

Pension Protection Act of 2006

After years of debate and months of negotiation between House and Senate lawmakers, Congress has passed and the President has signed the Pension Protection Act of 2006 (PPA). Besides strengthening traditional pension plans, the act includes provisions affecting retirement savings plans (such as IRAs and 401(k) plans), charitable deductions, charitable organizations, Section 529 college savings and prepaid tuition plans, and other areas of tax law.

Traditional pension plans

To help ensure the security of employer-provided pension plans, PPA takes measures to ensure full funding, including even stricter requirements on plans deemed “at risk.”

It also prohibits employers maintaining underfunded or terminated single-employer pension plans from funding nonqualified deferred compensation plans (which typically benefit top executives). This provision is effective for transfers or other reservations of assets that occur after Aug. 17, 2006, the date of enactment.

On the other hand, PPA allows assets in excess of 120% of current liability to be used to fund retiree health benefits for both single-employer plans and collectively bargained plans, effective for transfers made after Aug. 17, 2006.

In addition, the act makes permanent the increases in the annual benefit limit that had been set to expire after 2010.

IRAs and defined contribution plans

PPA includes provisions that enhance the retirement savings benefits of IRAs and defined contribution plans, such as 401(k)s, 403(b)s, 457s and SIMPLEs. For example, the act makes permanent provisions from the 2001 tax act that were to “sunset” after 2010. These include the higher annual contribution limits for IRAs and defined contribution

plans, catch-up contributions for those 50 and over, and Roth 401(k) and 403(b) plans. Moreover, PPA makes permanent the Saver’s credit, which had been set to expire Dec. 31, 2006. It also allows taxpayers to direct the IRS to deposit their income tax refunds into an IRA, effective for taxable years beginning after Dec. 31, 2006.

The new law also waives the early withdrawal penalty from IRAs or 401(k)s (and similar plans) for National Guard members and Reservists who are called up between Sept. 11, 2001, and Dec. 31, 2007, for a period exceeding 179 days. Plus it allows repayment within two years of the distribution without regard to the annual contribution limit.



Finally, PPA simplifies the rules for automatic enrollment in employer-sponsored defined contribution plans, effective for plan years beginning after Dec. 31, 2007.

Charitable giving

In an effort to encourage donations, PPA allows taxpayers to make tax-free distributions from their IRAs (up to \$100,000 annually) to tax-exempt charities through 2007, and it extends to Dec. 31, 2007, the enhanced food and book contribution rules that were enacted after Hurricane Katrina.

But to curtail charitable deduction abuses, the act:

- ▶ Allows deductions for cash contributions *only* if the donor can produce a bank record or written communication from the charity as to the contribution amount, effective for contributions made in tax years beginning after Aug. 17, 2006,
- ▶ Allows deductions for donations of clothing and household goods *only* if they are at least in “good condition,” effective after Aug. 17, 2006, and
- ▶ Lowers the threshold for imposing accuracy-related penalties on taxpayers who claim a deduction for donated property for which a qualified appraisal is required, effective for returns filed after Aug. 17, 2006.

In addition, the act clarifies the charitable deduction allowed with respect to easements for buildings and for land and structures located in a historic district.

Charitable organizations

To further curtail charity-related abuses, PPA also tightens federal oversight of the organizations themselves. For example, the act requires reports to the Treasury on an exempt organization’s



acquisition of certain life insurance contracts after Aug. 17, 2006. And it doubles fines and penalties for certain activities by exempt organizations, effective for taxable years beginning after Aug. 17, 2006.

PPA also requires certain organizations that are exempt from annual filing requirements because of their level of gross receipts to file an annual notice with the IRS containing basic contact and financial information, beginning with taxable years beginning after Dec. 31, 2006. And it extends present-law public disclosure requirements applicable to Form 990 to the Unrelated Business Income Tax (UBIT) returns of Section 501(c)(3) organizations, effective for returns filed after Aug. 17, 2006.

The new law also applies an excess benefits transaction tax on any loan, grant, compensation or other similar

payment from a donor-advised fund to a donor, donor advisor or related party, and from a supporting organization to a substantial contributor or related person, effective for transactions after Aug. 17, 2006.

Other provisions

PPA also includes several miscellaneous provisions, the most notable of which is a permanent extension of the Section 529 provisions with respect to college savings and prepaid tuition plans.

But a provision to allow a carryforward of up to \$500 of unused Flexible Spending Account holdings didn’t make it into the final bill. And legislation containing extensions of expiring tax provisions, estate tax relief and an increase in the minimum wage was defeated in the Senate. This legislation may resurface again in some other form. ♣