

DOL Updates Guidance on Terminated Plan Missing Participants

On August 14, 2014, the DOL issued new guidance on how fiduciaries of terminated defined contribution plans can fulfill their obligations under ERISA to try and locate missing participants/beneficiaries and distribute their account balances. This guidance removes the old requirement to use the IRS and SSA letter-forwarding services, which are no longer in existence, replacing it with one to use internet search tools. Otherwise, the guidance is much the same, namely that the preferred method of distributing assets is to open an individual retirement plan in the name of the missing participant or beneficiary.

Background

When terminating a defined contribution plan, all participants become immediately vested in their account balance and distribution of assets must occur as soon as administratively feasible. As part of the termination process, the plan administrator must notify and obtain direction from all participants (or their beneficiaries) about account balance distribution. However, participants may have moved, died, or may simply fail to respond to correspondence related to the plan termination. Where a plan administrator is unable to obtain direction about how to distribute assets, plan fiduciaries must decide how to handle distribution of these “missing participant” accounts.

The decision to terminate a plan is a settlor function; however the decision of how to distribute the terminating plan’s assets is a fiduciary one. Fiduciaries must act prudently and solely for the exclusive benefit of the participant or beneficiary when exercising that decision – or risk potential legal action.

Fiduciaries: Act Prudently

The choice of a distribution option for a missing participant is a fiduciary decision.

In 2004, the DOL issued [Field Assistance Bulletin \(FAB\) 2004-02](#), providing guidance for how to handle the missing participant scenario. The guidance required plan fiduciaries to conduct a reasonable search by using certified mail, examining related plan records, checking with the designated beneficiary or beneficiaries, and/or using IRS and Social Security Administration (SSA) letter forwarding services — which have since been discontinued (see our [September 13, 2012](#) and [April 21, 2014](#) *For Your Information* publications). If the search failed to find the participant or beneficiary, FAB 2004-02 said that the distribution should go into an individual retirement plan (i.e., an individual

retirement account or annuity — an IRA), if possible, to avoid immediate taxation and possible penalties. If the fiduciary is unable to locate an IRA provider willing to accept the rollover distribution, the account balance could be deposited in an interest-bearing savings account or escheated to state unclaimed property funds.

First Step — Search for Missing Participants

Under the new guidance in [FAB 2014-01](#), plan fiduciaries are advised to take the following actions in the course of trying to locate missing participants:

- **Contact participant using certified mail.** Easy to use, low cost, and will confirm if the participant is still at the last known address. The DOL [model notice](#) may be utilized in this mailing, but is not required.
- **Check related plan and employment records.** Even though the terminated plan may not contain current address records, other employer plans such as a medical plan may have more up-to-date contact information. Plan fiduciaries must ask the employer and related plans for information. If there is an issue of privacy, the fiduciary may ask the employer to forward the letter to the missing participant or beneficiary directing the participant to contact the plan fiduciary.
- **Check with designated plan beneficiary.** The plan fiduciary must try to contact any individual that the missing participant has named as a beneficiary — again with privacy issues, the fiduciary can request that the beneficiary contact or forward a letter to the missing participant.
- **Use electronic or Internet tools.** Many Internet search tools are free and can be used to locate a missing participant or beneficiary — including search engines, public record databases, obituaries, and social media.

If warranted by the size of a participant's account balance, additional search efforts may be appropriate. Possibilities include the use of Internet search tools, commercial locator services, credit reporting agencies, information brokers, investigation databases, and analogous services that may involve charges.

Comment. A fiduciary need not take these steps in any particular order. Rather, fiduciaries should consider cost and potential efficacy in determining the best search approach for a missing participant.

The plan fiduciary may charge reasonable expenses to participants' accounts for the cost of finding them. The amount charged must be consistent with the terms of the plan and the fiduciary's ERISA duties. The fiduciary can use paper or electronic records to demonstrate compliance if audited.

