



Fourth Quarter 2006

Retirement PLAN WATCH

LINKS and LINES

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Pension Protection Act of 2006

In early August, Congress passed the Pension Protection Act of 2006 (PPA). This new legislation was designed in great part to strengthen traditional pension plans and help to stabilize them before employers resort to bankruptcy. The new law also strengthens the Pension Benefit Guaranty Corporation (PBGC), the pension provider of last resort.

EGTRRA Provisions

A long list of benefits introduced by the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) have been made permanent by PPA. The following provisions no longer face a sunset in 2010:

- Higher IRA contributions (\$4,000 in 2006; \$5,000 in 2008; adjusted by inflation thereafter)
- Higher defined contribution plan limits – i.e., the \$415 limit (\$44,000 in 2006; \$45,000 in 2007), higher elective deferral limits – i.e., the §402(g) limit (\$15,000 in 2006; \$15,500 in 2007), higher SIMPLE plan limits (\$10,000 in 2006; \$10,500 in 2007) (this also means the MEA is really dead!!)
- Higher benefit limit under a defined benefit plan (\$175,000 for 2006; \$180,000 in 2007)
- Catch-up contributions for taxpayers over age 50 (\$1,000 for IRAs, \$2,500 for SIMPLE plans, and \$5,000 for employer plans in 2006 and 2007)
- Faster vesting of employer matching contributions
- Greater portability for §457 plans

- Higher deduction limit for stock bonus and profit sharing plans (25%)
- Roth §403(b) and Roth §401(k) permanency
- Portability for eligible retirement plans and IRAs
- ESOP enhancements
- Modifications to the top-heavy nondiscrimination and coverage rules
- Authorization for IRS to waive the 60-day rollover rule under events beyond the taxpayer's control

Note: The over-50 catch-up for IRAs is not indexed to inflation. The over-age catch-up for SIMPLE IRAs and employer plans is indexed to inflation in \$500 increments. The §402(g) elective deferral limits for §401(k)s, §403(b)s, SAR-SEPs and SIMPLE IRAs, the §457 elective deferral limit and the §415 annual additions limit are indexed to inflation.

Non-Spouse Beneficiary Transfers

One great provision that we have needed for years will benefit non-spouse beneficiaries. In the past, these beneficiaries have been forced to take lump sum distributions from employer plans because these plans have no provisions to make any other type of payments to this type of beneficiary and a non-spouse beneficiary cannot roll the assets into his/her own name. This new provision will allow a non-spouse beneficiary to transfer the assets into an *inherited* IRA. Note the emphasis on inherited – they still cannot roll the assets into their own names. This provision is effective January 1, 2007.

New §72(t) Premature Penalty Exceptions

The new law waives the premature penalty on distributions from governmental plans for certain public safety employees, i.e., those providing police protection, firefighting services, or emergency medical services, if the employee retires in the year s/he attains age 50 or more. This is effective immediately. Also, distributions from a governmental plan to pay for health or long-term care insurance premiums of a retired public safety employee will be excluded from income up to \$3,000. This provision is effective in 2007.

Miscellaneous Provisions

The automatic enrollment of newly eligible employees into an employer's §401(k) plan has been made easier under the new law.

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Taxpayers may now direct the IRS to deposit their tax refunds into an IRA and, as announced in May, to other accounts. The IRS expects to issue a new form (Form 8888) in time for the 2007 filing season. Taxpayers may use the form to split the deposit of their refunds.

PPA allows taxpayers who have attained age 70½ to donate money to charity from their IRA account. Taxpayers are allowed to donate up to \$100,000 in 2006 and 2007. Since the direct rollovers will be tax-free, the individuals will not be able to claim a tax deduction for the charitable contribution.

The new law extends the nonrefundable "saver's credit," which provides low-income taxpayers who contribute to retirement plans or IRAs a credit of up to \$2,000. In addition, beginning in 2007, the income levels used in determining eligibility for the credit will be indexed.

Taxpayers who are called to active military duty may take penalty-free early distributions from their IRAs and other retirement plans. S/he must be a member of the Reserves who is called to active duty after September 11, 2001 and before December 31, 2007. The new law gives these individuals two years after the end of their military service period to re-contribute the amounts they withdrew and avoid paying income tax on the distributions.

In 2008 it will be possible to convert assets directly from a qualified retirement plan, §403(b) or §457 to a Roth IRA.

The new law also permanently extends the tax free treatment of qualified distributions from §529 plans. It also added stricter rules related to the operation of these plans to prevent abuse.

