

109<sup>TH</sup> CONGRESS  
1<sup>ST</sup> SESSION

# S. 1590

To amend the Internal Revenue Code of 1986 to increase participation and savings in cash or deferred plans through automatic contribution and default investment arrangements, and for other purposes.

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## IN THE SENATE OF THE UNITED STATES

JULY 29, 2005

Mr. BAYH introduced the following bill; which was read twice and referred to the Committee on Finance

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## A BILL

To amend the Internal Revenue Code of 1986 to increase participation and savings in cash or deferred plans through automatic contribution and default investment arrangements, and for other purposes.

1 *Be it enacted by the Senate and House of Representa-*  
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the “Making Savings Auto-  
5 matic Act of 2005”.

1 **SEC. 2. INCREASING PARTICIPATION AND SAVINGS IN**  
 2 **CASH OR DEFERRED PLANS THROUGH AUTO-**  
 3 **MATIC CONTRIBUTION ARRANGEMENTS.**

4 (a) **AUTOMATIC CONTRIBUTION ARRANGEMENTS RE-**  
 5 **QUIRED FOR SECTION 401(k) SAFE HARBOR.**—Section  
 6 401(k)(12)(A) of the Internal Revenue Code of 1986 (re-  
 7 lating to alternative methods of meeting nondiscrimination  
 8 requirements) is amended by striking “and” at the end  
 9 of clause (i), by striking the period at the end of clause  
 10 (ii), and by adding at the end the following new clause:

11 “(iii) constitutes an automatic con-  
 12 tribution trust under paragraph (13).”.

13 (b) **AUTOMATIC CONTRIBUTION TRUST.**—Section  
 14 401(k) of the Internal Revenue Code of 1986 (relating to  
 15 cash or deferred arrangement) is amended by adding at  
 16 the end the following new paragraph:

17 “(13) **AUTOMATIC CONTRIBUTION TRUST.**—

18 “(A) **AUTOMATIC CONTRIBUTION TRUST**  
 19 **DEFINED.**—

20 “(i) **IN GENERAL.**—For purposes of  
 21 paragraph (12)(A)(iii), the term ‘automatic  
 22 contribution trust’ means an arrange-  
 23 ment—

24 “(I) except as provided in clause  
 25 (ii), under which each employee eligi-  
 26 ble to participate in the arrangement

1 is treated as having elected to have  
2 the employer make elective contribu-  
3 tions in an amount equal to the appli-  
4 cable percentage of the employee's  
5 compensation, and

6 “(II) which meets the require-  
7 ments of subparagraph (B).

8 “(ii) EXCEPTIONS.—

9 “(I) EXCEPTION FOR EXISTING  
10 EMPLOYEES.—Clause (i)(I) shall not  
11 apply to any employee who was eligi-  
12 ble to participate in the arrangement  
13 (or a predecessor arrangement) imme-  
14 diately before the first date on which  
15 the arrangement is an automatic con-  
16 tribution trust.

17 “(II) ELECTION OUT.—Each em-  
18 ployee eligible to participate in the ar-  
19 rangement may specifically elect not  
20 to have contributions made under  
21 clause (i), and such clause shall cease  
22 to apply to compensation paid on or  
23 after the effective date of the election.

24 “(iii) APPLICABLE PERCENTAGE.—

25 For purposes of this subparagraph—

1           “(I) IN GENERAL.—The term  
2           ‘applicable percentage’ means, with  
3           respect to any employee, the percent-  
4           age (not less than 3 percent) deter-  
5           mined under the arrangement.

6           “(II) INCREASE IN PERCENT-  
7           AGE.—In the case of the second plan  
8           year beginning after the first date on  
9           which the election under clause (i)(I)  
10          is in effect with respect to the em-  
11          ployee and any succeeding plan year,  
12          the applicable percentage shall be a  
13          percentage equal to the sum of the  
14          applicable percentage for the employee  
15          as of the close of the preceding plan  
16          year plus the number of percentage  
17          points (not less than 1 percentage  
18          point) specified by the plan. Such in-  
19          crease shall continue until the applica-  
20          ble percentage is at least 10 percent  
21          or such higher percentage specified by  
22          the plan.

