

## Missing Participants: Gone but Not Forgotten

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Plan administrators know all too well the practical challenges associated with the timely payment of benefits to plan participants, especially in those cases where individuals remain unresponsive to plan communications and are presumed missing. Last year, both the Department of Labor (“DOL”) and the Internal Revenue Service (“IRS”) showed an increased interest in this area. During the early part of 2016, the DOL stated that it would begin investigating large defined benefit pension plans to determine whether benefits were paid in a timely manner to terminated participants. Likewise, the IRS modified its instructions to Line 4l on the 2015 Form 5500 to address compliance issues regarding the timely payment of benefits. (Line 4l asks “Has the Plan failed to provide any benefit when due under the Plan?”) For plan sponsors to be able to answer “no” to Line 4l, the IRS clarified that they needed to make a “reasonable effort” to find unresponsive participants who were entitled to receive minimum distributions under Code Section 401(a)(9). This issue was not previously raised in the instructions to prior Forms. Answering “yes” to Line 4l may result in a plan sponsor receiving a request for information from the IRS Employee Plans Compliance Unit (“EPCU”). The EPCU has stated that one of its current projects focuses on whether plans may incur a “failure to provide a benefit.”

The Pension Benefit Guaranty Corporation (“PBGC”) currently administers a missing participants program to retain the retirement benefits for those participants and beneficiaries that are determined to be missing after a single-employer defined benefit pension plan has been terminated. The purpose of the program is to help such individuals locate and receive their benefits after all assets from the terminated plans have been distributed. In order to transfer these benefits to the PBGC, plan administrators must first conduct a diligent search for these individuals, which includes asking the missing participant’s known beneficiaries (if any) for the participant’s current address, and using a commercial locator service. The DOL has also issued guidance in its Field Assistance Bulletin 2014-1 (“FAB 2014-1”) that addresses the fiduciary duties associated with ensuring that missing participants and beneficiaries retain the rights to their retirement benefits following the termination of a defined contribution plan.

Currently, the guidance regarding how to deal with missing participants extends only to terminated plans. While this issue is of vital importance for such plans since all assets must be liquidated,



it also continues to be a concern for ongoing plans. Plan administrators have a fiduciary obligation to protect and preserve participants' rights to benefits to ensure they receive them in a timely manner. On September 20, 2016, the PBGC issued proposed regulations expanding its missing participants program to include terminated multiemployer plans (covered by Title IV of the Employee Retirement Income Security Act of 1974, as amended ("ERISA")), terminated professional service plans with 25 or fewer participants, and most terminated defined contribution plans. Participation is voluntary for the last two types of plans. Certain modifications made in the proposed PBGC regulations may help further guide plan sponsors of ongoing plans on how to deal with missing participants. Though the current and proposed guidance applies only to terminated plans, it would seem prudent from a fiduciary standpoint to rely on similar principles, where applicable, when faced with missing participants in ongoing plans.

## **Key Modifications to the PBGC Missing Participants Program**

### ***Diligent Search Procedures***

More specificity has been added to the diligent search procedures in the proposed regulations. Under current guidance, a diligent search includes attempting to locate the lost individual by contacting the beneficiaries listed under the terminated plan. This procedure will be updated to require that such searches must also include any other plans maintained by the employer sponsoring the terminating plan (taking into account its health plans, if any). In addition to checking the participant information available in each such plan, all beneficiaries listed under all other plans of that employer must also be checked to uncover any discrepancies in the reported information. Finally, the employer's records also must be reviewed to ensure that all such potential information sources have been uncovered.

Currently, the regulations require the use of a "commercial locator service" to search for lost participants. However, this term is not defined. The proposed regulations now clarify that "commercial locator service" is "a business that holds itself out as a finder of lost persons for compensation using information from a database maintained by a consumer reporting agency." For those lost participants with small plan benefits, the PBGC has contemplated that this definition may not be cost-effective and has included a waiver on this requirement in such instances. However, the amount deemed to be a "small" benefit has not yet been determined. Under current guidance (while this term remains undefined), plan administrators have the flexibility to use a commercial locator service that charges either minimal fees or no fees to complete such searches.

Another proposal is to require the use of a free internet search engine for purposes of making a diligent search for lost participants, regardless of the size of the participant's benefit. This could be used in such cases where the cost of employing a commercial locator service is a significant deterrent, such as where there is a small plan benefit. Other search methods include examining a network database, a public record database (such as those available for licenses, mortgages, and real estate taxes) or a "social media" website.

