WRMarketplace

An AALU Washington Report

Thursday, September 11 2014 **WRM# 14-36**

The *WRMarketplace* is created exclusively for AALU Members by the AALU staff and Greenberg Traurig, one of the nation's leading tax and wealth management law firms. The *WRMarketplace* provides deep insight into trends and events impacting the use of life insurance products, including key take-aways, for AALU members, clients and advisors.

TOPIC: Department of Labor (DOL) Issues Updated Guidance for Dealing with Accounts of Missing Participants Under Terminated Defined Contribution Plans.

MARKET TREND: The prevalence of Internet-based search technologies has impacted the requirements for how plan fiduciaries may discharge their fiduciary duties when attempting to locate missing retirement plan participants and beneficiaries. Employers needing to terminate ERISA-governed defined contribution retirement plans will need to pay attention to new DOL guidelines that have been updated to reflect recent technological advances.

SYNOPSIS: The effective termination of a defined contribution plan requires the plan fiduciary to timely distribute ALL plan assets, which can be complicated if certain participants cannot be located. Due to changes in available search vehicles and Internet-based search tools, the DOL has updated its guidance on discharging fiduciary responsibilities to participants who cannot be located upon termination and distribution of such a plan. This guidance requires a thorough search utilizing all available avenues – including various Internet-based resources – for which no charge is assessed (although some cases may require paid search services). If the missing participant cannot be located, the plan fiduciary should prudently select an IRA provider (preferably following DOL safe harbors) to receive the distribution of the missing participant's account balance. As a last resort only, the plan fiduciary can distribute the account balance to a bank account in the participant's name or to a state unclaimed property fund. Under no circumstances should the fiduciary treat the full amount of the participant's account balance as having been withheld for income tax purposes.

TAKE AWAYS: Advisors to plan fiduciaries of terminated defined contribution plans should understand the updated DOL procedures for dealing with missing participants so that they can assist the fiduciaries in closing out their plans in a compliant manner. Although the guidance deals only with terminated defined contribution plans, arguably it articulates sound fiduciary practices that can be used in dealing with accounts held under active plans, though this approach should be taken only if a distribution from an active plan absolutely has to be made.

MAJOR REFERENCES: ***DOL Field Assistance Bulletin 2014-01.***

Last month, the DOL issued updated guidance to assist fiduciaries of terminated defined contribution plans in discharging their duties to act prudently in attempting to locate lost, missing or unresponsive participants (collectively, "**missing participants**") for purposes of making distributions of their account balances from those plans. This updated guidance, Field Assistance Bulletin ("**FAB**") 2014-01, reflects that previously recommended methods for locating lost participants – *i.e.*, use of the letter-forwarding services of the IRS or the Social Security Administration – have been discontinued, and that the search capabilities of the Internet have proliferated.

DEALING WITH MISSING PARTICIPANTS

The FAB makes clear that, while a plan sponsor's decision to terminate a retirement plan is not a fiduciary decision, once that decision is made, fiduciary duties arise to ensure that the decision is implemented prudently and solely in the interests of plan participants. A major part of this duty is ensuring that all participants are given ample opportunity to consent to and receive the distributions from the plan to which they are entitled.

First Step – Search Diligently using Specified Methodologies

The FAB provides that, to avoid violating its duties of prudence and loyalty, a plan fiduciary must take **all reasonable steps** to ensure that it has located a lost participant. **Four search methodologies** are specified, **each of which must be taken** before an unproductive search will be considered to satisfy all fiduciary responsibilities.

1. ***Use Certified Mail.*** The simplest method is to send a letter to the missing participant using certified mail. The DOL has provided a model notice that can be used for these mailings, but other notices can be sufficient.

2. ***Check Related Plan and Employer Records.*** Potentially, the employer's records or those of another employer-maintained benefits plan (such as a group health plan) may contain more current contact information for a participant than the terminating plan. The FAB provides that the fiduciary of the terminated plan must check with the employer and the administrator of the other plan and ask them to check their records for a more up-to-date address for the missing participant. If there are privacy concerns in making or responding to such a request, the fiduciary of the terminated plan can ask the other party to contact or forward a letter to the missing participant to ask the participant to contact the fiduciary of the terminated plan.

3. ***Check with Designated Plan Beneficiary.*** Similarly, the plan may have more accurate records concerning the participant's designated beneficiary than it does for the participant. Accordingly, the FAB directs that the plan fiduciary try to identify and contact any individual that the missing participant has designated as a beneficiary (such as a spouse or children) to attempt to find updated contact information for the participant. Again, if there are privacy concerns, the fiduciary can request that the designated beneficiary contact or forward a letter to the missing participant.

