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Pre-Tax Dollars for Make-Up Pension Contributions

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Q: I am a captain in the Air Force Reserve. I was called to active duty, for one year, in October 2002, and then I was extended for a second year. I expect to leave active duty in October 2004 and to seek re-employment at the XYZ Corp., where I have worked since October 1998.

At XYZ, I was covered by a contributory defined contribution pension plan. For each two-week pay period, while I was employed at XYZ, I made a contribution to my pension account, and the employer matched my contribution. My contribution was always made pre-tax, meaning that I paid federal income tax on what I was paid by XYZ, not including my contributions to the pension plan account.

I understand that I have up to five years, after my re-employment, to make up the employee contributions that I missed during my two years of active duty. How I can pay those make-up contributions with pre-tax dollars? Do I need to file amended tax returns for back years? Is there a limit on how much I can contribute (pre-tax), during a calendar year? If there is such a limit, and if I do not file amended returns, I am concerned that my current year pension plan contributions plus my make-up contributions will exceed the limit.

A: As discussed in prior articles, USERRA Section 4318 provides that a member of the military who is re-employed by his/her employer shall be treated as not having incurred a break in employment service. The period served in the military shall, upon re-employment, be deemed to constitute service with the employer maintaining the plan for the purpose of determining the nonforfeitality of their accrued benefits and their accrual of benefits under the plan.

¹I invite the reader's attention to www.roa.org/lawcenter. You will find more than 2000 "Law Review" articles about the Uniformed Services Employment and Reemployment Rights Act (USERRA), the Servicemembers Civil Relief Act (SCRA), the Uniformed and Overseas Citizens Absentee Voting Act (UOCAVA), the Uniformed Services Former Spouse Protection Act (USFSPA), and other laws that are especially pertinent to those who serve our country in uniform. You will also find a detailed Subject Index, to facilitate finding articles about very specific topics. The Reserve Officers Association, now doing business as the Reserve Organization of America (ROA), initiated this column in 1997.

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An employer who sponsors a retirement plan shall only be treated as meeting the requirements of USERRA if each of the following requirements are met: (a) the re-employed member is treated as not having incurred a break in service with the employer maintaining the plan by reason of his/her period of qualified military service; (b) each period of qualified military service is deemed to constitute service with the employer maintaining the plan for the purpose of determining the nonforfeitality of the individual's accrued and accrual of benefits under such plan; (c) a re-employed member is entitled to accrued benefits that are contingent on the making of, or derived from, employee contributions or elective deferrals only to the extent the member makes payment to the plan with respect to such contributions or deferrals. No payment may exceed the amount the member would have been permitted or required to contribute had the member remained continuously employed by the employer throughout the period of qualified military service.

Any payment to such plan shall be made during the period beginning with the date of re-employment and whose duration is three times the period of the qualified military service but not greater than five years.

Upon your return to work, you will need to inform XYZ of your decision to make up the defined contribution plan payments that you did not make while serving on active duty. Over the next five years, beginning the day you return to work, you will be entitled to contribute the "make-up" pension plan contributions to XYZ plan. XYZ must match your make-up contributions in accordance with the terms of their pension plan. Your make-up contributions will be as follows: \$11,000 for 2002, \$12,000 for 2003 and \$13,000 for 2004.

You will not need to file an amended tax return for the years that you were on active duty and made no pension plan contributions. The make-up contributions will be in addition to the contributions that you are entitled to make annually to the XYZ pension plan. Your employer will need to reflect the make-up contributions, over the term you make the contributions, on your future W-2 statements. The IRS will then be on notice of the fact that you are not making excess but make-up pension plan contributions.

In addition, depending upon the language of XYZ's plan, if you were over the age of 50 while serving on active duty, you may be entitled to make "catch- up" contributions. The catch-up contribution amount was \$1,000 in 2002 and increased by \$1,000 each year until \$5,000 in 2006. After 2006, the contributions will be indexed in \$500 increments.

Update – April 2022

Annual catch-up contributions have increased. As of 2022, those aged 50 and above can make catch-up contributions of an additional \$6,500. The catch-up contributions were up to \$6,500 in 2021; \$6,500 in 2020; and \$6,000 in 2015-2019. Be sure to stay up to date on the annual catch-up contributions that you can make.