23          “(B) NOTICE REQUIREMENTS.—

1           “(i) IN GENERAL.—The requirements  
2 of this subparagraph are met if the re-  
3 quirements of clauses (ii) and (iii) are met.

4           “(ii) REASONABLE PERIOD TO MAKE  
5 ELECTION.—The requirements of this  
6 clause are met if each employee to whom  
7 subparagraph (A)(i) applies—

8                   “(I) receives a notice explaining  
9 the employee’s right under the ar-  
10 rangement to elect not to have elective  
11 contributions made on the employee’s  
12 behalf, and how contributions made  
13 under the arrangement will be in-  
14 vested in the absence of any invest-  
15 ment election by the employee, and

16                   “(II) has a reasonable period of  
17 time after receipt of such notice and  
18 before the first elective contribution is  
19 made to make such election.

20           “(iii) ANNUAL NOTICE OF RIGHTS  
21 AND OBLIGATIONS.—The requirements of  
22 this clause are met if each employee eligi-  
23 ble to participate in the arrangement is,  
24 within a reasonable period before any year,

1           given notice of the employee’s rights and  
2           obligations under the arrangement.

3           The requirements of clauses (i) and (ii) of para-  
4           graph (12)(D) shall be met with respect to the  
5           notices described in clauses (ii) and (iii) of this  
6           subparagraph.”

7           (c)       MATCHING       CONTRIBUTIONS.—Section  
8   401(m)(11)(A) of the Internal Revenue Code of 1986 (re-  
9   lating to additional alternative method of satisfying non-  
10   discrimination test for matching contributions and em-  
11   ployee contributions) is amended by striking “and” at the  
12   end of clause (ii), by striking the period at the end of  
13   clause (iii) and inserting “, and” and by adding at the  
14   end the following new clause:

15                           “(iii) meets the requirements of sub-  
16                           section (k)(12)(A)(iii).”.

17           (d) INVESTMENTS AND PREEMPTION.—

18                   (1) CONTROL DEEMED TO HAVE BEEN EXER-  
19                   CISED WITH RESPECT TO DEFAULT INVESTMENT AR-  
20                   RANGEMENTS.—Section 404(c) of the Employee Re-  
21                   tirement Income Security Act of 1974 (29 U.S.C.  
22                   1104(c)) is amended by adding at the end the fol-  
23                   lowing new paragraph:

24                           “(4) TREATMENT OF DEFAULT INVESTMENT  
25                           ARRANGEMENT.—

1           “(A) IN GENERAL.—A participant in an  
2 individual account plan shall, for purposes of  
3 paragraph (1), be treated as exercising control  
4 over the assets in the account with respect to  
5 the amount of contributions made under a de-  
6 fault investment arrangement.

7           “(B) DEFAULT INVESTMENT ARRANGE-  
8 MENT DEFINED.—For purposes of this para-  
9 graph, the term ‘default investment arrange-  
10 ment’ means an arrangement—

11                   “(i) which meets the requirements of  
12 subparagraph (C),

13                   “(ii) under which the participant is  
14 treated as having elected to have the em-  
15 ployer exercise control over the assets in  
16 his account until the participant specifi-  
17 cally elects to exercise such control, and

18                   “(iii) under which assets described in  
19 clause (ii) are invested in accordance with  
20 regulations prescribed by the Secretary.

21 Such regulations shall provide guidance on the  
22 appropriateness of designating default invest-  
23 ments that include a mix of asset classes con-  
24 sistent with long-term capital appreciation. The  
25 regulations shall also provide guidance on the

1 designation of default investments in individual  
2 account plans that are not designed to meet the  
3 requirements of this section.

4 “(C) NOTICE REQUIREMENTS.—

5 “(i) TIME FOR NOTICE.—The admin-  
6 istrator of a default investment arrange-  
7 ment shall, within a reasonable period be-  
8 fore each plan year, give to each employee  
9 to whom a default investment arrangement  
10 applies for such plan year notice of the em-  
11 ployee’s rights and obligations under the  
12 arrangement which—

13 “(I) is sufficiently accurate and  
14 comprehensive to apprise the employee  
15 of such rights and obligations, and

16 “(II) is written in a manner cal-  
17 culated to be understood by the aver-  
18 age employee to whom the arrange-  
19 ment applies.

