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LOUIS KRAVITZ & ASSOCIATES INC

Information Release

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A New Era in Retirement Plans

The Pension Protection Act of 2006

On August 17 the President signed the Pension Protection Act of 2006 ("PPA 2006") into law. Weighing in at over 900 pages, the new law is the most comprehensive piece of pension legislation since ERISA was enacted in 1974. We are excited that many of the provisions of the new law enhance a taxpayer's ability to save for retirement.

We will address the details of the new law and the effect it will have on our clients' plans at our November seminars. Information about our seminars is on our website at http://www.lkravitz.com. An online brochure containing a detailed summary of PPA 2006 can also be found on our website at http://www.lkravitz.com/ppa.

Most provisions of PPA 2006 do not become effective until plan years beginning in 2008, although certain important provisions, including some that increase tax deductible contributions, go into effect immediately. This information release briefly highlights some of the changes that become effective in 2006 and 2007.

Immediate, Increased Tax Deductions for Defined Benefit and Cash Balance Plans

Maximum tax deductible contributions will increase, for many defined benefit plans, including cash balance plans, beginning in 2006. This will allow employers greater flexibility in determining the amount they contribute to their plans.

Increased Tax Deductions for Combined Defined Benefit and Defined Contribution Plans

In the past, many employers that sponsor both a defined benefit plan (such as a cash balance plan) and a defined contribution plan (such as a profit sharing plan) were limited in the amount they could contribute to their plans. They could not contribute more than 25% of covered payroll in total to the two plans. Beginning in 2006, this 25% limit applies only to the extent that contributions to the defined contribution plan exceed 6% of covered payroll.

What this means is that employers can take a deduction for contributions to their defined benefit plan without regard to their defined contribution plan, if they limit their contribution to their defined contribution plan to 6% of covered payroll. If the contribution to the defined contribution plan exceeds 6% of pay, the first 6% is not counted against the 25% deduction limit.

Cash Balance Plans

For the first time in history, cash balance plans have been given statutory recognition. PPA 2006 addresses several issues with respect to these plans.

- √ Interest credits under cash balance plans can be set at any rate that does not exceed a "market rate of return." The Secretary of the Treasury has been authorized to issue regulations defining "market rate of return." We expect a lot more flexibility in selecting interest rates and in investing plan assets.
- √ Cash balance plans will be required to provide for 100% vesting upon the completion of three years of service. This is effective for plan years beginning in 2008 for plans that were in existence on June 29, 2005 and immediately for all other plans.
- √ The Act makes it clear that cash balance plans do not inherently discriminate on the basis of age. This provision clarifies an area of uncertainty for employers who convert traditional defined benefit plans to cash balance plans

Expansion of Hardship Rules

PPA 2006 makes it easier for 401(k) participants to access their accounts in the event of financial hardship. The new law requires the Treasury Department to expand the definition of hardship to include the hardship of a non-spouse or non-dependent beneficiary. The new rules are to be issued by February 13, 2007.

Liberalized Rollover Rules

Beginning in 2007, non-spousal beneficiaries (for example, parents, children and significant others) will be able to roll benefits received from qualified retirement plans directly into an IRA. There is still a difference in tax treatment between spousal and non-spousal beneficiaries under the IRA. Spousal beneficiaries can wait until the participant would have reached age 70½ before beginning minimum required distributions. Non spousal beneficiaries must begin in the year following the participant's death.

Accelerated Vesting

Beginning in 2007, employer contributions to defined contribution plans (401(k), profit sharing and money purchase plans) must be fully vested after three years of service or vest in accordance with a graded schedule of 20% after two years of service, increasing by 20% for each additional year of service until 100% vesting is reached after six years of service.

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There is much more to PPA 2006 than what is summarized in this information release. We are continuing to analyze the effects that the new law will have on our clients' plans. Our consultants will be advising you of any changes that need to be made to your plans and of any changes that might be advisable to take advantage of the new rules. If you would like more information, consider attending one of our seminars in November or contact your Kravitz consultant.

Louis Kravitz & Associates, Inc. is the largest firm of retirement consultants headquartered in California. We specialize in the design, implementation and administration of virtually every type of retirement plan. Our consultants, actuaries and other specialists have the experience and ability to make certain your retirement plans are properly designed, meet your needs and operate to your satisfaction. We have been dedicated to providing high quality service since our firm was founded in 1977.