

RE: Maximum Deferral and Threshold Limits for 2008 and 2009¹
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The Internal Revenue Code (IRC) establishes a number of limits on retirement plan benefits and contributions. The limits are located in various sections of the Code and often apply in different ways to private and public-sector plans. Generally, plans must comply with the limits to maintain their tax-qualified status.

The Internal Revenue Service (IRS) periodically increases certain limits to reflect changes in the Consumer Price Index (CPI). In many cases, the adjustment is only made if the change in the limit attributable to the CPI exceeds a certain amount (e.g., \$1,000 or \$5,000). On October 16, 2008, the IRS published new limits in IRS Release IR-2008-118, generally effective for limitation years beginning on or after January 1, 2009.² The table below presents key limits for 2009 and compares them with the 2008 limits. The remainder of this memo briefly describes these limits.

Maximum Deferral and Threshold Limits for 2008 and 2009

	2008	2009
Maximum Benefit Dollar Limit IRC § 415(b)(1)(A)	\$185,000	\$195,000
Special Firefighter/Police 415(b) Dollar Limit IRC § 415(b)(2)(G)	185,000	195,000
Maximum Contribution to a Qualified Defined Contribution Plan IRC § 415(c)(1)(A)	46,000	49,000
Maximum Compensation Limit IRC § 401(a)(17)	230,000	245,000
Maximum Compensation Limit in Lieu of OBRA '93 IRC § 401(a)(17)	345,000	360,000
Elective Deferral Maximum for 401(k) Plans and 403(b) Plans IRC § 402(g)(1)	15,500	16,500
Elective Deferral Maximum for 457 Plans IRC § 457(e)(15)	15,500	16,500
Catch-Up Limit (Age 50 and Older) for 401(k), 403(b), and 457 Plans IRC § 414(v)(2)(B)(i)	5,000	5,500
Catch-Up Limit (Age 50 and Older) for SIMPLE Plans IRC § 414(v)(2)(B)(ii)	2,500	2,500
IRA Contribution Limit	5,000	5,000
IRA Catch-Up Limit (Age 50 and Older) IRC § 219(b)(5)(B)(ii)	1,000	1,000
Social Security Maximum Taxable Earnings – OASDI	102,000	106,800
Social Security Maximum Taxable Earnings – HI	No Limit	No Limit

Sources: IRS Release IR-2008-118 and SSA “2009 Social Security Changes” Fact Sheet.

¹ The author of this memorandum is not an attorney and the statements made are not intended as legal advice or opinion. Plan administrators should seek the advice of qualified legal counsel to ensure plan provisions and documents comply with applicable federal laws and regulations.

² With regard to the 415 limits, the default limitation year is the calendar year; however, an employer may elect any other consecutive 12-month period as the limitation year by adopting a written amendment to the plan.

Maximum Benefits

For governmental plans, IRC § 415 limits the benefits payable from defined benefit plans and the amounts contributed to defined contribution plans. Generally, IRC § 415(b) limits the employer-provided benefit payable to a member from a defined benefit plan to the lesser of \$195,000 for limitation years starting in 2009 (the "dollar limit") or 100% of the participant's average compensation for his or her three highest years.³ Although private-sector plans are subject to both limits, governmental plans are exempt from the 100% of compensation limit.

If benefits commence before age 62, IRC § 415(b) requires the dollar limit to be actuarially reduced using prescribed factors. However, for qualified full-time employees of police and fire departments with at least 15 years of service credit, no actuarial reduction is required.⁴ Consequently, the dollar limit for these members is the same as the unreduced § 415(b) dollar limit (\$195,000 in 2009), regardless of age.

Maximum Contributions

IRC § 415(c) limits the maximum "annual additions" that can be made to a member's defined contribution plan account to the lesser of \$49,000 in 2009, or 100% of annual compensation. In this context, annual additions include employer and employee contributions, as well as forfeitures. Annual compensation, for the purpose of determining this limit, includes elective deferrals to §§ 401(k), 403(b), governmental 457(b), and 125 "cafeteria" plans, along with certain transportation fringe benefits under IRC § 132(f)(4).

For governmental defined benefit plans that do not "pick-up" mandatory employee contributions under IRC § 414(h)(2), employee contributions are treated as contributions to a defined contribution plan and are subject to the § 415(c) limits. For governmental plans that do "pick-up" employee contributions, the contributions are treated as part of the employer-provided portion of accrued benefits subject to the § 415(b) dollar limits.

