Testimony

on Behalf of Aon Hewitt

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Before

ERISA Advisory Council

Locating Missing and Lost Participants

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Aon plc is the leading global provider of risk management, insurance and reinsurance brokerage, and human resource solutions and outsourcing services. We have 65,000 colleagues in 120 countries around the world. Aon has been named repeatedly as the world's best broker, intermediary, reinsurance intermediary, captives manager, and best employee benefits consulting firm by multiple industry sources.

As the global leader in talent, retirement, and health solutions, Aon Hewitt is the largest independent provider of administration services for retirement plans, serving more than 14 million retirement plan participants in the U.S. We have more than 7,500 retirement professionals dedicated to helping plan sponsors maximize retirement outcomes for their employees, manage risk, and control total plan costs.

My name is Rob Martorano, and I am the vice president of Aon Hewitt's Defined Benefit Administration practice. I am honored to be addressing the ERISA Advisory Council on locating missing and lost participants in retirement plans.

Joining me today is Mary Steigerwalt, partner and Chief Operating Officer at Risk Compliance Performance Solutions, LLC (RCP).

RCP is a risk management and compliance company. The Retirement Plan Management Services Group of RCP helps plan sponsors, record keepers and custodians mitigate risks associated with missing participants in retirement plans. RCP deals with unclaimed assets by having individuals take any required actions to put their account in good standing. Aon Hewitt partners with RCP to help our benefits administration clients search for and contact missing and lost participants.

Through our work with plan sponsors, we are committed to helping plan sponsors reduce the number of missing participants and most importantly, to unite participants with their retirement funds.

Our testimony will focus on four key areas:

I. The problems created by missing participants;
II. Fiduciary uncertainty and challenges associated with missing participants;
III. Common questions and considerations for plan sponsors; and
IV. Recommendations for providing further clarity and additional guidance on plan sponsors' role in locating lost and missing participants.

I. The missing participant problem

As the American workforce has become more transient, the number of participants who are "lost" to plan sponsors has increased as the connection between individuals and their previous employers becomes eroded. Aon Hewitt estimates that up to 30% of terminated vested participants can become lost. These so-called "missing participants" create problems for both plan sponsors and participants.

Participants become lost for a variety of reasons. A participant may have moved, changed marital status, not updated their records, or changed jobs without notifying their previous employer. In other cases, the participant may be deceased and their beneficiary is not able to be located by the plan sponsor, or the participant is unaware that a benefit is due to them. On the other hand, employer actions such as mergers, sales, divestitures, and bankruptcies can contribute to participants becoming lost or missing because of changes in plan sponsor name and oversight. These lost participants create six primary problems for plan sponsors and participants.

<u>Problems for plan sponsors</u>

1. As a plan fiduciary, plan sponsors must meet disclosure requirements for items such as Summary Annual Reports, Summary Plan Descriptions or Summary Material Modifications and the like. It is unclear what action is required to ensure compliance with disclosure rules when updated addresses are not available.
2. If the plan owes a benefit to a missing participant or beneficiary, the plan is obligated to make a "good faith effort" to locate the missing participant in order to avoid plan operation violations and breach of fiduciary duties. It is not clear what a good faith effort includes, creating uncertainty and risk for plan sponsors.
3. Missing participants limit plan sponsors from being able to execute certain pension plan de-risking strategies because the sponsor must be able to present participants with their benefits options and allow them to choose a form of payment, which isn't possible if participants cannot be found.

<u>Problems for participants</u>

4. Understanding and managing all their retirement assets is key to participants' ability to plan for their retirement. According to Aon Hewitt's analysis, just 29% of American workers are on track to meet 100% of their needs in retirement. If they aren't aware of possible benefits owed to them, they aren't able to manage or benefit from missing retirement dollars and the risk of insufficient retirement assets is increased.
5. Incorrect information may pose a security risk to participants if sensitive personal information is delivered to an outdated address.
6. Participants who can't be located are unable to choose potentially desirable payments in the event of plan sponsor de-risking strategies or other events that trigger potential payment.

In spite of increasing prevalence of lost and missing participants, it has recently become more difficult to address for plan sponsors. Plan sponsors previously had access to the IRS letter forwarding service to search for missing participants and verify addresses. However, in September, 2012, that service was eliminated and plan sponsors were left with few government-provided avenues to perform a good faith search for missing participants. While the Social Security Administration can provide letter forwarding services to employers, the process is expensive ($35 per participant), lengthy (can take up to eight months) and the long-term results are limited as only the requested letter is forwarded (plan sponsors do not receive address updates). In addition, neither the IRS letter forwarding service nor the Social Security Administration service was ever presented as a safe harbor or recommended approach by ERISA for missing participants in active plans.

