

TCRS 2006-05: The Pension Protection Act of 2006¹

On August 17, 2006, President Bush signed the Pension Protection Act of 2006. This landmark legislation provides the legal framework for defined contribution plans that will enable plan sponsors to maximize the effectiveness of their retirement plan and help their plan participants with building their nest eggs in preparation for retirement. The Transamerica Center for Retirement Studies² has prepared this summary of the new law and the attached outline of its provisions in order of effective date.

The Pension Protection Act of 2006 includes key provisions related to defined contribution retirement plans regarding:

- 401(k) plans with auto-enrollment, default investments such as strategic allocation or target maturity funds, annual deferral increases, and a safe harbor plan design provided certain requirements are met.
- Investment advice through the plan sponsor's retirement plan provider or an independent third party. Advice may take the form of a computer-based model that is audited by an independent third party, or it may be in the form of a compensation-based model in which a credentialed financial adviser delivers the advice for a fee that is not dependent on the participant's decision of whether or how to follow the advice.
- Economic Growth and Tax Relief Reconciliation Act of 2001 ("EGTRRA") permanence. Certain provisions of EGTRRA that were scheduled to sunset have been made permanent. These provisions include increased contribution limits to retirement plans and IRAs, catch-up contributions for individuals age 50 and older, the Saver's Credit for employees who meet certain income requirements, and the Roth 401(k) plan.
- Defined contribution plan design and administration provisions including annuities as an optional form of distribution, investment mapping, accelerated vesting, and expansion of hardship withdrawal rules.
- A new plan design, DB(k), to become effective beginning in 2010. This new plan design fully integrates a defined benefit feature as well as a defined contribution feature.

The Pension Protection Act of 2006 offers a wide array of opportunities for plan sponsors to enhance their defined contribution retirement plans. Now is the perfect time for plans sponsors to work with their plan advisers and retirement plan providers to determine which of these new opportunities is right for them and their participants and how to maximize their effectiveness.

Over the coming months, Transamerica Retirement Services³ will be reaching out to plan sponsors, advisers and third-party administrators to provide additional expertise and insights about this new legislation as we roll out innovative new product and service offerings that incorporate the opportunities created by the Pension Protection Act of 2006.

¹ This Summary is designed to provide an overview of H.R. 4-The Pension Protection Act of 2006 and is not intended to be comprehensive. Transamerica Retirement Services and its representatives cannot give ERISA, tax or legal advice. This material is provided for informational purposes only based on our understanding of the new law and should not be construed as ERISA, tax or legal advice. Clients and other interested parties must consult and rely solely upon their own independent advisors regarding their particular situation and the concepts presented here. Although care has been taken in preparing this material and presenting it accurately, TRS disclaims any express or implied warranty as to the accuracy of any material contained herein and any liability with respect to it.

² The Transamerica Center for Retirement Studies ("The Center") is a collaboration of experts assembled by Transamerica Retirement Services to promote public awareness of emerging trends surrounding retirement security in the United States.

³ Transamerica Retirement Services (Transamerica or TRS), a marketing unit of Transamerica Financial Life Insurance Company and other of its affiliates, specializes in the promotion of retirement plan products and services.

The Pension Protection Act of 2006 (“ACT”)