According to the proposed guidance, all of the proposed search methods must be attempted in order to satisfy the "diligent search" requirement. In proposing these changes, the PBGC has stated that it hopes to ensure that an "appropriate level of effort" will go into locating lost participants. The PBGC has also said that the modifications are intended to make the diligent search

procedures more consistent with the search guidance already provided in the current DOL FAB 2014-1 for terminated defined contribution plans. Based on these proposed modifications, it would seem that plan administrators for ongoing plans may have more assurance that reliance on the DOL guidance is appropriate and prudent in meeting the “diligent search” requirements when attempting to locate lost participants. It may also make sense to apply the definition of “commercial locator service” when selecting such providers, taking into account any waivers that may seem reasonable and cost-effective for small plan benefits. Note too that the IRS uses the same “commercial locator service” term in Revenue Procedure 2016-51 when recommending methods to locate lost participants under its Employee Plans Compliance Resolution System. It would seem reasonable to apply the definition proposed in the guidance in this instance as well.

### ***Unified Nationwide Pension Search Database***

Under the proposed regulations, a unified nationwide pension search database will be established to maintain information regarding missing participants’ benefits. It will be designed and operated for the PBGC by a private-sector entity with expertise in this area. The database is intended to be easy-to-use, designed to allow members of the public to easily search its directory to obtain missing participant information. Although access will be available to the public, the proposed regulations promise that the privacy of such participants will remain protected. Since the database will be made available to the public, it may benefit plan administrators of ongoing plans by providing an effective and free search method to assist in locating lost participants.

### ***Additional Proposed Modifications Addressed in the PBGC Regulations***

The following is a list of some of the other major modifications addressed in the proposed regulations:

- The definition of “missing participants” under defined benefit pension plans now allows non-responsive distributees subject to the mandatory cash-out plan provisions to be treated as missing participants, rather than as merely non-responsive ones. In those cases where there is an involuntary cash-out distribution in excess of \$1,000, the current program requires payment in the form of an automatic rollover to an IRA in the absence of an affirmative election by the participant or beneficiary under Code Section 401(a)(31)(B) and the PBGC instructions. Under the proposed regulations, this will no longer be the case. Defined benefit pension plans would be allowed to distribute the benefits of such participants to the PBGC rather than having to transfer them to an IRA.
- The PBGC will charge \$35 per each missing participant, payable when the benefits are transferred to the PBGC. No fee will be charged for amounts paid to the PBGC of \$250 or less (or for plans that only send information about missing participants’ benefits to the PBGC). Also, the PBGC will not charge continuing “maintenance” fees or distribution fees once benefits have been transferred.
- PBGC will create a user-friendly spreadsheet so that calculations can be handled by plan administrators (as opposed to hiring an actuary).
- Participation is voluntary for plans not subject to Title IV of ERISA, *i.e.*, most terminated defined contribution plans and terminated small “professional service plans” (those private sector defined benefit plans maintained by “professional service employers” such as

doctors, lawyers, accountants, actuaries, etc. with 25 or fewer participants). The intent is to provide plan administrators with another option for dealing with missing participants and beneficiaries when liquidating terminated plans. If such plans choose to participate, they could either elect to transfer the benefits to the PBGC or provide information concerning the disposition of the missing participants' benefits, if, for example, the benefit was transferred to IRA. Selective use of the missing participants program is not allowed for plans that have elected to transfer benefits to the PBGC. The concern is that a plan administrator might choose to transfer only small benefits to the PBGC, while larger accounts that potentially generate higher fees will be transferred to commercial providers. Plan administrators who dispose of benefits other than through transfers to the PBGC could elect to provide the PBGC with distribution information for only some of the missing participants rather than all.

- For defined benefit plans, there are fewer benefit categories and sets of actuarial assumptions for determining the amount of the benefit to be transferred to the PBGC.

### **Recommendations for Plan Administrators**

In light of the increased interest by both the DOL and the IRS in the timely payment of benefits, it is essential to have in place and follow plan procedures addressing how benefits will be distributed once participants become eligible for distributions, as well as the methods to be used in the event participants cannot be located or remain unresponsive. At a minimum, these procedures should include:

- a description of the timing and form of benefit distributions to be made to eligible participants;
- the frequency of plan communications to participants concerning their eligibility for distributions;
- when a diligent search is to be conducted in the case of lost and unresponsive participants (including those whose checks remain uncashed). For example, a search might be needed when participants are scheduled to begin receiving required minimum distributions ("RMDs") from the plan. The IRS has clarified on its website that a reasonable search, in the same manner as provided under the DOL FAB 2014-1 guidance, must be made to locate such participants when they are eligible to receive RMDs;
- the methods involved in satisfying the requirements of a diligent and reasonable search; and
- the manner in which benefits will be distributed once distribution must commence in the event lost or unresponsive participants are deemed to be missing participants following satisfaction of the diligent search procedures. Such options may include:
  - whether benefits will be forfeited (if the terms of the plan so provide, subject to reinstatement if a claim for benefits is later submitted to the plan);
  - whether benefits will be transferred to an IRA (or transferred to an insurance company that will issue an irrevocable commitment to pay benefits, in those cases where payments must be made in the form of an annuity);

- whether it may be feasible and necessary to transfer the benefit to a Federally-insured deposit account or the state of the missing participant's last known residence or work location under the state's escheat rules for abandoned property. This may occur in those cases where the above methods are not feasible in actual practice, such as where the accrued benefit is less than \$1,000.

