

# Year-end payroll issues to consider under Internal Revenue Code 409A

## Year-end base salary payroll considerations

Payroll periods near the end of a tax year often create confusion as to which base salary deferral election (current or future year) must be applied. Internal Revenue Code Section 409A creates rules to address this scenario and governs unless a plan document dictates differently.<sup>1</sup>

In general, the last day of the participant's tax year (i.e., December 31 for individuals) is the key date determining the applicable deferral election. If a payroll earnings period contains December 31 and is paid in the following year, the deferral election for the following year applies.

- **Example 1:** If a biweekly payroll earnings period runs from December 24, 2023, to January 7, 2024, with the pay date occurring in 2024, **the base salary deferral election for 2024** is applied and earnings from the entire payroll cycle are treated as if fully earned in 2024 (because the payroll earnings period included December 31, 2023, and is paid in the *next tax year*).
- **Example 2:** If a monthly payroll earnings period runs from December 1 through December 31, 2023, with the pay date occurring in 2024, **the base salary deferral election for 2024** is applied and earnings from the entire payroll cycle are treated as if fully earned in 2024 (because the payroll earnings period included December 31, 2023, and is paid in the *next tax year*).
- **Example 3:** If a monthly payroll earnings period runs from December 1 through December 31, 2023, with the pay date occurring on December 31, 2023, **the base salary deferral election for 2023** is applied as the entire payroll amount was earned and paid in the *same tax year*.

On the other hand, if a payroll earnings period is within the current tax year, but does not include December 31, the current year deferral election is applied, regardless of when the payment is made.

- **Example:** If a biweekly payroll earnings period runs from December 16, 2023, to December 30, 2023, with the pay date occurring on in 2024, **the base salary deferral election for 2023** is applied because the entire payroll amount was earned in 2023 (even though it's paid in the next tax year because the payroll earnings period *does not* include December 31, 2023).

<sup>1</sup> Treas. Reg. §1.409A-2(a)(13).



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