H.R. 4—Pension Protection Act of 2006 (PPA)

Prior to being signed into law on August 17, 2006, the Pension Protection Act of 2006 (PPA) had been under consideration by Congress for several years. The legislation is in part a response to recent failures of large defined benefit plans and the funding shortage of the Pension Benefit Guaranty Corporation (PBGC). Congress also recognized the need to provide more incentive for young workers to enroll in 401(k) plans. To some, the PPA represents the most significant and comprehensive changes to federal laws pertaining to retirement plans in the past 30 years, while others are disappointed that it will not provide security for millions who are facing retirement.

With over 900 pages, the Act covers a wide range of issues. Some of the key provisions from the House Committee on Education & the Workforce summary of the Act are noted below.

Funding Rules for Single-Employer Defined Benefit Plans

For single-employer defined benefit plans, the Act:

- Provides a new interest rate based on a modified "yield curve" for employers to more accurately measure current pension liabilities.
- Requires employers to make sufficient contributions to plans in order to meet a 100% funding target and erase funding shortfalls within seven years.
- Triggers accelerated contributions for "at-risk" plans.
- Permits employers to make additional maximum deductible contributions of up to 180% of current liability.
- Prohibits employers and union leaders from increasing benefits if a plan is less than 80% funded, unless the benefits are paid for immediately.
- Prohibits further benefit accruals for lump-sum distributions or shutdown benefits from plans funded at less than 60%.
- Restricts the use of deferred executive compensation arrangements for employers with severely underfunded plans.

Funding Rules for Multiemployer Defined Benefit Plans

For multiemployer defined benefit plans, the Act:

- Includes detailed new rules for multiemployer plans, requiring plans that fail to meet certain funding and other tests to adopt funding improvement plans or rehabilitation plans.
- Changes the amortization schedule for any planned benefit amendments from 30 years to 15 years.
- Increases the maximum deductible limit to 140% of current liability, providing additional funding flexibility for plans each year.
- Requires plan trustees to improve the health of the plan by one-third within 10 years if a plan is less than 80% funded or will hit a funding deficiency within seven years.
- Prohibits benefit increases if the increase causes the plan to fall below 65% funded status
- Establishes new funding standards and possible benefit restructuring for multiemployer plans that are funded at less than 65%.

Investment Advice

With regard to investment advice, the Act:

- Creates a new category of prohibited transaction exemption under ERISA for providing investment advice after 2006 through an "eligible investment advice arrangement" to participants and beneficiaries of a defined contribution plan who direct the investment of their accounts under the plan and to the beneficiaries of IRAs.
- Allows qualified "fiduciary advisors" to offer face-to-face, personally tailored investment advice to help employees manage their 401(k) and other retirement options.
- Requires tough fiduciary and disclosure safeguards to ensure that advice provided to employees is solely in their best interest.
- Requires fiduciary advisors for employer-sponsored plans to base their recommendations on a computer model that is certified and audited by an independent party.

Hybrid Pension Plans

For hybrid pension plans, the Act:

- Establishes legal certainty for hybrid pension plans by ending the legal uncertainties surrounding cash balance pension plans.
- Establishes an age discrimination standard for all defined benefit plans that clarifies current law with respect to age discrimination requirements under ERISA on a prospective basis.
- Provides rules for converting defined benefit plans into cash balance plans.

Other Provisions

Other provisions of the Act include the following:

- PPA includes a new safe harbor that encourages employers to offer automatic enrollment in defined contribution plans with salary deferrals, while giving workers the option to opt out of making the deferral.
- PPA makes permanent the retirement plan provisions under the Economic Growth and Tax Relief Reconciliation Act of 2001. This includes the "savers' credit" and savings provisions under §529.
- PPA provides for tax-free rollovers from the IRA or retirement plan of a deceased individual to an IRA or retirement plan of a non-spouse beneficiary.
- Defined contribution plans' vesting will be limited to three years cliff or six years for graded vesting starting at no less than 20% per year after two years of service.
- PPA requires defined contribution plans other than ESOPs holding publicly traded employer securities to offer a new diversification requirement beginning in 2007.
- Beginning in 2007, PPA indexes the income limits for deductible IRA contributions for active participants in an employer-sponsored plan and the $150,000 income limit for deductible contributions to a spousal IRA. PPA also indexes the $95,000 and $150,000 AGI phaseout figures pertaining to eligibility for Roth IRA contributions.
- Beginning in 2008, PPA allows distributions from qualified retirement plans, tax-sheltered annuities, and governmental 457 plans to be rolled over directly into a Roth IRA.
- The Act provides for phased retirement allowing in-service distributions to participants who have attained age 62 and have not yet separated from employment.

- PPA will allow rollovers between SIMPLE IRAs and other tax-favored retirement plans within the first two years of participation.
- PPA provides new rules for employer-owned life insurance contracts to provide income-tax-free death benefits. These requirements include the insured being an employee within 12 months of his or her death, the insured being a highly compensated employee, and the proceeds being paid to the individual's family or designated beneficiary or used to buy an equity or partnership interest from the family member or beneficiary. Notice and consent requirements are also required—i.e., the employee must be notified and provide written consent.
- PPA will allow long-term care insurance coverage to be combined with annuity contracts.

Summaries along with the actual Act are available at *The Library of Congress: Thomas*