II. Fiduciary uncertainty and challenges

Plan sponsors have a number of questions about satisfying their fiduciary responsibility including:

- What steps are required to obtain updated information for potential lost or missing participants?
- Is communicating to an address that is known to be a bad address acceptable to satisfy disclosure requirements?
- Whose responsibility is it to do this? The plan sponsor's? The record keeper's?
- What options are available now that the IRS no longer offers letter forwarding service?
- Is the Social Security Administration offering a viable option?
- When has the plan met its fiduciary obligations?
- What will stand up in court?

There are no clear answers to these questions. Plan sponsors recognize that there are communication requirements within their defined contribution (DC) and defined benefit (DB) plans, but there is no specific guidance when it comes to whether the plan is required to send the communication to the address of record versus determining if an updated address is available. This lack of guidance leads to broad uncertainty around fiduciary risk, including the questions posed above. Many plan sponsors believe that their fiduciary obligation is met if they mail communications to the last known address. Other plan sponsors feel obligated to take any returned mail and attempt to uncover additional address information.

In today's environment, absent clarity, there is no silver bullet. Each plan sponsor has a different risk tolerance and culture that influence the extent of additional searches they conduct.

III. Common questions and considerations for plan sponsors

In this section, we will outline responses to some commonly asked questions about lost or missing participants and provide considerations for plan sponsors.

What is a missing participant?

When a terminated participant with a balance in a DC plan or a vested pension benefit cannot be located after a mailing to the last known address, the person is generally referred to as a missing participant. There is a general understanding in the marketplace that plans have an obligation to try to locate all missing participants. This obligation is not specifically outlined in either ERISA or the Internal Revenue Code but, instead, is based on a combination of IRS Code vesting and distribution rules and from the fiduciary duties outlined in ERISA.

When do plan sponsors look for missing participants?

The concept of a bad address applies mostly to notification requirements. ERISA requires plans to send certain notifications to participants at their last known address. However, once mail has been returned from the last known address and it has been verified as a "bad address," plan sponsors often choose to cease sending notifications to that address, and document the presence of the bad address in the system of record. Further action is usually not taken for notification purposes.

The responsibility to locate a participant is much greater once the plan owes a benefit to a missing participant. The duty to pay a benefit should be distinguished from the ability to allow a payment if certain conditions are met. This is the difference between "may pay" versus "must pay." For example, in the DB world, plans *may* pay a benefit at the early retirement date but generally *must* pay a benefit in cash-out and Normal Retirement Age (NRA) situations and certainly by the required minimum distribution date. Similarly, most DC plans *may* pay at termination but *must* pay in cash-out situations and by the required minimum distribution date.

Once the plan is required to pay a benefit (*must* pay), the duty to locate a missing participant goes beyond notification purposes and further action is usually taken. Plans must make a good-faith effort to locate the missing participant in order to avoid plan operation violations and breach of fiduciary duties.

Not paying a benefit when it is owed violates both legal and plan rules. Failure to pay may lead to penalties and in some cases, places the plan's qualification status at risk. It is the responsibility of a fiduciary to operate the plan in accordance with the plan document and for the exclusive purpose of providing benefits to plan participants and beneficiaries. The plan sponsor must decide how to satisfy this responsibility.

How should plan sponsors look for missing participants?

Plan sponsors should have a process that will allow them to understand potential risks in their address data and to mitigate these risks by searching for correct addresses and communicating to the participants appropriately. Aon Hewitt has found that the typical plan sponsor process can be boiled down to three very basic components, each of which is necessary to maximize results, including:

1. Data scrubbing
    a. Search the entire plan database for any inconsistencies in the data such as bad addresses, incorrect date of birth, possible social security number inconsistencies, and available date of death.
    b. Search the known bad addresses for updated information.
2. Communications
    a. Confirm address updates via a mailing and a request for confirmation of the data in the plan either by mail or phone. By "confirm" we mean that the participants must confirm their identity and their current address. This is typically used in cases where the information provided in future communications is private or contains sensitive information.
    b. Unconfirmed address update via mailing of non-sensitive information.
    c. Phone outreach for confirmation of correct/incorrect information on file.
3. Deceased participant benefit option
    a. Use of a locator service to search for potential beneficiaries on first degree relatives.

