changes already in effect allows employer contributions to be made to Roth accounts. Roth employer contributions are allowed in 401(k), 403(b) and governmental 457(b) plans. (In reality, 457(b) plans usually don't have employer contributions to begin with.) Keep in mind that this covers employer contributions; many 401(k) (and other) plans already permit Roth *employee* contributions.

This change is one of several "Rothification" provisions within SECURE 2.0 that Congress hopes will raise revenue to help pay for other changes made by the new law. A similar provision allows SEP and SIMPLE IRA contributions to be made on a Roth basis.

Although this provision was actually effective on December 29, 2022 (the day SECURE 2.0 was signed into law), it will take recordkeepers some time to adjust their systems to accommodate the new provision. Also, recordkeepers will be reluctant to offer this option until the IRS clarifies several administrative issues, such as how employee taxes on Roth employer contributions will be reported. So, don't expect your employer to be offering this option anytime soon.

And, even when recordkeepers are ready to institute this change, employers will not be required to offer it. Further, if your employer offers Roth treatment for employer contributions, it can't impose it in on you. Instead, employees must elect to have their employer contributions deposited into the plan's Roth account.

For tax purposes, Roth employer contributions will be treated the same as Roth employee contributions. This means that you'll be taxed on the amount of the Roth contribution in the year it's made. When you take a distribution from your 401(k), the contributions themselves will come out tax-free. Earnings on the contributions also will be distributed tax-free if made after age 59 ½, disability or death and after a five-year holding period has been satisfied.

Many plans use vesting schedules for employer contributions. If your plan has a vesting schedule, you need to work a certain number of years with your employer before you are partially or fully vested in your employer contributions. (Being vested means you have earned a benefit that can't be taken away from you.) SECURE 2.0 says that only vested employer contributions qualify for Roth treatment. That may make this new option less attractive to you and create administrative headaches for your employer.