



## The Pension Protection Act of 2006

### Introduction


There are over 30,000 Defined Benefit Obligation (DBO) plans that are under funded by a combined total of \$450 billion in the United States. Some companies either have or are contemplating filing bankruptcy based upon their unfunded pension obligations alone. Further, the taxpayer funded Pension Benefit Guaranty Corporation's (PBGC), which guarantees employer provided pensions; deficit has increased from \$11.2 billion to \$23 billion in one year! This is not good news for the average company that sponsors an employee retirement plan and the 44 million Americans who participate in employer provided DBOs and traditional retirement plans. Congress and The President, in response, have enacted a law known as The Pension Protection

Act of 2006 to 1) require companies to fund their plans and 2) to encourage personal savings in approved retirement plans. This Advisory will discuss what it means for all companies and employees in the United States.

### How the Pension Protection Act Affects Companies

If you find yourself as an employer with a large, unfunded pension obligation, don't worry you are not alone or in bad company. Examples of troubled employers with large, unfunded pensions include Fortune 500 companies such as Ford, GM, and Delta. The previous pension law required companies with DBOs to fund their plans at a 90% funded level. Many employers have not been able to keep pace with their plans

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## A CASE STUDY

In a Technical Advice Memorandum, the IRS has stated that gift coupons given to employees as a gift is taxable compensation. In this case, the employer usually gave their employees hams, turkeys, etc... Due to cultural and religious differences, the company decided that it would be better to give each of their employees a gift certificate for \$35 which could be redeemed for

Gifts the employees found appropriate. The IRS decided that because these coupons had an easily discernable value, they should be included as wage income. The Code defines wages very broadly as all remuneration received for services. However, fringe benefits are not taxable because they are so small that accounting for them would be unreasonable and

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at a 90% funded level. Many employers have not been able to keep pace with their plan's pension obligation for many reasons. These reasons include financial down turn, expanded longevity of retirees, and earning low interest rates on the fund assets already in the pension fund.

Employers with under funded plans now have seven years to improve and fund their pension obligations. Those with severely under funded plans will even have less time to fund their plans. To help employers catch up, the law allows a higher limit on the amount of contributions that are tax deductible while requiring more funding of the PBGC.

### **How the Pension Protection Act Affects Employees**

In many studies performed as of late, it has been revealed that the vast majority of individuals are not putting enough away for retirement. In fact, some people are putting absolutely nothing away at all. The Pension Protection Act of 2006 makes the retirement savings incentives enacted as part of the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) permanent. Had the Pension Protection Act of 2006 not been enacted, the retirement savings provisions of EGTRRA would have expired December 31, 2010.

Among the provisions made permanent are: 1) Higher dollar amounts for IRA contributions (\$4000 in 2006, \$5000 in 2008, inflation adjusted thereafter); 2) Permanent higher dollar limits on defined contribution plans; 3) Permanent increase in the annual benefit limit under defined benefit plans; 4) Permanent "catch up" contributions for older workers (\$1000 additional dollars per year for IRAs); 5) Permanent enhanced rollover rules for retirement accounts; and 6) Roth 401(k)s and Roth 403(b)s are made permanent.



### **Conclusion**

Hopefully, the Pension Protection Act of 2006 will encourage businesses to make good on promises they made decades ago to provide for retiring workers. Additionally, and with the same hope, individuals will take the same initiative to take part in their own retirement planning. With the dire predications made for the Social Security Fund, it is likely Social Security will not be able to live up to the benefits that have been promised. As such, businesses and individuals must bear more responsibility in their own retirement planning. The Center routinely creates retirement plans along with business succession plans and valuations of companies. If you have any questions or would like to begin pension planning, succession planning, or need a business valuation, contact The Center for further details.

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impracticable. The exception to this rule is that cash fringe benefits are never excludible from income. Given that these coupons had a discernable value, they had to be included in income. (TAM 200437030)

**Editor's Comment:** Given that the holiday season coming up and many employers are faced with this exact situation, this is a very useful case. There has been some comment on this case stating that it may be overturned in the future. For now, employers must stick to hams, turkeys, and other de minimis items to gift to their employees.

## Points of Interest

- **There are over 30,000 Defined Benefit Obligation (DBO) plans that are under funded by a combined total of \$450 billion in the United States.**
- **In many studies performed as of late, it has been revealed that the vast majority of individuals are not putting enough away for retirement. In fact, some people are putting absolutely nothing away at all.**
- **If you find yourself as an employer with a large, unfunded pension obligation, don't worry you are not alone or in bad company.**

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### Avoiding Common Mistakes in M&A – Time Kills All Deals

There is probably no greater truth in all M&A activities – for Buyers, Sellers and M&A Advisors alike – than “Time Kills All Deals.”

In my experience, no other factor has caused more potentially good deals to go bad than letting the M&A process between two parties drag on and on until it eventually grinds to a halt.

While M&A Advisors play a large role in leading/setting the pace of negotiations, due diligence and pre-closing preparations, all parties share responsibility for ensuring that they – and their advisors – come to the discussions fully prepared and poised to give this matter their full attention and priority.

Whether you're a Buyer or a Seller, your M&A Advisor should provide you with a checklist of the Things You'll Need To Get Started, as well as a much more detailed checklist of Things You'll Need to Complete Due Diligence.

Some tips to keep you out in front of the process:

- Assemble basic information in advance
- Prepare a Confidential Company Information Memorandum, including all of the basic documents, and update it regularly.
- Contact legal, financial, & accounting advisors to let them know what's going on and that you're counting on their full and timely support
- Stay focused on your primary goal which should be: Getting the Deal Done, and make certain that all parties keep their egos in check

If you know of a business owner who's thinking of selling or buying a business and who might benefit from a free consultation with us, have them contact me, or any of the M&A professionals at [www.bradwaygroup.com](http://www.bradwaygroup.com)

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## Frequently Asked Questions...



**Q: I operate my entity as a general partnership. For tax purposes am I self-employed or can I consider myself an employee?**

**A: Operating as a general partnership, you are considered to be self-employed. As such, schedule SE must be filled out with form 1040. Other forms of business, such as S Corporations, C Corporations, etc., offer the owners a chance to be an employee and earn a wage. Further, S and C Corporations offer owners a chance to limit their liability in terms of contract and tort damages.**

**Q: I recently formed an LLC and I employ no employees. Does my LLC need a separate tax number?**

**A: No, you do not need a separate federal ID number. If you decide to employ employees in the future, you must have a federal ID number once those employees become employees.**

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