Rollover to an Individual Retirement Plan Always the Option of Choice

If, after exhausting all of the above search methods, the participant cannot be located, the plan will be forced to distribute the assets. The FAB makes no changes to previous guidance on distributing assets, reiterating that the best option is distribution to an individual retirement plan. In this scenario, the assets continue to grow tax-deferred, and the distribution is not subject to 20% mandatory withholding and avoids the 10% early withdrawal penalty. Plan fiduciaries are reminded that the selection of an individual retirement plan is a fiduciary act. The DOL established a plan



termination [safe harbor](#) that describes issues for plan sponsors to consider when selecting an individual retirement plan and related investments, namely, preservation of principal, reasonable rate of return, and fee structure.

The guidance also acknowledged that some fiduciaries have expressed concerns about legal issues that would make it difficult to open an individual retirement plan for a missing participant, and explained that customer identification and verification provisions (CIP) of the USA PATRIOT Act set standards to deal with these issues. Identification is not required at the time the account is set up, rather only when the participant or beneficiary comes forward to claim the account.

Distribution Options when IRA Not Available

If a fiduciary cannot find an individual retirement plan provider willing to accept the direct rollover for a missing participant, or decides not to make a rollover distribution for another compelling reason based on the particular facts and circumstances involved, as a last resort, it is permissible to open an interest-bearing federally insured bank account in the name of the participant or beneficiary, or transfer the account to a state unclaimed property fund. These actions should only be considered after all efforts to search for the missing participant have been exhausted, and the fiduciary is unable to open an individual retirement plan as such action will result in immediate taxation to the participant and future growth on the funds will no longer be tax-deferred. Therefore, plan fiduciaries must consider all aspects of these options including fees, interest rates, bank charges, and ability to search internet databases for the state unclaimed property information.

Comment. The plan fiduciary must perform all due diligence, and take care to document every step of this decision-making process. Such documentation will help the fiduciary demonstrate procedural prudence should legal action ever be taken.

Finally, as in earlier guidance, the FAB makes clear that it is not permissible to use the 100% income tax withholding option as a means of distributing the assets.

Scope of Guidance

The FAB is directed at terminating defined contribution plans that do not have either an annuity feature or where the sponsoring employer does not have an appropriate defined contribution plan to which the assets could be transferred. Money purchase pension plans and profit sharing plans that must retain annuity options, however, may also utilize the search methods described above — but they may not rely on this guidance for distributing the assets without obtaining appropriate consent. Where feasible, profit sharing plans with annuity options may want to consider removing the plan's annuity feature prior to termination.

Comment. Although anti-cutback rules generally protect a participant's accrued benefits and payment forms, a specific IRS regulatory exception allows for elimination of a profit sharing plan's annuity feature so long as participants are entitled to receive a single-sum distribution as of the date an annuity would have otherwise begun. This exception would not, however, override consent requirements for accounts subject to the qualified joint and survivor requirements.

Additionally, although the DOL guidance specifically applies to terminated plans, the search methods identified in the FAB may be helpful to administrators of ongoing plans that need to distribute assets to missing participants.

In Closing

Terminating plans must distribute all assets regardless of the size of the participant's account. How the assets are distributed is a fiduciary act, and plans fiduciaries are advised to handle the process accordingly. The selection of search methods for locating missing participants, and the search process itself, should be thorough, well thought-out, and documented.

Participants typically do not go missing overnight. In many cases, plan sponsors will be aware of a lost participant prior to plan termination — via returned statements or notices. That is the time to attempt to find participants, when the likelihood of finding them is highest.

Even if the plan sponsor never intends to terminate the plan, distribution of a participant's assets may still need to occur at some point in the future. To that end, plan sponsors may want to schedule a routine review of “bad addresses,” where plan mailings have been returned. A good, clean, up-to-date inventory of participant contact information can save a lot of headache and may prevent — or at least mitigate the effects of — legal action should a participant question plan processes.

Authors

Lisa A. Scalia, CPC, QPFC, QPA, QKA
Julia Zuckerman, JD

Produced by the Knowledge Resource Center of Buck Consultants at Xerox

The Knowledge Resource Center is responsible for national multi-practice compliance consulting, analysis and publications, government relations, research, surveys, training, and knowledge management. For more information, please contact your account executive or email fyi@xerox.com.

You are welcome to distribute *FYI*® publications in their entirety. To manage your subscriptions, or to sign up to receive our mailings, visit our [Subscription Center](#).

This publication is for information only and does not constitute legal advice; consult with legal, tax and other advisors before applying this information to your specific situation.