20 “(ii) FORM OF NOTICE; RESPONSE.—  
21 A notice shall not be treated as meeting  
22 the requirements of clause (i) with respect  
23 to an employee unless—

24 “(I) the notice includes a notice  
25 explaining the employee’s right under

1 the arrangement to elect to exercise  
2 control over the assets in his account,

3 “(II) the employee has a reason-  
4 able period of time after receipt of the  
5 notice described in subclause (I) and  
6 before the assets are first invested to  
7 make such election, and

8 “(III) the notice explains how  
9 contributions made under the ar-  
10 rangement will be invested in the ab-  
11 sence of any investment election by  
12 the employee.”.

13 (2) PREEMPTION OF CONFLICTING STATE REG-  
14 ULATION.—Section 514 of such Act (29 U.S.C.  
15 1144) is amended by adding at the end the following  
16 new subsection:

17 “(e) AUTOMATIC CONTRIBUTION ARRANGEMENTS.—

18 “(1) IN GENERAL.—Notwithstanding any other  
19 provision of this section, any law of a State which  
20 would directly or indirectly prohibit or restrict the  
21 inclusion in any plan of an automatic contribution  
22 arrangement shall be superseded. The Secretary may  
23 prescribe regulations which would establish min-  
24 imum standards that such arrangements would be

1 required to satisfy in order for this subsection to  
2 apply.

3 “(2) AUTOMATIC CONTRIBUTION ARRANGE-  
4 MENT DEFINED.—For purposes of this subsection,  
5 the term ‘automatic contribution arrangement’  
6 means an arrangement—

7 “(A) which meets the requirements of  
8 paragraph (3),

9 “(B) under which a participant may elect  
10 to have the employer make payments as con-  
11 tributions under the plan on behalf of the par-  
12 ticipant, or to the participant directly in cash,

13 “(C) under which the participant is treated  
14 as having elected to have the employer make  
15 such contributions in an amount equal to a uni-  
16 form percentage of compensation provided  
17 under the plan until the participant specifically  
18 elects not to have such contributions made (or  
19 specifically elects to have such contributions  
20 made at a different percentage), and

21 “(D) under which contributions described  
22 in subparagraph (C) are invested in accordance  
23 with regulations prescribed by the Secretary.

24 Such regulations shall provide guidance on the ap-  
25 propriateness of designating default investments

1 that include a mix of asset classes consistent with  
2 long-term capital appreciation.

3 “(3) NOTICE REQUIREMENT.—

4 “(A) IN GENERAL.—The administrator of  
5 an individual account plan shall, within a rea-  
6 sonable period before each plan year, give to  
7 each employee to whom an automatic contribu-  
8 tion arrangement applies for such plan year no-  
9 tice of the employee’s rights and obligations  
10 under the arrangement which—

11 “(i) is sufficiently accurate and com-  
12 prehensive to apprise the employee of such  
13 rights and obligations, and

14 “(ii) is written in a manner calculated  
15 to be understood by the average employee  
16 to whom the arrangement applies.

17 “(B) OTHER REQUIREMENTS.—A notice  
18 shall not be treated as meeting the require-  
19 ments of subparagraph (A) with respect to an  
20 employee unless—

21 “(i) the notice includes a notice ex-  
22 plaining the employee’s right under the ar-  
23 rangement to elect not to have elective con-  
24 tributions made on the employee’s behalf

1 (or to elect to have such contributions  
2 made at a different percentage),

3 “(ii) the employee has a reasonable  
4 period of time after receipt of the notice  
5 described in clause (i) and before the first  
6 elective contribution is made to make such  
7 election, and

8 “(iii) the notice explains how contribu-  
9 tions made under the arrangement will be  
10 invested in the absence of any investment  
11 election by the employee.”.

