Employer Update

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The information contained herein is meant for general educational purposes only.

DOL ISSUES GUIDANCE ON LOCATING MISSING PARTICIPANTS IN TERMINATED DEFINED CONTRIBUTION PLANS (FIELD ASSISTANCE BULLETIN 2014-01)

Under the Internal Revenue Code, a plan administrator must distribute all plan assets as soon as administratively feasible following plan termination. When terminating a defined contribution plan, the plan fiduciary must notify the plan participants that the plan is terminating and that all benefits will be distributed. In turn, the plan participants should provide directions to the plan administrator on how to distribute their account balances. In the Bulletin, the Department of Labor (DOL) stated "sometimes, however, participants fail to respond to the notices (or mail sent to their addresses is returned), creating a practical dilemma for the plan administrator who has a fiduciary obligation to search for missing participants and distribute their benefits.” The DOL refers to these unresponsive participants as “missing participants”.

Plan fiduciaries must make reasonable efforts to locate missing participants or beneficiaries, so that they can properly make plan distributions. In accordance with the Bulletin, fiduciaries are required, at a minimum, to take the following steps to find a missing participant:

1. **Use Certified Mail**. Provide a notice through certified mail to determine whether the participant can be located.
2. **Check Related Plan and Employer Records**. If the terminated plan does not contain the current address, check to see if other employer records or employer plans have up-to-date information regarding the participant.
3. **Check With Designated Plan Beneficiary**. The plan fiduciary must try to identify and contact the missing participant’s beneficiary to obtain updated information for the missing participant.
4. **Use Free Electronic Search Tools**. The plan fiduciary must make reasonable efforts to use free of charge internet search tools to locate missing participants, such as internet search engines, public record data bases (such as those for licenses, mortgages, and real estate taxes), obituaries and social media.

If after following the required search steps, the plan fiduciary does not locate the missing participant or beneficiary, the fiduciary has an obligation under the duty of loyalty and prudence to determine if additional steps are appropriate. The DOL suggests that the size of a participant’s account balance and the cost of further search efforts should be taken into consideration. Regardless of the size of the plan, the DOL also pointed out that some search steps involve so little cost and such a high potential for success that a fiduciary should always take them before abandoning all search efforts. Additionally, the DOL stated that when the account balance is large enough to justify additional plan expenses, more expensive approaches may be required. A plan fiduciary may charge the missing participants’ accounts for reasonable expenses in the efforts to find them.

In situations where the plan fiduciary cannot locate the missing participant, despite using the search methods, the plan fiduciary must select an appropriate distribution option for the participant in order to distribute all the plan assets and complete the
plan termination. ERISA requires that plan fiduciaries consider rolling over missing participant benefits into individual retirement accounts (IRAs). An eligible direct rollover will avoid immediate taxation and avoid the 20 percent mandatory withholding, as well as the 10 percent additional tax for early distributions. The funds in the IRA will continue to grow tax-free and income taxes will not have to be paid until the money is withdrawn. For these reasons, the DOL’s preferred method of distribution for missing participants is a direct rollover to an IRA.

Although the DOL guidance specifically addressed locating missing participants when terminating a defined contribution plan, the guidance provides good insight on the steps plans should be taking in all instances where there is a need to locate a missing participant.

**IRS and DOL ISSUE GUIDANCE ALLOWING DEFERRED ANNUITIES IN TARGET DATE FUNDS**

The IRS and DOL recently issued guidance permitting defined contribution plans, such as 401(k) plans and 403(b) plans, to offer a series of target date funds (TDFs) that include deferred annuities among their investment options, even if some of the TDFs within the series are only available to older participants. In particular, in the TDF series, as participants reach older ages, the mix of equity and fixed income exposure becomes more conservative over time. The new rules allow a percentage of the portfolio to be applied to the purchase of deferred annuities.

Since many older participants in defined contribution plans tend to be more highly compensated, there is a likelihood that the TDFs holding the deferred annuities will disproportionately favor highly compensated employees. The question posed to the IRS was whether a defined contribution plan would violate the nondiscrimination requirements if the TDF series includes deferred annuities that are only available to older participants. In Notice 2014-66, the IRS concluded that a series of TDFs is treated as a single right or feature and would not violate the nondiscrimination requirements, if certain conditions are met:

- The series of TDFs is designed to serve as a single integrated investment program under which the same investment manager manages each TDF and applies the same generally acceptable investment theories across the series of TDFs. Thus, the only difference among the TDFs is a mix of assets selected by the investment manager, which difference results solely from the intent to achieve the level of risk appropriate for the age-band of individuals participating in each TDF.
- Some of the TDFs available to participants in older age-bands include deferred annuities, and none of the deferred annuities provide a guaranteed lifetime withdrawal benefit (GLWB) or guaranteed minimum withdrawal benefit (GMWB) feature.
- The TDFs do not hold employer securities that are not readily tradeable on an established securities market.
- Each TDF in the series is treated in the same manner with respect to rights or features other than the mix of assets. For example, the fees and administrative expenses for each TDF are determined in a consistent manner, and the extent to which those fees and expenses are paid from plan assets (rather than by the employer) are the same.