ACT PROVISION	EFFECTIVE DATE
<ul style="list-style-type: none"> • Distributions to Certain Reservists – 401(k) plan distributions made after September 11, 2001 to reservists called up for duty between September 11, 2001 and December 31, 2007 and serve more than 179 days are exempt from the 10 percent early withdrawal tax. Such distributions may be repaid within 2 years following the end of active duty. 	Distributions after September 11, 2001
<ul style="list-style-type: none"> • Sarbanes-Oxley – The blackout notice requirement is removed for plans that benefit the sole owner/partners only and their spouses. 	Retroactive to the original effective date of Sarbanes-Oxley
<ul style="list-style-type: none"> • EGTRRA Permanency – The Act makes permanent certain pension-related provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001 (“EGTRRA”). These include: <ul style="list-style-type: none"> ○ Higher Contribution/Maximum Compensation Limits ○ Higher Employer Deduction Limits ○ Annual Limit Increases ○ Catch-up Contributions ○ Roth 401(k) ○ Enhanced Portability ○ Expanded Rollover Options ○ Saver’s Credit <p>Without EGTRRA permanency, these provisions would have sunset in 2010 (2006 for the Saver’s Credit). The EGTRRA sunset would have been unfavorable to participants and plan sponsors alike. For example, the overall participant limit on contributions will now remain at 100 percent of compensation rather than reverting to 25 percent as in effect prior to EGTRRA. In addition, the employer deduction limit of 25 percent of eligible payroll will remain at this level rather than reverting to the pre-EGTRRA level of 15 percent for profit sharing plans.</p>	Date of enactment
<ul style="list-style-type: none"> • Increase in Penalties for Coercive Interference with Exercise of ERISA Rights – The criminal penalties for coercive interference with the exercise of ERISA rights has been increased to \$100,000 and imprisonment for up to ten years. Previously, the maximum penalty was \$10,000 and 1 year of imprisonment. 	Violations occurring on and after date of enactment
<ul style="list-style-type: none"> • Tribal Government Plans – The definition of governmental plan is expanded to include a plan of an Indian tribal government, a subdivision of an Indian tribal government, or an agency or instrumentality of either, if all of the plan participants are employees of the entity substantially all of whose services are in the performance of essential government functions (but not in the performance of commercial activities). 	Plan years beginning on and after date of enactment
<ul style="list-style-type: none"> • Safest Available Annuity – The Act requires the Department of Labor (DOL) to issue final regulations within 1 year of the date of enactment clarifying that the selection of an annuity contract as an optional form of distribution from a defined contribution plan is not subject to the “safest available annuity” standard, but would be subject to other applicable fiduciary standards. 	Date of enactment

This Summary is designed to provide an overview of H.R. 4-The Pension Protection Act of 2006 and is not intended to be comprehensive. Transamerica Retirement Services and its representatives cannot give ERISA, tax or legal advice. This material is provided for informational purposes only based on our understanding of the new law and should not be construed as ERISA, tax or legal advice. Clients and other interested parties must consult and rely solely upon their own independent advisors regarding their particular situation and the concepts presented here. Although care has been taken in preparing this material and presenting it accurately, TRS disclaims any express or implied warranty as to the accuracy of any material contained herein and any liability with respect to it.

The Pension Protection Act of 2006 (“ACT”)