12 (e) CORRECTIVE DISTRIBUTIONS.—

13 (1) IN GENERAL.—Section 414 of the Internal  
14 Revenue Code of 1986 (relating to definitions and  
15 special rules) is amended by adding at the end the  
16 following new subsection:

17 “(w) AUTOMATIC CONTRIBUTION ARRANGEMENTS.—

18 “(1) IN GENERAL.—For purposes of this title,  
19 the amount of any corrective distribution from a  
20 plan shall be treated as if such amount had never  
21 been held in such plan and shall be treated as a pay-  
22 ment of compensation from the employer maintain-  
23 ing the plan to the employee receiving such distribu-  
24 tion.

1           “(2) CORRECTIVE DISTRIBUTION.—For pur-  
2           poses of this subsection, the term ‘corrective dis-  
3           tribution’ means a distribution from an applicable  
4           employer plan of all amounts attributable to an erro-  
5           neous automatic contribution.

6           “(3) ERRONEOUS AUTOMATIC CONTRIBU-  
7           TION.—For purposes of this subsection, the term  
8           ‘erroneous automatic contribution’ means an elective  
9           contribution made on behalf of an employee under  
10          any applicable employer plan pursuant to a plan pro-  
11          vision treating the employee as having elected to  
12          have the employer make such elective contribution  
13          until the employee affirmatively elects not to have  
14          such contribution made or affirmatively elects to  
15          make contributions at a specified level, if the fol-  
16          lowing requirements are satisfied:

17                 “(A) Within the applicable period, the em-  
18                 ployee notifies the plan administrator that the  
19                 employee elects to have the elective contribution  
20                 treated as an erroneous automatic contribution.

21                 “(B) The sum of the elective contributions  
22                 that are treated as erroneous automatic con-  
23                 tributions with respect to an employee does not  
24                 exceed the greater of—

25                         “(i) \$400, or

1           “(ii) the amount of the elective con-  
2           tributions described in paragraph (3) with  
3           respect to the employee which were made  
4           during the first 4 payroll periods to which  
5           the arrangement applies.

6           “(4) APPLICABLE EMPLOYER PLAN.—For pur-  
7           poses of this subsection, the term ‘applicable em-  
8           ployer plan’ has the meaning given such term by  
9           subsection (v)(6)(A).

10          “(5) APPLICABLE PERIOD.—For purposes of  
11          this subsection, the term ‘applicable period’ means,  
12          with respect to an employee, the 3-month period  
13          that begins on the first date that an amount is with-  
14          held from compensation payable to the employee in  
15          order to make a plan contribution pursuant to a  
16          plan provision described in paragraph (3).”.

17          (2) VESTING CONFORMING AMENDMENTS.—

18                (A) INTERNAL REVENUE CODE OF 1986.—

19                   (i) Section 411(a)(3)(G) of such Code  
20                   is amended by inserting “an erroneous  
21                   automatic contribution under section  
22                   414(w),” after “402(g)(2)(A),”.

23                   (ii) The heading of section  
24                   411(a)(3)(G) of such Code is amended by

1 inserting “OR ERRONEOUS AUTOMATIC  
2 CONTRIBUTION” before the period.

3 (iii) Section 401(k)(8)(E) of such  
4 Code is amended by inserting “an erro-  
5 neous automatic contribution under section  
6 414(w),” after “402(g)(2)(A),”.

7 (iv) The heading of section  
8 401(k)(8)(E) of such Code is amended by  
9 inserting “OR ERRONEOUS AUTOMATIC  
10 CONTRIBUTION” before the period.

11 (B) EMPLOYEE RETIREMENT INCOME SE-  
12 CURITY ACT OF 1974.—Section 203(a)(3)(F) of  
13 the Employee Retirement Income Security Act  
14 of 1974 (29 U.S.C. 1053(a)(3)(F)) is amended  
15 by inserting “an erroneous automatic contribu-  
16 tion under section 414(w) of such Code,” after  
17 “402(g)(2)(A) of such Code,”.