In connection with the Notice issued by the IRS, the DOL responded to whether a series of TDFs which include deferred annuities for older participants would meet the requirements necessary to be considered a qualified default investment alternative (QDIA). In a letter by the Assistant Secretary of Labor, the DOL concluded that the use of deferred annuities in the TDFs, as described in the IRS Notice, would not cause the series of TDFs to fail to meet the QDIA regulations, as long as the designated investment manager for the fund satisfies the conditions of the annuity selection safe harbor set forth under ERISA when choosing the deferred annuities. Therefore, the DOL stated that in order to ensure that the investment manager is complying with the statutory standards and conforms with the terms and needs of the plan, the plan fiduciary is responsible for prudent selection of the investment manager for the TDF and monitoring the manager’s performance at reasonable intervals.

**IRS ISSUES FINAL REGULATIONS and PROPOSED REGULATIONS RELATED TO HYBRID PENSION PLANS**

Hybrid pension plans, such as cash balance plans and pension equity plans are defined benefit plans which define the benefits in terms that are characteristic of a defined contribution plan, such as stating the benefit as a lump-sum account balance. In accordance with the Pension Protection Act of 2006 (PPA), when calculating formulas under a hybrid plan, the plan cannot use an interest credit for any plan year that exceeds the “market rate of return.” In 2010 the IRS issued proposed regulations describing the market rate of return requirements, and on September 18, 2014, the IRS issued long anticipated final regulations. Under the final regulations, there are several methodologies a plan can use to satisfy the market rate of return requirements.
Although the primary issue covered by the final regulations involves the market rate of return, the regulations also address several other issues related to hybrid plans. The 2014 final regulations go into effect for plan years beginning on or after January 1, 2016. Plan sponsors of hybrid pension plans should carefully review the final regulations with their actuaries to determine whether changes are required to be made in order to bring their plans into compliance with the rules.

Coincident with the final regulations, the IRS also issued proposed regulations on September 18th as well. In some cases plans will have to amend their plans to satisfy the market rate of return when calculating benefits, and this could result in a cut-back in benefits to participants, a violation under the Code. The purpose of the proposed regulations is to address this issue and how a plan sponsor can amend the plan to comply with the final regulations and receive relief from the anti-cutback Code provisions.

IMPORTANT YEAR-END COMPLIANCE DEADLINES

Before year-end, plan sponsors may have to take action to ensure compliance with certain statutory and regulatory requirements. Here are some key compliance deadlines that may have to be addressed by December 31, 2014:

1. **Adopt Discretionary Plan Amendments** – December 31, 2014 is the deadline applicable to calendar year plans for the formal adoption of any discretionary changes that became effective during the plan year.
2. **Make 2014 Required Minimum Distributions (Age 70 ½)** – December 31, 2014 is the deadline to make minimum required distributions to participants who have begun to receive such distributions.
3. **Allocate Forfeiture Accounts** – Review the plan document for forfeiture allocation requirements; allocate forfeitures by the last day of the plan year.
4. **Make Corrective Distributions for Excess 2013 Contributions** – December 31, 2014 is the deadline applicable to calendar year plans for distributing corrective distributions for failed ADP/ACP tests with a 10% excise tax.
5. **Amendments for Same-Sex Marriage** – Plans that defined spouse or marriage as only between a man and woman, or incorporated the now unconstitutional definition under DOMA must be amended by December 31, 2014 to remove such references and recognize same-sex marriage. However, plans that do not have a specific definition of spouse within their plan documents do not require an amendment.
6. **Plan Restatements** – Individually designed plans with an Employer Identification Number (EIN) ending in 4 or 9, are considered Cycle D filers and have until January 31, 2015 to restate their plans and submit them to the IRS for a determination letter.

Next Steps

Review your plan for these year-end compliance deadlines. Please feel free to call your representative at USI Consulting Group for assistance and additional information.

ANNUAL PARTICIPANT NOTICES FOR DEFINED CONTRIBUTION PLANS

Below is a list of Notices and deadlines that plan sponsors may have to distribute by November 30th (deadlines applicable for calendar-year retirement plans):

1. **Automatic Enrollment Notice (ACA) (EACA) (QACA)** – Deadline for plans with automatic enrollment features: 30-90 days prior to the start of each Plan Year.
2. **Qualified Default Investment Alternative Notice (“QDIA”)** – Deadline for plans that have a QDIA: 30-90 days prior to the start of each Plan Year.
3. **Safe Harbor Notice** – Deadline for Safe Harbor Plans: 30-90 days prior to the start of each Plan Year.
4. **Participant Fee Disclosure (ERISA Section 404a-5)** – Deadline for all plans: Department of Labor’s extension permits the 2014 notice to be provided with the annual notices listed above.

Next Steps

Verify that all notices applicable to your plan have been or will be distributed by the corresponding deadline(s). Please feel free to call your representative at USI Consulting Group for assistance and additional information.

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