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IRS Issues Guidance on Overpayment Correction Rules under SECURE 2.0

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The SECURE 2.0 Act of 2022 (“SECURE 2.0”) made significant changes to the rules governing the correction of overpayments from employer sponsored retirement plans, including 401(k) plans, 403(b) plans, and defined benefit pension plan, as described in our prior [Legal Alert](#).

On October 15, 2024, the IRS issued Notice 2024-77, which provides guidance on the rules applicable to overpayment corrections under the IRS’s correction program. This guidance confirms that because of SECURE 2.0’s changes to the overpayment rules, plan sponsors are generally not required to seek recovery of overpayments from participants and beneficiaries, or to make corrective contributions to the plan to make the plan whole for overpayments that are not recovered as part of a correction.

Notice 2024-77 addresses some of the key questions raised by SECURE 2.0’s changes to the overpayment rules:

- Inadvertent benefit overpayments. SECURE 2.0’s changes to the overpayment rules are applicable to “inadvertent benefit overpayments”, which were not defined by SECURE 2.0. Notice 2024-77 provides that “inadvertent benefit overpayments” do not include:
 - o Overpayments made to a “disqualified person”, which includes plan fiduciaries, service providers, and officers and directors of the plan sponsor; or
 - o Overpayments that relate to corrections of different qualification failures. This means, for example, that the new overpayment correction rules do not apply if a corrective distribution is made in the wrong amount in connection with another correction.
- Overpayments violating other legal requirements. Reasonable efforts to recover overpayments from a participant or beneficiary and a make-whole payment to the plan by the plan sponsor or another party (to the extent the overpayment is not recovered) are still required when overpayments exceed the limits under Sections 401(a)(17) or 415 of the Internal Revenue Code (“Code”), or when a pension plan is subject to

distribution restrictions (due to its underfunded status or the bankruptcy of the plan sponsor) under Section 436 of the Code.

- Rollover of overpayments. Prior to SECURE 2.0, overpayments were not treated as rollover eligible, which could lead to adverse tax consequences to the participant if the overpayment was not returned to the plan. SECURE 2.0 provides that an inadvertent benefit overpayment may be treated as eligible for rollover if the plan sponsor does not seek recovery of the overpayment from the participant or beneficiary. Notice 2024-77 clarifies that, conversely, if the plan sponsor seeks to recover the overpayment, the overpayment will not be treated as an eligible rollover distribution, which is consistent with the pre-SECURE 2.0 rules. In this case, the plan sponsor would be required to notify the participant or beneficiary that the overpayment is not eligible for tax-free rollover (which can be included in the request for return of the overpayment). The overpayment recipient may avoid adverse tax consequences by returning the overpayment to the plan. Notice 2024-77 also clarifies that if an overpayment exceeds the limits under Sections 401(a)(17) or 415 of the Code, the plan sponsor is automatically treated as seeking recovery (so those overpayments are never treated as eligible for rollover under this rule unless they are actually recovered).

Notice 2024-77 addresses only the overpayment rules applicable to the IRS correction procedures. SECURE 2.0 also added rules that limit or restrict the ability of a plan to recover overpayments from participants or beneficiaries in many circumstances, which are not addressed in Notice 2024-77 because they are under the Department of Labor's jurisdiction. As a result, guidance from the Department of Labor will be needed to have a complete understanding of the SECURE 2.0 correction rules, but Notice 2024-77 is helpful in clarifying many of the open questions.