PPA promulgated new rules for donations of cash, clothing, household items, etc. for charities. Non-itemizers are not permitted to deduct their charitable contributions. Also, no deduction is allowed for used clothing and household items unless the items are in "good" condition. This change is in effect as of the date of enactment.

In a major change, no deduction is allowed for any contribution of cash, check or monetary gift unless the donor can show a bank record or a written communication from the charity indicating the amount of the contribution, the date the contribution was made, and the name of the charity. This new requirement appears to give taxpayers absolutely no leeway. Cash donations, regardless of amount, must be substantiated either by a cancelled check or a bank record. Donations made by debit or credit card can be substantiated by the taxpayer's bank statement. Charities will likely be spending more time and resources on issuing receipts to their supporters.

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Bankruptcy Protection for Retirement Funds

The Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCA) created new rules to protect an individual taxpayer's tax-favored funds, including traditional IRAs, Roth IRAs, §403(b) plans, §457 plans, all types of qualified plans, §529 college savings plans and §530 Coverdell Education Savings Accounts. BAPCA also protects employee funds which have been withheld and not yet deposited to ERISA plans in the case of employer bankruptcies.

Until BAPCA, only plans covered by ERISA had federal protection during bankruptcy. To be considered ERISA-qualified a plan had to cover one or more common-law employees who were not principal owners. After BAPCA, assets held by an employer plan in good standing, or an IRA, are protected from creditors.

Participant loans are permitted from qualified plans, §403(b) plans and §457 plans. Provided that a plan loan meets either the ERISA or Internal Revenue Code standards, it will not be dischargeable in bankruptcy. This protects loans up to \$50,000. Typically, bankruptcy trustees have notified plan administrators that loan repayments from salary withholdings must cease after bankruptcy filing. That has forced plans to put the

loans into default and has triggered premature taxation to participants under §72(p). BAPCA relieves this situation. An employed taxpayer filing for bankruptcy can continue to have loan repayments withheld from salary, and will not be faced with premature income tax burdens on top of his other problems.

BAPCA protection is unlimited, except as follows:

- **“Non-rollover” assets in IRAs limited to \$1,000,000** – protection for regular contributions and the earnings thereon in IRAs is limited to \$1,000,000. This amount does not include rollovers from other tax-favored accounts. For example, an IRA which has \$250,000 from regular contributions and an additional \$850,000 from a qualified plan rollover is fully exempt under BAPCA.
- **Recent deposits to §529 College Savings Plans and Coverdell Education Savings Accounts** – to obtain protection under BAPCA, the savings plan must be established for the benefit of a child, stepchild, grandchild or stepgrandchild. Deposits within 365 days of filing are not protected. Deposits within 720 days of filing which exceed \$5,000 for any one beneficiary are also not protected.

2007 Cost of Living Adjustments

Limit	2006	2007
§402(g) Elective Deferral Limit for §403(b)/§401(k)/SAR-SEP	\$15,000	\$15,500
§457 Elective Deferral Limit	\$15,000	\$15,500
SIMPLE IRA/§401(k) Elective Deferral Limit	\$10,000	\$10,500
§415 Annual Additions Limit to Defined Contribution Plans	\$44,000	\$45,000
Age 50 Catch-up for §403(b)/§401(k)/SAR-SEP	\$5,000	\$5,000
Age 50 Catch-up for SIMPLE IRA/§401(k)	\$2,500	\$2,500
Definition of Highly Compensated Employees	\$100,000	\$100,000
IRA/Roth IRA Annual Contribution Limit	\$4,000	\$4,000
Age 50 Catch-up for IRA/Roth IRA	\$1,000	\$1,000
Compensation that may be considered in defined contribution plans	\$220,000	\$225,000
Income subject to Social Security taxes	\$94,200	\$97,500



Access bills and make changes to participant contributions online!

Employers using ADSERV's Billing Services can now access their bills via the internet and make changes to participants' accounts online. It's convenient, and it improves processing time and accuracy.

When billing changes are submitted by an employer, the information is downloaded and stored in a "workfile" program on our AS/400 system. When the Employee Benefit Account Department receives the money relating to the employer's account, this bill will be pulled from the "workfile" program and processed.

Procedures on submitting checks remain the same.

A unique access code is required in order for each employer to use this system.

1. Call ADSERV at 1-800-749-4221 (other than NY) or 1-800-749-4321 (NY only) to receive your unique employer access code.
2. If you need technical help during the set-up process, or have any questions about using this process, call the appropriate phone number above and ask for Alejandra Salatino at ext. 718.



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