



## Compliance News

### *Pension Protection Act Passes Congress*

The Pension Protection Act passed the House of Representatives on July 28, 2006, and the Senate on August 3, 2006. President Bush is expected to sign the bill into law shortly. The bill is intended to strengthen workers' retirement security by changing defined benefit plan funding rules, legitimizing cash balance plans, encouraging automatic enrollment in 401(k) plans, making permanent the improvements in the Economic Growth and Tax Relief Reconciliation Act (EGTRRA), and allowing for the creation of a combination defined benefit and 401(k) plan, called the DB(k). The bill also extends the use of corporate bonds rates for funding through 2006 and 2007. Most changes are effective with plan years that begin in 2008.

#### EGTRRA PERMANENCY

The increased limits in the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) were set to expire after 2010. The bill makes the EGTRRA retirement plan changes and IRA changes, including the low-income Saver's Credit, permanent.

#### AUTOMATIC ENROLLMENT

The bill provides an automatic enrollment safe harbor design for 401(k), 403(b), and governmental 457 plans that gives relief from nondiscrimination and top heavy testing. It also gives relief from state tax withholding laws and directs the Department of Labor to issue fiduciary safe harbors for default investments.

#### OTHER DEFINED CONTRIBUTION (DC) PLAN CHANGES

- The act encourages 401(k) sponsoring firms to hire outside financial advisors to provide personal retirement guidance to workers.
- Allows employers to automatically increase employee deferrals.
- The act sanctions the use of suitable "default" investments for workers who don't choose specific investments.
- Creates two new prohibitive transaction exemptions for giving investment advice to plan participants.
- Requires that plan participants have immediate diversification rights with respect to elective deferrals and employee contributions.
- Allows taxpayers to direct the IRS to rollover the refund of their income tax directly into an IRA of the taxpayer's choice.
- Permits a non-spouse beneficiary a tax-free rollovers between a qualified, 403(b), and governmental 457 plan and an IRA.



# National Retirement Partners

## DEFINED BENEFIT (DB) PLAN CHANGES

- Makes substantial changes to the funding rules for multi-employer collectively bargained plans.
- Clarifies that cash balance plans are not inherently age discriminatory, benefits must be fully vested in three years, interest credits cannot exceed a market rate of return, and pay credits cannot be lost.
- Requires lump sum benefit payments to be based on the same yield curve approach used for pension funding, phased in over five years beginning in 2008.
- Increases disclosure requirements for all plans so that participants are better aware of the funding status of their employer's plan.

## SINGLE EMPLOYER PLAN FUNDING

The bill changes the current defined benefit funding rules after 2007 to require:

- A funding target of 100% of current liability. Plans that are fairly well funded can phase-in the 100% target from 2008-2010. Plans that are required to make a deficit reduction calculation in 2007 are not eligible for the phase-in.
- The difference between current liability and assets to be amortized over 7 years.
- The current liability to be measured using a modified yield curve interest rate.

## "AT-RISK" PLANS

A plan is considered "at risk" based on its funding status. At-risk plans are subject to accelerated funding requirements. Plans with fewer than 500 participants are exempt from the at-risk rules.

## RESTRICTIONS ON BENEFITS

A plan's funding status triggers the following:

- Below 80% funded – Prohibits amendments to increase benefits (unless certain conditions exist).
- Between 60% and 80% funded – Prohibits lump sum benefits generally in excess of 50% of the participant's accrued benefit.
- Below 60% funded:
  - Freezes benefit accruals
  - Prohibits plant shutdown benefits
  - Prohibits lump sum benefits
  - Restricts nonqualified executive compensation arrangements

## MODIFIED YIELD CURVE

The yield curve is based on a 24-month average of the yield on AAA, AA, and A rated corporate bonds of varying maturities. The modified yield curve interest rate for valuing liabilities includes three interest rates; for liabilities due in under 5 years, between 5 and 20 years, and in over 20 years. The change in calculating a plan's liabilities is phased in during 2008 and 2009.

