

## Retirement provisions made permanent in the Pension Protection Act of 2006

The recently passed Pension Protection Act of 2006 includes a number of significant tax incentives to enhance retirement savings for millions of Americans. Specifically, the Act makes permanent a number of retirement plan and IRA liberalizations that were added to the tax laws in 2001 but were set to sunset after 2010. Here are the details.

The Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) substantially increased pension and individual retirement account (IRA) contribution limits through 2010 as well as making other improvements in pensions and retirement savings through enhanced vesting, portability and reduced regulatory burdens. For example, prior to 2001, the maximum amount that a taxpayer could contribute to a tax-favored IRA plan was \$2,000 a year. EGTRRA increased that limit in steps to \$5,000 by 2008. (The limit is \$4,000 today.) The \$5,000 limit will then be increased each year after 2008 to reflect inflation.

The 2001 legislation similarly increased the limits on the maximum tax-deductible amount that an employee can contribute to an employer-sponsored defined contribution retirement plan such as a 401(k) plan. This limit was increased in steps from the \$10,500 a year in effect in 2001 to \$15,000 a year in 2006. That limit will then be adjusted to reflect inflation in years after 2006.

EGTRRA also instituted new catch-up contributions for individuals age 50 and older -- allowing them to annually contribute an extra \$5,000 to 401(k) plans and an extra \$1,000 to IRAs. Catch-up contributions provide a significant savings boost for baby boomers, women previously out of the workforce, and those who fell behind in their retirement savings.

EGTRRA also created incentives for small employers to offer pension plans. As mentioned above, all these favorable provisions were scheduled to end at the conclusion of 2010 (reverting back to pre-EGTRRA law and limits), but under the new law these favorable changes are made permanent.

Similarly, EGTRRA removed existing barriers that prevented employees from being able to take their retirement savings with them when they switched jobs, particularly when they moved from different employment sectors. For the first time, employees changing jobs were permitted to take their retirement savings with them when they moved between 401(k), 403(b) and state and local section 457 arrangements.

If EGTRRA had not been made permanent, this portability would have ended, once again presenting employees with a frustrating set of barriers that often led them to cash out their retirement savings. The new law, however, ensures that these flexible rollover and portability rules will stay in place.

In short, the new law, by making EGTRRA permanent, preserves the advantages of higher employee contribution limits for employer plans, higher IRA contribution limits, more flexible plan rules, portability, a catch-up for those over 50, and an increase in employer contribution limits.

The new law also makes permanent the saver's credit, which would not have been available after 2006 absent the extension.

The saver's credit is a tax credit for low and moderate-income savers (specifically, single individuals with AGI of up to \$25,000 and married couples with AGI of up to \$50,000) who contribute to workplace retirement plans or IRAs. Under this provision, an eligible taxpayer can claim a nonrefundable tax credit for the applicable percentage (50%, 20%, or 10%, depending on filing status and AGI) of up to \$2,000 of his qualified savings contributions. The new law also indexes the saver's credit income limits to prevent this benefit from being eroded by inflation.