

Number 82, July-August 2003: Pre-Tax Dollars for Make-up Pension Contributions

By LT Marc J. Soss, SC, USNR*

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 nonforfeitability of their accrued benefits and their accrual of benefits under the plan.

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 nonforfeitability 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.

*Marc J. Soss is a tax-estate planning, probate and guardianship attorney with the law firm of Becker & Poliakoff, P.A., in the firm's Sarasota, Fla., office. He is the officer-in-charge of Naval Reserve Unit, Cargo Handling Battalion 11, Bravo Company, Tampa, Fla. He can be reached at MSOSS@Becker-Poliakoff.com.

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