It is also advisable to include a statement on all plan communications noting that it is the responsibility of plan participants to keep the plan informed of their current address. For this purpose, plan communications include summary plan descriptions, as well as applications for benefits.

## Notifications

For those participants who fail to keep the plan informed of their current addresses, another consideration is how to craft plan notices and communications to these individuals. This issue is of special concern in those instances where there has been a significant lapse in contact with plan participants regarding their eligibility for benefits. In an ongoing plan, the plan's provisions and its administrative procedures will generally dictate how and when benefits are paid once participants terminate employment and become eligible for distributions. Sometimes, notification may not take place until a great deal of time has passed following the participant's active participation in the plan. In a defined benefit plan, for instance, it is likely that notification will not occur until after the participant has reached his normal (or early, where applicable) retirement age, which may occur well after his termination of employment. Where a plan offers distributions following termination of employment, the plan procedures may leave it to the participant to make the initial contact concerning his benefit, waiting until the benefit is required to be distributed before notification from the plan is generated, except in those cases where the benefit must be distributed because it is a mandatory distribution.

Benefit payments may also be delayed where the plan administrator is not aware that a participant has died. In such cases, the plan administrator may only realize that the death has occurred after a claim for benefits has been submitted to the plan. Likewise, payments to alternate payees under a qualified domestic relations order may also be delayed where a plan administrator has not been informed of a divorce or settlement.

In such situations where a considerable length of time has passed, it is increasingly likely that plan records will include obsolete information. When attempting to make a "reasonable effort" to locate such participants and satisfy the "diligent search" requirements, it may be advisable to adapt any communications to include the following recommendations:<sup>1</sup>

- list any changes that may have occurred in the plan's name or sponsor since the individual participated in the plan to help prompt his recognition of the plan. This is especially important where the plan may have undergone name changes or plan mergers;
- include the length of the individual's plan participation to help reassure the participant that the communication is legitimate;
- keep participant information private by not including sensitive data (such as social security numbers) in the event the letter is opened by an unintended recipient;
- provide appropriate plan administrator/plan sponsor contact information so that the

individual may write to or speak with a representative to discuss his benefit. Adding a web address is also recommended so that the participant may verify the validity of the communication, if he so desires, by checking the website; and

- include a self-addressed stamped envelope to make it easier for the individual to respond to the communication.

Such recommendations may help to encourage a response from such individuals, who may have either forgotten that they maintain a benefit under the plan or are suspicious that such correspondence may be from disreputable sources.

## Summary

The proposed PBGC modifications may help provide further guidance for plan administrators of ongoing plans who still struggle with the administrative burden and fiduciary liabilities associated with dealing with missing participants' benefits. While the PBGC program considers only terminated plans, it is reasonable to assume that plan administrators could rely on the proposed guidance as a means of complying with their fiduciary requirements when conducting searches and attempting to locate lost participants, especially since the proposed regulations incorporate the current guidance provided under DOL FAB 2014-1. While the proposed regulations will not be finalized and in effect until 2018, reliance on the proposed modifications in the diligent search procedures may help fiduciaries further reduce their liability when attempting to locate lost individuals and distribute benefits to missing participants in a timely manner.

The establishment of a nationwide PBGC database may also provide another effective method for conducting searches since it will be made available to the public. Because no fee is associated with its use, it could be viewed as a prudent, cost-effective alternative for locating such participants. In addition, voluntary use of the missing participants program by terminated defined contribution plans (as well as small terminated professional service plans) may provide a more attractive method of dealing with missing participants by eliminating the need to transfer benefits to an IRA. By transferring the responsibility of missing participants' benefits directly to the PBGC, it may help ensure that missing participants are more likely to receive their benefits, rather than having them placed in IRAs that may be difficult to find years later.

In light of the more robust efforts being taken by the IRS and DOL in this area, it is best to craft or update procedures to help demonstrate compliance in locating lost participants and the timely payment of plan benefits. Having such procedures in place helps ensure that plan administrators are properly managing their fiduciary liability risk by taking reasonable and prudent steps to protect participants' and beneficiaries' rights to plan benefits.

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<sup>1</sup> Lois Gleason. "9 Pointers for Contacting Missing Pension Participants," *Word on Benefits* (blog), International Foundation of Employee Benefit Plans, December 19, 2016, <https://blog.ifebp.org/index.php/9-pointers-for-contacting-missing-pension-participants>.