18 (f) APPLICATION OF AUTOMATIC CONTRIBUTION RE-  
19 QUIREMENT TO FEDERAL THRIFT SAVINGS PLAN.—Sec-  
20 tion 8432(a) of title 5, United States Code, is amended  
21 by adding at the end the following:

22 “(4)(A) An employee who begins employment  
23 after January 1, 2006, or any Member who is elect-  
24 ed or appointed to office after that date (regardless  
25 of whether that employee (or Member) has prior pe-

1       riods of service covered under this chapter or chap-  
2       ter 83) shall be treated as having made an election  
3       to make contributions under subsection (b) in an  
4       amount equal to the applicable percentage of the  
5       employees compensation unless the employee specifi-  
6       cally elects not to have such contributions made

7               “(B)(i) For purposes of this paragraph, the  
8       term ‘applicable percentage’ means, with respect to  
9       any employee, 3 percent.

10              “(ii) In the case of the second plan year begin-  
11       ning after the first date on which the election under  
12       subparagraph (A) is in effect with respect to the em-  
13       ployee and any succeeding plan year, the applicable  
14       percentage shall be a percentage equal to the sum of  
15       the applicable percentage for the employee as of the  
16       close of the preceding plan year plus the number of  
17       percentage points (not less than 1 percentage point)  
18       specified by the plan. Such increase shall continue  
19       until the applicable percentage is 10 percent.

20              “(C) Each employee to whom subparagraph (A)  
21       applies shall—

22                      “(i) receive a notice explaining the employ-  
23       ee’s right under the Thrift Savings Plan to  
24       elect not to have elective contributions made on  
25       the employee’s behalf, and how contributions

1           made under the Thrift Savings Plan will be in-  
2           vested in the absence of any investment election  
3           by the employee, and

4                   “(ii) have a reasonable period of time after  
5           receipt of such notice and before the first elec-  
6           tive contribution is made to make such election.

7           A similar notice shall be provided within a reason-  
8           able period of time before each calendar year.

9                   “(D) In the case of an employee who does not  
10          make an investment election, the Thrift Savings  
11          Plan shall invest the contributions in accordance  
12          with the regulations prescribed by the Secretary of  
13          Labor under section 404(c)(4)(B) of the Employee  
14          Retirement Income Security Act of 1974.”.

15          (g) EFFECTIVE DATE.—

16                   (1) IN GENERAL.—Except as provided in para-  
17          graph (2), the amendments made by this section  
18          shall apply to plan years beginning after December  
19          31, 2005.

20                   (2) REGULATIONS.—Final regulations under  
21          section 404(c)(4)(B)(iii) of the Employee Retirement  
22          Income Security Act of 1974 (added by this section)  
23          shall be issued no later than 6 months after the date  
24          of enactment of this Act.

1 **SEC. 3. DIRECT PAYMENT OF TAX REFUNDS TO INDIVIDUAL**  
2 **RETIREMENT PLANS.**

3 (a) IN GENERAL.—Paragraph (3) of section 219(f)  
4 of the Internal Revenue Code of 1986 is amended to read  
5 as follows:

6 “(3) TIME WHEN CONTRIBUTIONS MADE.—

7 “(A) IN GENERAL.—Except as provided in  
8 subparagraph (B), for purposes of this sub-  
9 section, a taxpayer shall be deemed to have  
10 made a contribution to an individual retirement  
11 plan on the last day of the preceding taxable  
12 year if the contribution is made on account of  
13 such taxable year and is made not later than  
14 the time prescribed by law for filing the return  
15 for such taxable year (not including extensions  
16 thereof).

17 “(B) DIRECT PAYMENT OF TAX REFUNDS  
18 TO INDIVIDUAL RETIREMENT PLANS.—

19 “(i) IN GENERAL.—To the extent pro-  
20 vided in rules prescribed by the Secretary,  
21 a tax refund owed to a taxpayer and paid  
22 directly to an individual retirement plan  
23 shall be deemed a contribution made by  
24 the taxpayer—

1                   “(I) on the last day of the tax-  
2                   able year to which such refund re-  
3                   lates, and

4                   “(II) on account of such taxable  
5                   year.