Maximum Compensation

IRC § 401(a)(17) limits the amount of compensation that can be taken into account by the plan, for the purpose of determining benefits and contributions, to \$245,000 in 2009. For private-sector plans, even if a plan member earns more than this amount, only \$245,000 may be used in 2009 to calculate employee contributions to, or benefits provided by, the qualified plan.

Special rules apply to some public-sector plan members hired before 1996. In 1993, IRC § 401(a)(17) was amended by the Omnibus Budget Reconciliation Act (OBRA '93), lowering the maximum compensation limit from \$200,000 to \$150,000, indexed for inflation. OBRA '93 allowed governmental plans to grandfather the compensation limits specified in the plan as of July 1, 1993, for employees hired before 1996 – provided the plan was amended to apply the OBRA '93 limits to employees hired in 1996 and after. For governmental plans applying the pre-OBRA '93 limits, the maximum compensation limit in 2009 is \$360,000 for grandfathered employees. For governmental plans that had no maximum compensation limit as of July 1, 1993, and that amended the plan to grandfather these provisions, benefits can be determined without reference to any compensation limit for grandfathered employees.⁵

³ Under IRC § 415(m), state and local governments are allowed to pay benefits in excess of the 415(b) limit by establishing a "qualified excess benefit arrangement" (QEBA), also referred to as a "benefit restoration plan". However, these funds must be held separately from the pension trust.

⁴ In this context, the term "department" refers to a state or local governmental unit that provides police protection, firefighting services, or emergency medical services. It relates to the unit's function rather than the unit's name.

⁵ Treas. Reg. § 1.401(a)(17)-1(d)(4)(ii).

Maximum Elective Deferrals

Elective deferrals are voluntary agreements in which employees elect to forego current income in return for the employer's contributions to retirement or other benefit plans. Elective deferrals are available for a variety of tax-qualified retirement plans, including 401(k) and 403(b) plans, for which the maximum elective deferral per participant is \$16,500 in 2009. Governmental employees may have access to deferred compensation plans established under IRC § 457(b). The maximum elective deferral for 457(b) plans is also \$16,500 in 2009.

IRA Contribution Limit

The maximum annual contribution to a traditional IRA and a Roth IRA is \$5,000 in 2009. After 2009, the IRA contribution limits are indexed for inflation in \$500 increments.

Catch-Up Dollar Limits

As a result of the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), plan participants who are or will be age 50 or older by the end of the plan year may voluntarily make additional "catch-up" contributions to the plan, above the maximum elective deferral limits. The maximum catch-up contribution is the lesser of (1) a specific dollar amount (the "catch-up dollar limit") or (2) the participant's compensation for the year reduced by any other elective deferrals made during the year. For 2009, the catch-up dollar limit for 401(k), 403(b), SEPs, and 457(b) plans is \$5,500. For SIMPLE plans, the 2009 catch-up dollar limit is \$2,500. For IRAs, the catch-up dollar limit is \$1,000 for 2009 and thereafter.

Note: 457(b) plans have an additional catch-up provision under IRC § 457(b)(3). As amended by EGTRRA, a 457(b) plan participant may, in one or more of the three years ending before normal retirement age, defer the lesser of (1) twice the applicable dollar limit (i.e., twice \$16,500 or \$33,000 in 2009) or (2) the sum of the applicable dollar limit for the year (i.e., \$16,500 in 2009) plus the amount by which the applicable dollar limit in preceding years exceeded actual deferrals in those years. In the three years ending before normal retirement age, a 457(b) plan participant may apply the greater of the 414(v) catch-up provision or the 457(b)(3) catch-up provision, but not both.

Taxable Earnings for Social Security and Medicare

To fund Social Security's Old Age, Survivor, and Disability Insurance (OASDI) program, both employers and employees pay a 6.20% payroll tax on earnings up to the maximum taxable earnings limit. This limit is adjusted annually for inflation and is increased to \$106,800 in 2009. Because the maximum earnings limit was eliminated for the Medicare Hospital Insurance (HI) program in 1993, there is no limit on earnings subject to the 1.45% Medicare tax.

On October 16, 2008, the Social Security Administration (SSA) announced a 5.8% cost-of-living adjustment for 2009. The adjustment is based on the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W) from the third quarter of 2007 to the third quarter of 2008. The cost-of-living adjustment will be effective for payments beginning in January 2009 to Social Security and Supplemental Security Income (SSI) beneficiaries.

Links

IRS News Release (IR-2008-118) is available at: <http://docs.cpamerica.org/wtu/ir-2008-118.pdf>

The 2009 Social Security report is at:

<http://www.socialsecurity.gov/pressoffice/factsheets/colafacts2009.pdf>

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