4. ***Use Free Electronic Search Tools.*** The final step set forth in the FAB requires the plan fiduciary to make reasonable use of Internet search tools *that do not charge a fee* to search for a missing participant. Examples include Internet search engines, public record databases, obituaries and social media.

Additional Searches May Be Required. While use of the above search methodologies may be sufficient to discharge a fiduciary's duty in many cases, the FAB points out that a plan fiduciary should consider factors such as the size of a participant's account balance and the cost of further search efforts to determine if additional steps are required. Where appropriate, a plan fiduciary may be obligated to take such further actions as using Internet search tools, commercial locator services, credit reporting agencies, information brokers, investigation databases and analogous services that may involve charges. These charges can, however, be passed on to the participant.

Next Step – Distribute Plan Account

A plan fiduciary may be required to distribute a participant's plan account, even when the participant cannot be located. The FAB describes methods for distributing accounts that may be used – as well as one that cannot be used.

Preferred Method – Individual Retirement Plan Rollovers. If the missing participant cannot be located, the optimal next step is to distribute his or her account balance into an individual retirement plan (e.g., an IRA), which avoids immediate taxation of the distribution and allows the amounts to continue to accumulate, tax-free, while in the IRA. The FAB notes that the **selection of an IRA provider is also a fiduciary function**. The DOL, however, has previously published safe harbor rules for selecting an IRA to receive mandatory plan distributions. Using these safe harbors will ensure that the plan fiduciary has properly discharged its duties in the distribution of benefits, the selection of the IRA provider, and the investment of the distributed funds.

Alternative Distribution Methods. If a plan fiduciary determines not to follow the IRA route or cannot find an IRA provider that will accept the proposed distribution, the FAB describes two other acceptable distribution alternatives: (1) opening an interest-bearing federally insured bank account in the name of the missing participant; and (2) transferring the account balance to a state unclaimed property fund. To use either of these approaches, however, the plan fiduciary must conclude that the particular approach is appropriate despite the potential adverse tax consequences. Unlike with an IRA, a distribution to a bank account or state unclaimed property fund results in current taxation to the participant of the distribution (plus a 10% early distribution penalty if the participant is younger than 59½), plus current taxation of earnings on the distributed amounts as they accrue. The FAB expresses an extremely dim view of these consequences and, therefore, these distribution methods should only be used as a last resort.

Unacceptable Distribution Option. In all circumstance, the DOL ***clearly*** disapproves of treating 100% of the distributable amount as being withheld to pay taxes on the distribution, with the idea that the participant, if ever found, might be able to claim a refund of the overpaid amounts. The participant may not ultimately be able to receive a refund, the amounts are not credited with earnings (other than the potential for a relatively nominal overpayment interest credit), and the participant may ultimately lose his retirement benefit totally.

TAKE-AWAYS

- When dealing with missing participants, plan fiduciaries that need to ensure distribution of all plan assets upon termination of a defined contribution plan:
  - Must undertake a thorough search utilizing all available avenues – including Internet-based resources – for which no charge is assessed (and, in some cases, use paid search services).

  - Should carefully select an IRA provider (preferably following DOL safe harbor rules) to which it can distribute a missing participant's account balance if the missing participant cannot be located.

  - Can, as a last resort only, distribute the account balance to an appropriate bank account in the name of the participant or to a state unclaimed property fund.

- The plan fiduciary cannot, under any circumstances, treat the full amount of the participant's account balance as having been withheld for income tax purposes.

- Advisors to plan fiduciaries of terminated defined contribution plans should understand these FAB procedures so that they can assist plan fiduciaries in closing out their plans in a compliant manner.

- Although the FAB deals only with terminated defined benefit plans, arguably it articulates sound fiduciary practices that can be used in dealing with accounts held under active plans, though this approach should only be taken if a distribution from an active plan absolutely has to be made.

Disclaimer

The AALU *WRNewswire* and *WRMarketplace* are published by the Association for Advanced Life Underwriting® as part of the Essential Wisdom Series, the trusted source of actionable technical and marketplace knowledge for AALU members—the nation's most advanced life insurance professionals.

WRM #14-36 was written by Greenberg Traurig, LLP
Jonathan M. Forster
Martin Kalb
Richard A. Sirus
Steven B. Lapidus
Rebecca Manicone

Counsel Emeritus
Gerald H. Sherman 1932-2012
Stuart Lewis 1945-2012