6                   “(ii) LIMITATION.—This subpara-  
7                   graph shall not apply to a tax refund un-  
8                   less such refund is shown on a return filed  
9                   not later than the time prescribed by law  
10                  for filing the return for the taxable year to  
11                  which such refund relates (not including  
12                  extensions thereof).

13                  “(iii) DIRECT PAYMENT.—For pur-  
14                  poses of this subparagraph, a tax refund is  
15                  paid directly to an individual retirement  
16                  plan if it is paid in the form of a direct  
17                  transfer from the Secretary to the trustee  
18                  or issuer of the individual retirement plan.

19                  “(iv) TAX REFUND.—For purposes of  
20                  this subparagraph, the term ‘tax refund’  
21                  means any overpayment of an internal rev-  
22                  enue tax under section 6401 which the  
23                  Secretary may credit or refund under sec-  
24                  tion 6402 (after application of subsections  
25                  (c), (d), and (e) thereof).”.

1 (b) REGULATIONS.—

2 (1) IN GENERAL.—Not later than 1 year after  
3 the date of enactment of this Act, the Secretary of  
4 the Treasury shall issue rules which permit a tax-  
5 payer—

6 (A) to elect to have all or any portion of  
7 a tax refund owed to the taxpayer paid directly  
8 to an individual retirement plan,

9 (B) to specify the individual retirement  
10 plan to which such tax refund is to be paid  
11 (and the investment option in which such tax  
12 refund is to be invested), and

13 (C) to the extent provided in rules pre-  
14 scribed by the Secretary, to specify the taxable  
15 year on account of which such payment is  
16 made, except that the Secretary may require  
17 that the amount subject to such an election ex-  
18 ceed a dollar threshold determined by the Sec-  
19 retary as necessary or appropriate to ensure the  
20 administrability of such elections.

21 (2) INFORMATION.—The Secretary may require  
22 that the taxpayer provide, and agree to the disclo-  
23 sure of, any information necessary to pay the tax re-  
24 fund to the individual retirement plan specified by  
25 the taxpayer.

1           (3) SPECIAL RULE.—The Secretary may pro-  
2           vide that if, for any reason, the trustee or issuer  
3           does not accept payment of a tax refund, the tax re-  
4           fund shall instead be paid as if the taxpayer had not  
5           elected a direct payment to an individual retirement  
6           plan.

7           (c) EFFECTIVE DATE.—The amendments made by  
8           this section shall apply to taxable years the due date for  
9           which (without regard to any extension) occurs after the  
10          date on which final rules implementing the amendments  
11          made by this section are prescribed.

12   **SEC. 4. CREDIT TO ENCOURAGE UNIVERSAL ACCESS TO**  
13                   **OPT OUT DIRECT DEPOSIT RETIREMENT SAV-**  
14                   **INGS.**

15          (a) IN GENERAL.—Subpart D of part IV of sub-  
16          chapter A of chapter 1 of the Internal Revenue Code of  
17          1986 (relating to business related credits) is amended by  
18          adding at the end the following new section:

19   **“SEC. 45J. EMPLOYER SALARY REDUCTION COSTS.**

20          “(a) GENERAL RULE.—For purposes of section 38,  
21          in the case of the first taxable year which includes the  
22          date that a qualified salary reduction arrangement of the  
23          eligible employer becomes effective, the employer salary re-  
24          duction cost credit determined under this section for such

1 taxable year is the amount determined under subsection  
2 (b).

3 “(b) AMOUNT OF CREDIT.—The amount of the credit  
4 determined under this section for any taxable year with  
5 respect to an eligible employer shall be equal to 50 percent  
6 of the costs paid or incurred by the taxpayer in estab-  
7 lishing the qualified salary reduction arrangement referred  
8 to in subsection (a).

9 “(c) ELIGIBLE EMPLOYER.—For purposes of this  
10 section, the term ‘eligible employer’ means, with respect  
11 to any calendar year in which the taxable year begins, an  
12 employer which maintains a qualified salary reduction ar-  
13 rangement meeting the requirements of subsection (d) and  
14 which did not maintain a qualified plan or arrangement  
15 (within the meaning of subsection (d)(8)) for the pre-  
16 ceding 2 calendar years.