ACT PROVISION	EFFECTIVE DATE
<ul style="list-style-type: none"> • Expansion of Hardship Rules – The Act requires the Treasury Department to expand the definition of hardship, within 180 days of the date of enactment, to include the hardship of a non-spouse or non-dependent beneficiary. 	Date of enactment
<ul style="list-style-type: none"> • Domestic Relations Orders – The DOL is required to issue regulations, within one year of the date of enactment, clarifying that a domestic relations order will not fail to be a qualified domestic relations order merely because it is issued after, or revises, another order, or because of the time the order is issued. 	Date of enactment
<ul style="list-style-type: none"> • Nondiscrimination Requirements for Governmental Plans – Governmental plans are exempt from the nondiscrimination requirements. 	Years beginning after date of enactment
<ul style="list-style-type: none"> • Simplified Reporting – Simplified reporting on Form 5500 is available for plan years beginning after December 31, 2006 for certain plans with 25 or fewer participants. 	Date of enactment
<ul style="list-style-type: none"> • Default Investments - The DOL must issue regulations within 6 months of the date of enactment, providing guidance on the appropriateness of certain investments for designation as default investments, such as those used with automatic enrollment, but the guidance is expected to cover more than automatic enrollment. 	Plan years beginning after December 31, 2006
<ul style="list-style-type: none"> • Accelerated Vesting for Nonelective Contributions – The Act applies the vesting schedules currently in effect for matching contributions to nonelective contributions. 	Contributions made for plan years beginning after 2006 (delayed date for collectively bargained plans & certain ESOPs)
<ul style="list-style-type: none"> • Direct Rollover of Beneficiary Distributions – Benefits received from retirement plans by non-spouse beneficiaries may be rolled directly into an IRA. 	Distributions after December 31, 2006
<ul style="list-style-type: none"> • Extension of Joint and Survivor Consent Period – The earliest date to provide joint and survivor distribution notices is changed from 90 days to 180 days before the annuity starting date. 	Plan years beginning after December 31, 2006
<ul style="list-style-type: none"> • New Diversification Rules – The Act added new diversification rules designed to limit the ability of plans (except certain ESOPs) to require investment in employer securities. Under these new rules, participants must be permitted to diversify their contributions immediately, and those with 3 or more years of service must be allowed to diversify other contributions. 	Plan years beginning after December 31, 2006 (delayed date for collectively bargained plans)
<ul style="list-style-type: none"> • Periodic Statements – Quarterly statements are required for participant-directed plans (annually for other plans). Within one year of the date of enactment, the DOL will issue one or more model benefit statements that will satisfy this requirement. Statements must include an explanation of the importance of portfolio diversification, a discussion of the inherent risk of holding more than 20 percent of the portfolio in a single security and a statement that additional information is available on the DOL website. 	Plan Years beginning after December 31, 2006 (delayed date for collectively bargained plans)

This Summary is designed to provide an overview of H.R. 4-The Pension Protection Act of 2006 and is not intended to be comprehensive. Transamerica Retirement Services and its representatives cannot give ERISA, tax or legal advice. This material is provided for informational purposes only based on our understanding of the new law and should not be construed as ERISA, tax or legal advice. Clients and other interested parties must consult and rely solely upon their own independent advisors regarding their particular situation and the concepts presented here. Although care has been taken in preparing this material and presenting it accurately, TRS disclaims any express or implied warranty as to the accuracy of any material contained herein and any liability with respect to it.

The Pension Protection Act of 2006 (“ACT”)

ACT PROVISION	EFFECTIVE DATE
<ul style="list-style-type: none"> • Saver’s Credit – The income limit for the Saver’s Credit will be indexed for inflation. 	Taxable years beginning after December 31, 2006
<ul style="list-style-type: none"> • Rollover of After-Tax Amounts in Section 403(b) Annuity Contracts – After-tax amounts in 403(b) annuity contracts may be rolled over into a qualified plan. 	Taxable years beginning after December 31, 2006
<ul style="list-style-type: none"> • Fiduciary Responsibility for Selecting an Investment Adviser – A plan fiduciary who arranges for the provision of investment advice will not violate the fiduciary requirements if: <ul style="list-style-type: none"> ○ Advice is provided by a permitted fiduciary adviser; ○ The fiduciary adviser is required under the arrangement to comply with the requirements for investment advice exemption; and ○ The terms of the arrangement require the adviser to acknowledge in writing that it is a plan fiduciary with respect to investment advice. 	Investment advice provided after December 31, 2006
<ul style="list-style-type: none"> • Investment Advice – The Act adds a new statutory exemption for the provision of investment advice to participants and beneficiaries. This exemption allows: <ul style="list-style-type: none"> ○ “Fiduciary advisers” to render investment advice; ○ Investment advice to be given with respect to the fiduciary’s own investment products; and ○ Investment advice to be given under an “eligible investment advice arrangement.” <p>An eligible investment advice arrangement is an arrangement:</p> <ul style="list-style-type: none"> ○ That is based on a computer model that is certified and audited by an independent third party; or under which the fiduciary’s fees do not vary depending on the investment option selected. 	Investment advice provided after December 31, 2006
<ul style="list-style-type: none"> • Form 5500-EZ – One-participant plans with assets not exceeding \$250,000 will be exempt from filing Form 5500-EZ. 	Plan years beginning after December 31, 2006
<ul style="list-style-type: none"> • Special Catch-up Provision for Certain 401(k) Participants – Certain catch-up eligible participants in certain 401(k) plans of bankrupt employers under criminal indictment or conviction may make special IRA catch-up contributions for 2007, 2008, and 2009. 	Taxable years beginning after December 31, 2006 and before January 1, 2010
<ul style="list-style-type: none"> • Electronic Display of Form 5500 Information – The Act requires the DOL to electronically display certain information related to the Form 5500 annual filing within 90 days of receipt of the information and employers are required to display the same information on their intranet website (if available). 	Plan Years beginning after December 31, 2007

