FEATURES OF THE PENSION PROTECTION ACT OF 2006 ("PPA") – REVISITED

PPA - SOMETHING FOR EVERYONE IN 401(K)

This year marks the 10th anniversary of the Pension Protection Act of 2006 ("PPA"), which is described as "the most sweeping reform of America's pension laws in over 30 years". Although PPA earns high marks for its contribution to a uniform and relatively straightforward approach to pension plan funding methodology and actuarial assumptions, the highest kudos must be awarded to PPA's provisions that paved the way for greater automatic enrollment in 401(k) plans. Once thought of as a secondary retirement plan to an employer's defined benefit pension plan, 401(k) plans have grown exponentially during the same time as the decline and elimination of many defined benefit pension plans. As a result, the 401(k) plan rapidly became the primary and, in many cases, the only employee benefit plan for retirement security.

The typical 401(k) plan in 2006 was strictly a "do-it-yourself" sort of retirement program. Participation was strictly voluntary and participants were free to determine how much, if any, of their compensation they would contribute to the 401(k) plan. While Roth IRAs had been around since the 1990s, there was no law giving 401(k) plan participants the opportunity to designate contributions to an account taxed like a Roth IRA. **PPA included a provision allowing 401(k) plans to be designed to accept either "traditional" before-tax contributions or "Roth Account" after-tax contributions where investment results can accumulate tax free.**

Most 401(k) plans require participants to determine how much to contribute to the plan and when, if ever, to change the size of the contribution. If Roth Accounts are maintained, the participant must determine how much of his or her contribution will be treated as Roth after-tax vs. pre-tax deferred contributions. Finally, most plans require the participant to determine how this money is invested within the plan. This contrasts sharply with defined benefit plans where participants automatically became eligible to accrue benefits. Before PPA, some 401(k) plans experimented with "automatic enrollment plans," but a number of issues discouraged the expansion of the auto-enrollment movement. Some state laws prohibited an employer from deducting sums from a paycheck unless the employee specifically authorized it. In addition, automatic enrollment plans had to resolve the question as to how money automatically taken from a paycheck is invested and whether the employer was assuming liability by making investment decisions for nonresponsive employees.

PPA contained provisions that solved the "unauthorized payroll deduction" and the "unauthorized investment decision" problems. It also **created incentives for employers to adopt one of two automatic enrollment plans** authorized by the PPA: the Eligible Automatic Contribution Arrangement ("**EACA**") and the Qualified Automatic Contribution Arrangement ("**QACA**"), both of which generally must be added at the beginning of the Plan year, with a notice to employees issued 30 days *prior* to the beginning of the plan year.

EACAs, for example, permit the plan to contain a provision that permits an automatically enrolled employee to rescind the action within 90 days. It also extends the 2½ month period for correcting any plan non-discrimination failures to 6 months.

QACAs have similar provisions, but also have automatic escalators that boost the initial contribution rate (with the minimum contribution being 3%) up 1% per year until the rate reaches at least 6%. Annual employee notices are required for these plans.

<u>By the Numbers: PPA Really Worked</u>

The Callan 2016 Defined Contribution Trends statistics below demonstrate the dramatic increase in automatic enrollment plans after PPA was adopted in 2006.

	2006/2007	**Current**
Plans using automatic enrollment	35%	61%
Plans using automatic increases in contribution rates	26%	46%

Automatic enrollment has increased typical participation rates from the 60%-70% range to the 80%-90% range. Since the great majority of automatically enrolled employees are relatively lower paid, increased participation translates to better non-discrimination testing results. This in turn results in more tests passing or if not passing either lower refunds to Highly Compensated Employees (generally employees earning under $120,000 in 2016) or lower required employer contributions to Non-Highly Compensated Employees.

In short, **automatic enrollment encourages employees to contribute to a 401(k) plan by automatically answering questions concerning the amount, type, and investment of 401(k) contributions and by reversing the result of inaction from non-participation to participation.** This benefits the auto-enrolled participant by creating or increasing a retirement nest egg and may also result in the contribution of employer matching contributions. Automatic enrollment benefits Highly Compensated Employees by reducing or eliminating refunds due to non-discrimination requirements. It benefits employers by reducing or eliminating special employer plan contributions needed to pass non-discrimination requirements while avoiding making contribution refunds to Highly Compensated Employees. Finally, automatic enrollment is good for America because it enhances the value of the American workers' 401(k) retirement plan.

REMINDERS FOR JUNE

June 15 – Minimum funding requirements for defined benefit, money purchase, and target benefit plan years ended 9/30/15 must be met by June 15 in order to avoid excise taxes. An electronic transfer must be completed or a check mailed by this date.

June 15 – Forms 5500 Series/8955-SSA – Forms that are on extension are due for the Plan Year ended 8/31/15.

June 15 – Retirement plan employer contributions are due in order to be **deducted** on employer tax returns due to be filed June 15, 2016.

June 30 – Forms 5500 Series/8955-SSA – Forms are due for the Plan Year ended 11/30/15 that are not on extension.

For more information or to request a proposal, please visit our website at www.NRServices.com, or for sales support, please contact:

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