17 “(d) EMPLOYEE ACCESS TO OPT OUT SALARY RE-  
18 DUCATION CONTRIBUTIONS TO INDIVIDUAL RETIREMENT  
19 PLANS.—

20 “(1) IN GENERAL.—Every employer which does  
21 not maintain a qualified plan or arrangement for a  
22 calendar year may provide a qualified salary reduc-  
23 tion arrangement for the calendar year.

24 “(2) QUALIFIED SALARY REDUCTION ARRANGE-  
25 MENT.—For purposes of this section, the term

1 ‘qualified salary reduction arrangement’ means a  
2 salary reduction arrangement which meets the re-  
3 quirements of paragraphs (4) and (5).

4 “(3) SALARY REDUCTION ARRANGEMENT.—For  
5 purposes of this section, the term ‘salary reduction  
6 arrangement’ means a written arrangement of an  
7 employer under which—

8 “(A) an employee eligible to participate in  
9 the arrangement may elect to—

10 “(i) contribute to an individual retire-  
11 ment plan established by or on behalf of  
12 the employee by having the employer make  
13 direct deposit payments to the plan by pay-  
14 roll deduction, or

15 “(ii) receive the amounts directly as  
16 cash compensation,

17 “(B) no other contributions may be made  
18 under the arrangement,

19 “(C) each employee eligible to participate  
20 in the arrangement is treated as having elected  
21 to have the employer make elective contribu-  
22 tions under subparagraph (A)(i) in an amount  
23 equal to the applicable percentage (within the  
24 meaning of section 401(k)(13)(A)(iii)) of the  
25 employee’s compensation unless the employee

1 specifically elects not to have such contributions  
2 made, and

3 “(D) there is established the methods by  
4 which contributions made under the arrange-  
5 ment will be invested in the absence of any in-  
6 vestment election by the employee.

7 “(4) PARTICIPATION REQUIREMENTS.—

8 “(A) IN GENERAL.—The requirements of  
9 this paragraph are met with respect to a salary  
10 reduction arrangement for a year only if, under  
11 the arrangement, all employees of the employer  
12 are eligible to make the election under para-  
13 graph (3)(A).

14 “(B) EXCLUDABLE EMPLOYEES.—An em-  
15 ployer may exclude from the requirement under  
16 paragraph (3) employees described in section  
17 410(b)(3) and any employee who has not com-  
18 pleted hours of service for the employer on a  
19 regular basis during a period of at least 30 con-  
20 secutive days during the calendar year.

21 “(5) ADMINISTRATIVE REQUIREMENTS.—The  
22 requirements of this paragraph are met with respect  
23 to any salary reduction arrangement if, under the  
24 arrangement—

1           “(A) the employer must make the pay-  
2           ments elected under paragraph (3)(A) or re-  
3           quired under paragraph (3)(C) not later than  
4           the close of the 30-day period following the last  
5           day of the month with respect to which the con-  
6           tributions are to be made, or, if later, the dead-  
7           line under applicable rules and regulations for  
8           the employer to deposit tax under section 3102  
9           for wages paid in that month,

10           “(B) an employee may elect to terminate  
11           participation in the arrangement at any time  
12           during the year, except that if an employee so  
13           terminates, the arrangement may provide that  
14           the employee may not elect to resume partici-  
15           pation until the beginning of the next year,

16           “(C) each employee eligible to participate  
17           may elect, during the 60-day period before the  
18           beginning of any year (and the 60-day period  
19           before the first day the employee is eligible to  
20           participate), to participate in the arrangement,  
21           or to modify the amounts subject to the ar-  
22           rangement, for such year, and

23           “(D) immediately before the period for  
24           which an election described in paragraph (3)(A)  
25           may be made, the employer provides a notice to

1           each employee of the employee’s opportunity to  
2           make the election and the maximum amount  
3           which may be contributed to an individual re-  
4           irement plan on an annual basis.