This Summary is designed to provide an overview of H.R. 4-The Pension Protection Act of 2006 and is not intended to be comprehensive. Transamerica Retirement Services and its representatives cannot give ERISA, tax or legal advice. This material is provided for informational purposes only based on our understanding of the new law and should not be construed as ERISA, tax or legal advice. Clients and other interested parties must consult and rely solely upon their own independent advisors regarding their particular situation and the concepts presented here. Although care has been taken in preparing this material and presenting it accurately, TRS disclaims any express or implied warranty as to the accuracy of any material contained herein and any liability with respect to it.

The Pension Protection Act of 2006 (“ACT”)

ACT PROVISION

EFFECTIVE DATE

- **Automatic Enrollment in 401(k) Plans** – The Act addresses employer concerns regarding automatic enrollment and provides incentives and safe harbors provided certain conditions are met and is designed to increase participation and simplify administration.
 - General Provisions:
 - Automatic enrollment is optional for employers.
 - An employee notice similar to the current safe harbor notice is required.
 - ERISA will preempt state withholding laws provided the annual employee notice requirement is satisfied and the plan meets the default investment guidelines prescribed by the DOL.
 - Automatic enrollment applies to all employees, including highly compensated employees, but may exempt certain employee groups.
 - Default funds must be invested in accordance with guidelines established by the Department of Labor (DOL). The Act directs the DOL to issue minimum standards required to retain ERISA preemption.
 - Automatically-enrolled employees have a 90-day penalty-free opt-out period, provided the plan satisfies the notice requirement.
 - Employees who opt out will be entitled to a corrective distribution (contributions made during first 90 days plus income). The corrective distribution is taxable, is disregarded in the ADP test and exempt from the 10 percent early withdrawal tax.
 - Excess ADP/ACP contributions if returned to participants within 6 months following the plan year-end will be exempt from the 10 percent excise tax.
 - Optional Safe Harbor Provisions:
 - 100 percent match of first 1 percent of pay, plus 50 percent match of the next 5 percent of pay (maximum 3.5 percent of pay); **or** a 3 percent of pay nonelective contribution.
 - Entry level deferral contribution must be between 3 percent and 10 percent, and must not be less than 4 percent in year two, 5 percent in year three and 6 percent in each year thereafter.
 - 100 percent vesting after 2 years.
 - Exempt from ADP/ACP tests, and deemed to meet the top-heavy requirements, if certain conditions are met.
- **Modifications to Combined Employer Deduction Limit** – The employer combined deduction limit that applies when an employer sponsors both defined benefit and defined contribution plans will be computed without regard to all defined benefit plans of the employer covered by the PBGC. For 2006 and 2007, the combined limit would not apply if employer contributions to the defined contribution plan(s) do not exceed 6 percent of eligible payroll. Elective deferrals continue to be disregarded in determining the deduction limit.
- **Increase in Fiduciary Bond** – The maximum fiduciary bond amount is increased from \$500,000 to \$1,000,000 for plans that hold employer securities.

