



Plan Sponsor Digest

Issue 4, 2018

Your Challenge, Our Solutions™

How to locate missing participants

In 2004, the Department of Labor (DOL) issued guidance (FAB 2004-02) on locating missing participants in terminating defined contribution (DC) plans. One of the steps called for using a federal letter-forwarding program. At the time, both the IRS and the Social Security Administration offered letter-forwarding services, but those programs have since been discontinued.

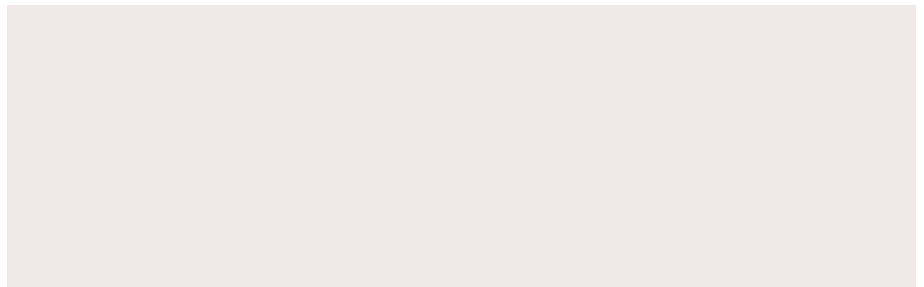
The DOL issued guidance (FAB 2014-01) on locating missing participants of terminating DC plans. This article is a discussion of the guidance.

Search steps

When a retirement plan is terminated, a plan administrator must generally distribute all plan assets within one year of the plan's termination date. Prior to making distributions, the plan administrator must contact plan participants (and beneficiaries) to explain the process involved in distributing their account balances. The DOL provides a model notice at www.law.cornell.edu/cfr/text/29/2550.404a-3.

Administrators often have difficulty locating some former employees. Under FAB 2014-01, the required steps for locating missing participants are to:

1. Use certified mail. This is an easy and often inexpensive way to determine if a participant can be located.
2. Check related plan and employer records. Other employer plans, such as a group health plan, may have more up-to-date information. If there are privacy concerns, a fiduciary can simply ask a provider to forward a letter to the missing participant.
3. Check beneficiary records. Contact the individuals the missing participant named on his or her beneficiary form to obtain updated contact information.





4. Use free electronic search tools. This step replaces the letter-forwarding requirement. Plan fiduciaries must make reasonable use of free Internet search tools, such as search engines, public record databases (e.g., those with licenses, mortgages, and real estate taxes), obituaries, and social media.

Additional search methods

Other search methods may involve using credit reporting agencies, investigation databases, and commercial locator services. However, fiduciaries must consider the size of a participant's account balance and the cost of additional search methods. A plan fiduciary is permitted to charge a missing participant's account reasonable expenses related to efforts to locate the participant (consistent with the terms of the plan).

Next steps for plan fiduciaries

If a participant cannot be located, the plan fiduciary is responsible for deciding where to put the missing participant's assets and is charged with choosing the most prudent investment vehicle. Section

404(a) of ERISA requires plan fiduciaries to consider individual retirement accounts or individual retirement annuities that preserve assets for retirement.

IRA safe harbor. A regulation published by the DOL in 2006 (Section 2550.404a-3) included a fiduciary safe harbor covering participant distributions from a terminated DC plan for assets moved into an IRA. The safe harbor requires that the plan fiduciary ensure the investment product is designed to preserve principal and that fees and expenses are not excessive.

Other distribution options. If a fiduciary is unable to find a provider that will accept a rollover distribution (which is very unlikely) or determines that a rollover distribution is not appropriate based on facts and circumstances, there are two additional options:

- Open an interest-bearing, federally insured bank account in the name of the missing participant, or
- Transfer the assets to a state unclaimed property fund, subject to the applicable state's escheat laws.

However, these options subject the participant's assets to tax, withholding, and possibly a 10% early distribution tax. By choosing one, a fiduciary might well be violating ERISA's prudence and loyalty requirements. The DOL has confirmed that another alternative, a distribution of 100% income tax withholding (essentially transferring the account balance to the IRS), is not an acceptable way to distribute a missing participant's benefits.

CIP issues

Fiduciaries may have concerns about legal issues that might prevent them from establishing IRAs or bank accounts for missing participants. The DOL states that banks and other financial institutions will not be required to comply with customer identification and verification provisions (CIP) when an employee benefit plan establishes an account and transfers the funds for the missing participant. CIP programs will apply when a former participant or beneficiary first contacts the institution.

FAQs about low balance accounts

Work force reductions over the past couple of years have left some employers with a lot of low-balance plan accounts owned by former employees. These accounts can be expensive to maintain and burdensome to administer. Below, you will find answers to commonly asked questions about handling these small accounts.

Can we just distribute small accounts to the former employees?

Check your plan's provisions. Under federal law, plans can provide that, if a former employee has not made an affirmative election to receive a distribution of his or her account assets or to roll those assets over to an IRA or another employer's plan, the plan can distribute the account – as long as its balance does not exceed \$5,000. For accounts valued at \$1,000 or less, the plan can simply send the former employee a check for his or her balance. Distributions of more than \$1,000 must be directly transferred to an IRA set up for the former employee. Accounts valued at \$1,000 or less may also be rolled over for administrative convenience.

Should nonvested assets be included when determining whether a mandatory distribution can be made?

You only have to include the value of the former employee's nonforfeitable accrued benefit. If the employee was not fully vested in any portion of the account when he or she left your employ, you do not have to count the nonvested portion.

What about rollovers?

A plan may provide that any amounts that a former employee rolled over from another employer's plan (and any earnings on those rolled over assets) are to be disregarded in determining the employee's nonforfeitable accrued benefit. Thus, you may be able to cash out and roll over accounts greater than \$5,000. Note that rolled over amounts are

included in determining whether a former employee's accrued benefit is greater than \$1,000 for purposes of the automatic rollover requirement.

What requirements do we have to meet when rolling over a small account?

To fulfill your fiduciary duties as a plan sponsor, the following requirements must be met:

- The rollover must be a direct transfer to an IRA set up in the former employee's name.
- The IRA provider must be a state or federally regulated financial institution, such as an FDIC-insured bank or savings association or an FCUA-insured credit union; an insurance company whose products are protected by a state guaranty association; or a mutual fund company.
- You must have a written agreement with the IRA provider that addresses appropriate account investments and fees.
- The IRA provider cannot charge higher fees than would be charged for a comparable rollover IRA

(Other fiduciary responsibilities apply.)

Are there rules for investing the rollover IRA?

The investments chosen for the IRA must be designed to preserve principal and provide a reasonable rate of return and liquidity. Examples include money market mutual funds, interest-bearing savings accounts, certificates of deposit, and stable value products.



Do we have to provide disclosures?

Yes. Before you cash out an account, you must notify the former employee in writing, either separately or as part of a rollover notice, that, unless the employee makes an affirmative election to receive a distribution of his or her account assets or rolls them over to another account, the distribution will be paid to an IRA. As long as you send the notice to the former employee's last known mailing address, the notice requirement generally will be considered satisfied. In addition, you must include a description of the plan's automatic rollover provisions for mandatory distributions in the plan's summary plan description (SPD) or summary of material modifications (SMM).