5           “(6) USE OF DESIGNATED FINANCIAL INSTITU-  
6           TION.—An employer shall not be treated as failing  
7           to satisfy the requirements of this subsection or any  
8           other provision of this title merely because the em-  
9           ployer makes all contributions (or all contributions  
10          on behalf of employees who do not specify an indi-  
11          vidual retirement plan, trustee, or issuer to receive  
12          the contributions) to individual retirement plans of  
13          a designated trustee or issuer. The preceding sen-  
14          tence shall not apply unless each participant is noti-  
15          fied in writing that the participant’s balance may be  
16          transferred without cost or penalty to another indi-  
17          vidual retirement plan in accordance with subsection  
18          (d)(3).

19          “(7) MODEL NOTICE.—The Secretary shall pro-  
20          vide a model notice, written in a manner calculated  
21          to be understandable to the average worker, that  
22          employers may use to satisfy the requirement of  
23          paragraphs (5)(D) and (6). Model notices shall be  
24          provided in English, in Spanish, and in any other  
25          language deemed appropriate by the Secretary.

1           “(8) QUALIFIED PLAN OR ARRANGEMENT.—For  
2 purposes of this section, an employer is treated as  
3 maintaining a qualified plan or arrangement for a  
4 calendar year if the employer maintains for such  
5 year a plan, contract, pension, or trust described in  
6 subparagraph (A) or (B) of section 219(g)(5) or an  
7 eligible deferred compensation plan (within the  
8 meaning of section 457(b)) with respect to which  
9 contributions are made, or benefits are accrued, for  
10 service in such year.

11           “(e) SALARY REDUCTION CONTRIBUTIONS TREATED  
12 LIKE OTHER CONTRIBUTIONS TO INDIVIDUAL RETIRE-  
13 MENT PLANS.—

14           “(1) TAX TREATMENT UNAFFECTED.—The fact  
15 that a contribution to an individual retirement plan  
16 is made on behalf of an employee under a qualified  
17 salary reduction arrangement instead of being made  
18 directly by the employee shall not affect the deduct-  
19 ibility or other income tax treatment of the contribu-  
20 tion or of other amounts under this title.

21           “(2) SALARY REDUCTION CONTRIBUTIONS  
22 TAKEN INTO ACCOUNT.—Any contribution made on  
23 behalf of an employee under a qualified salary reduc-  
24 tion arrangement shall be taken into account in ap-  
25 plying the limitations on contributions to individual

1 retirement plans and the other provisions of this  
 2 title applicable to individual retirement plans as if  
 3 the contribution had been made to the plan directly  
 4 by the employee.”.

5 (b) CREDIT ALLOWED AS PART OF GENERAL BUSI-  
 6 NESS CREDIT.—Section 38(b) of the Internal revenue  
 7 Code of 1986 (defining current year business credit) is  
 8 amended by striking “plus” at the end of paragraph (18),  
 9 by striking the period at the end of paragraph (19) and  
 10 inserting “, plus”, and by adding at the end the following  
 11 new paragraph:

12 “(20) in the case of an eligible employer (as de-  
 13 fined in section 45J(c)), the employer salary reduc-  
 14 tion cost credit determined under section 45J(a).”.

15 (c) TREATMENT AS DEFAULT INVESTMENT AR-  
 16 RANGEMENT.—Section 404(c)(4)(B) of the Employee Re-  
 17 tirement Income security Act of 1974, as added by section  
 18 2 of this Act, is amended by adding at the end the fol-  
 19 lowing new sentence: “For purposes of this subsection, an  
 20 arrangement described in section 45J(d) shall be treated  
 21 as a default investment arrangement.”

22 (d) CLERICAL AMENDMENT.—The table of sections  
 23 for subpart D of part IV of subchapter A of chapter 1  
 24 of the Internal Revenue Code of 1986 is amended by add-  
 25 ing at the end the following new item:

“Sec. 45J. Employer salary reduction costs.”.

1       (e) EFFECTIVE DATE.—The amendments made by  
2 this section shall apply to taxable years beginning after  
3 December 31, 2005.

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