

DB digest

Best Practices for Pension Administration

UPCOMING KEY DATES

1/15/17

Due date for the fourth quarterly contribution for 2016, either through cash contributions or a signed election to use available carryover and/or prefunding balances.

1/31/17

Pay participants the increase in monthly age-70 1/2 required minimum distribution (RMD) to reflect additional benefits accrued in 2016.

1/31/17

Provide 2016 IRS Form W-2 (Wage and Tax Statement) to employees, reporting wages and coverage as an "active participant" in a qualified plan.

1/31/17

Provide 2016 IRS Form 1099-R (Distributions from Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.) to recipients of 2016 distributions.

3/15/17

Deadline for a calendar year employer to make a qualified plan contribution and deduct it for 2016 (though extended if the employer's tax return is extended.)

3/31/17

Deadline for a plan administrator to provide a Summary Plan Description to an individual who became a plan participant on 1/1/2017.

To download a PDF of the DB calendar, please go to:
tinyurl.com/DBSECalendar2017

Plan terminations – Breaking up is hard to do

Stephanie Sorenson

Your defined benefit (DB) plan is frozen for participation and accruals—all new hires are directed to enroll in a 401(k) plan. It is anticipated that the plan will be terminated when asset values are sufficient to satisfy all plan benefits.

You know the termination process can be lengthy, time consuming, and costly. There are multiple notices to be sent, forms to file, and annuities to purchase. You know your actuary, trust custodian, attorney, trustee, and investment advisor will assist with many of the tasks, but as plan administrator what can you do to be prepared?

Data

It is important to review and validate the participant data. Quality data is critical to the termination process. Insurer quotes will reflect the accuracy, actual or perceived, of the data provided to them.

Also the Pension Benefit Guaranty Corporation (PBGC) requires that the plan sponsor maintain the participant and plan data for six years after plan termination (the date on which PBGC Form 501 is filed). The data should be gathered during the plan termination process and remain accessible during the six-year period.

Does the data have valid identification numbers for all participants? Does the data contain valid dates of birth, hire, participation, and termination? If not, review employment records and update.

Does the data include addresses for all participants and beneficiaries? Are the addresses valid? Do any participants reside outside the United States? Many notices are required to be sent during the termination process. An address and death search for all inactive participants may be prudent. Verifying addresses prior to termination can save time and frustration.

Have all of the accrued benefits been calculated and certified? If yes, does the data include the information that was used to calculate the stored accrued benefit? During the termination process, a Notice of Plan Benefits will need to be supplied to all participants. This notice is required to provide the personal data used to calculate the participant's accrued benefit along with a statement requesting that the participant correct any information they believe to be incorrect. If the plan has frozen accrued benefits but the calculation data is not available, the best available data must be provided to the participant on the Notice of Plan Benefits along with a statement giving the participant the opportunity to provide the missing data.

If benefits are not calculated and certified, does the data contain all of the information necessary to calculate the benefits? Final benefits will need to be calculated, not estimated, for all participants.

Data is fluid and constantly changes. Participants move, die, quit, get married/divorced, and retire during the termination

process. Ensuring and maintaining accurate data is key to preparing for a plan termination.

Missing Participants

Does the plan have any missing participants? If yes, a 'diligent' search should be performed for any missing participants or beneficiaries. Unless there is proof of death, missing participants are assumed to be living and must be covered by an annuity or transferred to the PBGC during the termination process. The Employee Retirement Income Security Act (ERISA) defines a diligent search as: 1) beginning not more than six months prior to when the Notice of Intent to Terminate is issued, 2) contacting alternate payees and/or designated beneficiaries, and 3) using a locator service.

Required Minimum Distributions (RMDs)

It is important to make sure all operational issues have been addressed and corrected. For example, if there are a number of locatable participants over 70 ½ who have not received a required minimum distribution, that issue should be corrected using the Self-Correction Program or the Voluntary Compliance Program under the IRS Employee Plans Compliance Resolution System (EPCRS).

Qualified Domestic Relations Orders (QDROs)

Any outstanding or questionable QDROs should be cleaned up. All alternate payees should be easily identifiable and linked to a related participant. If possible, offsets from the participant and benefits for the alternate payee should be calculated and stored.

Small lump sums

Except for participants with small benefits, DB plans are required to offer participants an annuity upon plan termination. Therefore, participants with present values under the mandatory cash out limit should be located and lump sums distributed.

What is the current mandatory cash out limit in the plan? Is it under \$1,000? Can the limit be increased and an automatic rollover provision for amounts between \$1,000 and \$5,000 be implemented?

If it is not already included, the plan document may need to be amended to add a small lump sum provision or, if desired, to make the provisions more robust.

Audits

Are there any outstanding uncashed or stale checks? Since the plan will be purchasing annuities prospectively and closing the trust account, all uncashed past distributions should be resolved with the trust.

Are disability audits or death audits necessary? Unresolved periodic administration items should be taken care of and kept current.

Plan document

A terminating plan must be amended for any and all current laws that apply to the plan and are in effect as of the date of termination. This is true even if the plan would not otherwise be required to amend the plan by that date.

Are other plan provision changes wanted? For example, if the plan does not offer a lump sum, it may be less costly to offer non-retired participants the choice of a lump sum distribution rather than provide a benefit over their lifetimes under a group annuity contract.

If a lump sum window or provision is not desired, mandatory lump sum provisions should be considered as noted above.

All amendments should be adopted—either required or desired—and, if necessary, the Summary Plan Description updated and distributed. Translation of materials into foreign languages should also be done, if needed.

Determination letter

Most plan sponsors will request a final determination letter from the IRS. Distribution of plan assets often occurs a year after the termination date. There is an exception of 120 days following the issuance of the determination letter, if the plan applies with the IRS or 240 days after the PBGC Form 500 is filed, whichever is later. If a determination letter is requested, distributions should be delayed until after the letter is received (except ordinary distributions for

death, termination, etc.). Therefore, it needs to be decided if the termination process will wait for IRS approval prior to moving forward and distributing assets. Obtaining the final determination letter prior to asset distribution is prudent and ensures that all qualification requirements have been met, but could add several months to the overall process.

Investments

It is important to include the plan's investment advisor, custodian, and trustee in the plan termination process so that the plan will be ready to pay lump sums and transfer money to the annuity provider.

Communication

A communication strategy should be designed. There are several individualized notices that must be sent to participants. It is also common for the plan sponsor to explain the overall process in a cover letter and, once annuities are purchased, to send a "goodbye from trust, welcome to the annuity provider" letter. In addition, the plan sponsor should ensure that participants understand why this change is being made and, in some instances, what would happen if the change were not made. Robust participant communication is essential for a successful termination.

Summary

The plan termination process can seem overwhelming. However, understanding the termination process and industrious preparation can make the task manageable and efficient. It may be helpful to break the plan termination project into steps and assign the steps to the responsible party with frequent check-in meetings along the way. A Milliman consultant would be happy to help you navigate the plan termination process.

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