Employee Benefits Law Action Memo

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Electronic Dispatch

Go to BS&K Employee Benefits Home Page

COST-OF-LIVING ADJUSTMENTS FOR 2006 ANNOUNCED

The Internal Revenue Service recently announced the annual cost-of-living adjustments for various dollar limits applicable to contributions and benefits under qualified retirement plans. The dollar limits for 2006 are as follows:

	2005	2006
Maximum basic employee elective deferral to 401(k) plans and tax-sheltered annuity plans	$ 14,000	$ 15,000
General "catch-up" contribution limit for 401(k) and 403(b) plan participants age 50 and over	$ 4,000	$ 5,000
Maximum annual allocation (contributions plus forfeitures) under defined contribution plans	$ 42,000[1]	$ 44,000[1]
457(e)(15) basic deferral limit for eligible deferred compensation plans of state and local governments and tax-exempt organizations	$ 14,000	$ 15,000
Maximum annual benefit under defined benefit plans	$ 170,000[2]	$ 175,000[2]
Compensation cap for deduction, benefit and allocation purposes	$ 210,000	$ 220,000
Compensation threshold for highly compensated employee definition	$ 95,000[3]	$ 100,000[3]
Compensation threshold for simplified employee pension plan participation	$ 450	$ 450
Social Security taxable wage base	$ 90,000	$ 94,200

[1] In no event may a participant's annual allocation exceed 100% of the participant's compensation.

[2] In no event may a participant's annual benefit exceed 100% of the participant's average compensation for the participant's high three years.

[3] See explanation on reverse side.

An employee is considered "highly compensated" if the employee:

(a) was a five-percent owner of the employer at any time during the current or preceding year; or

(b) received compensation from the employer in the preceding year of more than the applicable dollar limit for that year.

In a calendar year plan, an employee will be considered highly compensated for 2006, if the employee's compensation for 2005 was greater than $95,000. As an alternative to (b), an employer may elect to consider as "highly compensated" only those employees who received compensation in excess of the applicable dollar limit in the preceding year and who also were in the top 20 percent of employees when all employees are ranked on the basis of compensation. Once this election is made, it applies for all subsequent determination years unless changed by the employer. The definition of the term "highly compensated employee" in the plan must reflect the change, and this definition generally must apply to all of the employer's qualified retirement plans.

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