

determining Participant E's ADR for the plan year ending October 31, 2006, is \$15,000 (\$16,600 in elective deferrals for the current plan year, less \$1,600 in catch-up contributions).

(iii) The ADP test is run for Plan R (after excluding the \$1,600 in elective deferrals in excess of the section 401(a)(30) limit), but Plan R needs to take corrective action in order to pass the ADP test. After applying the rules of section 401(k)(8)(C) to allocate the total excess contributions determined under section 401(k)(8)(C), the maximum deferrals that may be retained by any highly compensated employee under Plan R (the ADP limit) is \$14,800.

(iv) Under paragraph (d)(2)(ii) of this section, elective deferrals that exceed the section 401(a)(30) limit under Plan R are also subtracted from Participant E's elective deferrals under Plan R for purposes of applying the rules of section 401(k)(8). Accordingly, for purposes of correcting the failed ADP test, Participant E is treated as having contributed \$15,000 of elective deferrals in Plan R. The amount of elective deferrals that would have to be distributed to Participant E in order to satisfy section 401(k)(8)(C) is \$200 (\$15,000 minus \$14,800), which is less than the excess of the applicable dollar catch-up limit (\$5,000) over the elective deferrals previously treated as catch-up contributions under Plan R for the taxable year (\$1,000). Under paragraph (d)(2)(iii) of this section, Plan R must retain Participant E's \$200 in elective deferrals and is not treated as failing to satisfy section 401(k)(8) merely because the elective deferrals are not distributed to Participant E.

(v) Even though Participant E's elective deferrals for calendar year 2006 have exceeded the section 401(a)(30) limit, Participant E can continue to make elective deferrals during the last 2 months of the calendar year, since Participant E's catch-up contributions for the taxable year are not taken into account in applying the section 401(a)(30) limit for 2006. Thus Participant E can make an additional contribution of \$200 (\$15,000 minus (\$16,000 minus \$1,200)) without exceeding the section 401(a)(30) for the calendar year and without regard to any additional catch-up contributions. In addition, Participant E may make additional catch-up contributions of \$3,800 (the \$5,000 applicable dollar catch-up limit for 2006, reduced by the \$1,200 (\$1,000 plus \$200) of elective deferrals previously treated as catch-up contributions during the taxable year). The \$3,800 of catch-up contributions will not be taken into account in the ADP test for the plan year ending October 31, 2007.

Example 7. (i) Participant F, who is 58 years old, is a highly compensated employee who earns \$100,000 per year. Participant F participates in a section 401(k) plan, Plan S, for the first 6 months of the year and then transfers to another section 401(k) plan, Plan T, sponsored by the same employer, for the second 6 months of the year. Plan S limits highly compensated employees' elective deferrals to 6% of compensation for the period of participation, but permits catch-up eligible participants to defer amounts in excess of 6% during the plan year, up to the applicable dollar catch-up limit for the year.

Plan T limits highly compensated employees' elective deferrals to 8% of compensation for the period of participation, but permits catch-up eligible participants to defer amounts in excess of 8% during the plan year, up to the applicable dollar catch-up limit for the year. Participant F earned \$50,000 in the first 6 months of the year and deferred \$6,000 under Plan S. Participant F also deferred \$6,500 under Plan T.

(ii) As of the last day of the plan year, Participant F has \$3,000 in elective deferrals under Plan S that exceed the employer-provided limit of \$3,000. Under Plan T, Participant F has \$2,500 in elective deferrals that exceed the employer-provided limit of \$4,000. The total amount of elective deferrals in excess of employer-provided limits, \$5,500, exceeds the applicable dollar catch-up limit by \$500. Accordingly, \$500 of the elective deferrals in excess of the employer-provided limits are not catch-up contributions and are treated as regular elective deferrals (and are taken into account in the ADP test). The determination of which elective deferrals in excess of an applicable limit are treated as catch-up contributions is permitted to be made in any manner that is not inconsistent with the manner in which such amounts were actually deferred under Plan S and Plan T.

Example 8. (i) Employer X sponsors Plan P, which provides for matching contributions equal to 50% of elective deferrals that do not exceed 10% of compensation. Elective deferrals for highly compensated employees are limited, on a payroll-by-payroll basis, to 10% of compensation. Employer X pays employees on a monthly basis. Plan P also provides that elective contributions are limited in accordance with section 401(a)(30) and other applicable statutory limits. Plan P also provides for catch-up contributions. Under Plan P, for purposes of calculating the amount to be treated as catch-up contributions (and to be excluded from the ADP test), amounts in excess of the 10% limit for highly compensated employees are determined at the end of the plan year based on compensation used for purposes of ADP testing (testing compensation), a definition of compensation that is different from the definition used under the plan for purposes of calculating elective deferrals and matching contributions during the plan year (deferral compensation).

(ii) Participant A, a highly compensated employee, is a catch-up eligible participant under Plan P with deferral compensation of \$10,000 per monthly payroll period. Participant A defers 10% per payroll period for the first 10 months of the year, and is allocated a matching contribution each payroll period of \$500. In addition, Participant A defers an additional \$4,000 during the first 10 months of the year. Participant A then reduces deferrals during the last 2 months of the year to 5% of compensation. Participant A is allocated a matching contribution of \$250 for each of the last 2 months of the plan year. For the plan year, Participant A has \$15,000 in elective deferrals and \$5,500 in matching contributions.

(iii) A's testing compensation is \$118,000. At the end of the plan year, based on 10%

of testing compensation, or \$11,800, Plan P determines that A has \$3,200 in deferrals that exceed the 10% employer provided limit. Plan P excludes \$3,200 from ADP testing and calculates A's ADR as \$11,800 divided by \$118,000, or 10%. Although A has not been allocated a matching contribution equal to 50% of \$11,800, because Plan P provides that matching contributions are calculated based on elective deferrals during a payroll period as a percentage of deferral compensation, Plan P is not required to allocate an additional \$400 of matching contributions to A.

(i) *Effective date*—(1) *Statutory effective date.* Section 414(v) applies to contributions in taxable years beginning on or after January 1, 2002.

(2) *Regulatory effective date.* Paragraphs (a) through (h) of this section apply to contributions in taxable years beginning on or after January 1, 2004.

Robert E. Wenzel,
Deputy Commissioner for Services and Enforcement.

Approved: June 27, 2003.

Pamela F. Olson,
Assistant Secretary (Tax Policy).
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ENVIRONMENTAL PROTECTION AGENCY

40 CFR Part 52

[VA127-5064; FRL-7523-2]

Approval and Promulgation of Air Quality Implementation Plans; Virginia Nitrogen Oxides Budget Trading Program

AGENCY: Environmental Protection Agency (EPA).

ACTION: Final rule.

SUMMARY: EPA is approving a State Implementation Plan (SIP) revision submitted by the Commonwealth of Virginia which consists of its nitrogen oxides (NO_x) allowance trading program for large electric generating and industrial units, with the exception of the programs' NO_x allowance banking provisions, which EPA is conditionally approving. The effect of this action is to approve the Virginia NO_x Budget Trading Program, with conditions on the approval of its allowance banking provisions, because the program substantively addresses the requirements of Phase I of the NO_x SIP Call which will significantly reduce ozone transport in the eastern United States.

EFFECTIVE DATE: This final rule is effective on August 7, 2003.