

TAX UPDATE - August 2006

To Our Clients, Business Partners and Friends...

We hope this letter finds you and your business doing well and that you are enjoying another fine, Midwestern summer. Before taking their summer recess, Congress finally got something done by passing the Pension Protection Act of 2006 (PPA). In addition to many important qualified plan changes, there are some nonqualified deferred compensation provisions in PPA:

1. **Corporate Owned Life Insurance** rules (the industry “best practices” we have mentioned before) were adopted. These rules will require informed consent of insureds (our clients already do this); will restrict COLI purchases to the lives of highly-compensated employees (or HCEs) [again, our clients already comply]; and will require some ongoing disclosure and recordkeeping of a companies COLI policies (we will provide all of the required information to our clients).
2. **Nonqualified plan funding restrictions** for companies with under-funded qualified pension plans have also been adopted. This will affect only those companies offering defined benefit pension plans and only if those plans are inadequately funded. More clarity on these rules will be forthcoming from Treasury.
3. **Major qualified plan rule changes** include: “automatic enrollment” features in 401(k) plans that may help with discrimination testing – thus allowing HCEs to contribute more to the 401(k); and the 2001 Tax Act increases on allowable contributions to 401(k) plans, etc., have been made permanent (they were due to expire in 2010).

The President is expected to sign the bill into law on August 17, 2006 – and we will keep you apprised of more developments regarding regulations, effective dates, etc. Many provisions are expected to apply to policies/plans established after the date of enactment.

Plan Amendment / Documentation under §409A

As previously reported, the requirement for plan amendments is still officially December 31, 2006 – assuming those plans are being operated in good faith under the proposed regulations.

We continue to recommend that plans in effect prior to January 1, 2005, NOT be amended until more guidance is received. It could be Fall before the next round of guidance is received from the Treasury / IRS.

Further, rumors from Treasury (fed by various presentations made by Treasury staffers this summer) lead us to believe that the 12/31/2006 compliance deadline will shift into 2007 – because there won’t be enough time for plan sponsors to comply between the issuance of the final regulations and the end of the year. If you have questions about whether or not your specific plan needs to be amended and when is the right time to do so, please contact us.

Thank you for the chance to be of service. Let us know if we can provide you with additional information related to the topics discussed above, or in the general area of management compensation and benefits.