Plan Years beginning after December 31, 2007, except for ERISA preemption which is effective on date of enactment

Generally, for taxable years beginning after December 31, 2007

Plan Years beginning after December 31, 2007

This Summary is designed to provide an overview of H.R. 4-The Pension Protection Act of 2006 and is not intended to be comprehensive. Transamerica Retirement Services and its representatives cannot give ERISA, tax or legal advice. This material is provided for informational purposes only based on our understanding of the new law and should not be construed as ERISA, tax or legal advice. Clients and other interested parties must consult and rely solely upon their own independent advisors regarding their particular situation and the concepts presented here. Although care has been taken in preparing this material and presenting it accurately, TRS disclaims any express or implied warranty as to the accuracy of any material contained herein and any liability with respect to it.

The Pension Protection Act of 2006 (“ACT”)

ACT PROVISION	EFFECTIVE DATE
<ul style="list-style-type: none"> • Investment Mapping – The Act clarifies that ERISA Section 404(c) protection applies to changes in investment options (a common practice referred to as “mapping”, for example, when plans switch service providers), provided certain requirements are satisfied. 	Plan years beginning after December 31, 2007 (delayed date for collectively bargained plans)
<ul style="list-style-type: none"> • Direct Rollovers from Retirement Plan to Roth IRA – Individuals with AGI not exceeding \$100,000 may make a direct rollover from a retirement plan to a Roth IRA. Amounts rolled over would be subject to income tax, but exempt from the 10 percent early withdrawal tax. Roth IRA conversion rules would apply. 	Distributions made after December 31, 2007
<ul style="list-style-type: none"> • Additional Joint and Survivor Annuity Option – Certain money purchase plans are required to offer a joint and 75 percent survivor annuity. 	Plan years beginning after December 31, 2007 (delayed date for collectively bargained plans)
<ul style="list-style-type: none"> • Missing Participants – The Pension Benefit Guaranty Corporation’s missing participant program for defined benefit plans is expanded to cover terminated defined contribution plans. 	Distributions made after final regulations are issued
<ul style="list-style-type: none"> • Modification to Employee Plans Compliance Resolution System – The Act gives the Internal Revenue Service authority to design, modify, and waive income or excise taxes with respect to the Employee Plans Compliance Resolution System or any successor program. 	Unspecified
<ul style="list-style-type: none"> • DB(k) - The Act permits a new kind of plan, the DB(k), a combination defined benefit and 401(k) plan for employers with 500 or less employees as of the date of plan establishment. Key features of the DB(k) include: 	Plan years beginning after December 31, 2009
<ul style="list-style-type: none"> • Single plan and trust document. <ul style="list-style-type: none"> ○ Single Form 5500. ○ Each portion of the plan will be subject to its respective rules under the Internal Revenue Code and ERISA. ○ The defined benefit portion is required to provide either (1) a minimum benefit of 1 percent of final pay per year of service up to 20 years or (2) a cash balance formula. Full vesting is required after 3 years. ○ The 401(k) portion must constitute an automatic enrollment plan with a default deferral contribution of 4 percent of pay, provide a minimum match of 50 percent of at least the first 4 percent of pay, immediate vesting, and must satisfy other current safe harbor requirements. ○ Nonelective contributions are permitted, but must be fully vested after 3 years. ○ A DB(k) is exempt from ADP/ACP and top-heavy testing. However, each portion of the DB(k) will have to separately satisfy coverage and other nondiscrimination requirements. 	

Plan Amendment Requirement – Plans are required to be amended to conform to the Act by the last day of the first plan year beginning on and after January 1, 2009 (2011 for governmental plans). Operational compliance is required starting on the respective effective dates.

This Summary is designed to provide an overview of H.R. 4-The Pension Protection Act of 2006 and is not intended to be comprehensive. Transamerica Retirement Services and its representatives cannot give ERISA, tax or legal advice. This material is provided for informational purposes only based on our understanding of the new law and should not be construed as ERISA, tax or legal advice. Clients and other interested parties must consult and rely solely upon their own independent advisors regarding their particular situation and the concepts presented here. Although care has been taken in preparing this material and presenting it accurately, TRS disclaims any express or implied warranty as to the accuracy of any material contained herein and any liability with respect to it.