The frequency and thoroughness of efforts will depend on the size of the plan and the magnitude of the lost or missing participant problem. When mail is returned, the plan should have an established bad address process. In general, an effort should be made to establish that it is truly a bad address and document the presence of the bad address in the system of record. For example, at Aon Hewitt, a bad address indicator is placed on the account in the system once any mail is returned. At that time, we will work with the plan sponsor to search for the participant. If the participant does not contact us, the bad address indicator will remain on the system until they are located. Since the expiration of the IRS letter forwarding service, Aon Hewitt has found that using private locator services to search for lost or missing participants and then providing updated information back to the record keeper and plan sponsor is the most effective method for searching for lost and missing participants.

Aon Hewitt's approach is to use a first class mail outreach service as it most closely mirrors the IRS letter forwarding service with the added benefit that the participant can confirm their address and the confirmation is tracked. Similar to our practice with the IRS Locator service, this approach identifies potential current addresses and sends the participant a letter asking them to contact us. If the participant contacts us and confirms the address, we update the address on our record keeping systems. At the end of the search period, Aon Hewitt receives a detailed audit trail summarizing the results of the search that can then be shared with the plan sponsor to help prove that a good faith search effort was completed.

Successful missing participant case studies

The following case studies illustrate successful examples of missing participants that were located via the three processes previously outlined.

1. Data scrubbing:
A plan sponsor moved their retirement plan from one record keeper to another and in an attempt to properly communicate this change and to make sure that they are did not give bad data to the new record keeper, the plan sponsor completed a scrub of the data and determined that there was a large population of deceased or lost participants. Typical results from RCP efforts include identifying

addresses for more than 90% of missing or lost participants, and identifying deceased participants at a rate of approximately 2%.

2. Knowledge of data issues:
A plan sponsor indicated they completed a lump sum communication to its participants and believed they reached everyone at their current address. Their service provider indicated that their address information was “clean.” However, after a review of the file and a scrub of the data by RCP, 47% of the participants actually had a new address. As a result, the initial communication was not successful and if not discovered, almost half of the participants would not have received the information needed to make a decision.

3. Terminated plan outreach:
In this case, communication with participants during the plan termination process (using the FAB 2004–02 guideline) gave the plan sponsor a prime opportunity to locate participants. In fact, RCP’s data suggests that up to 60% of lost participants come forward during the termination process.

4. Phone number search:
A plan sponsor wanted to communicate with participants via phone because of the lack of response they received from a mailed communication. The phone number search by RCP resulted in the identification of 91% of available numbers and gave the plan sponsor the opportunity to contact those participants who had not previously responded.

What is the problem with un-cashed checks and how are they handled?

Un-cashed checks in retirement plans are also a major issue for plan sponsors of both DB and DC plans. These occur when checks are created and distributed to plan participants, but they remain un-cashed and the dollars usually sit in a cash account, typically not earning meaningful investment return. Many plan sponsors believe that even though it is not clear that dollars from un-cashed checks are ERISA protected, the process of location and communication is handled as if the asset is indeed ERISA protected and is the plan’s fiduciary responsibility to unite the asset with its rightful owner. Plan sponsors attempting to determine if the funds should be treated as protected often ask; “is the asset still held in the general fund of the specific plan and /or in the trust account?” Ultimately, the goal should be to put the asset in the owner’s hands regardless, and we find that plan sponsors usually work towards this goal, which requires both identifying and encouraging the participant to take the action to receive the funds by cashing or depositing the check.

IV. Recommendations and observations

In the council’s objective and scope statement, the council requested input and feedback on seven specific items. Aon Hewitt has provided recommendations and observations that will to address the council’s request.

<u>Recommendations</u>

A. **Identification of current industry practices, including methods for searching for lost participants:** Aon Hewitt recommends the Department of Labor provide a safe harbor that clarifies fiduciary obligation has been fulfilled with respect to lost and missing participants if, at least, an annual search for any known bad addresses is performed on mail that has previously been returned. Frequency of searches should expand to include all participants as they approach Required Begin Dates (Normal Retirement Age, Required Minimum Distributions, etc.). Based on Aon Hewitt’s experience, this search should involve a request for confirmation from the participant to ensure the correct participant is located. Because there is not a one size fits all solution for the missing participant problem, we recommend flexibility with respect to methods and providers, including government and private providers, but suggest that detailed, auditable reports be required.

B. **When does a distributed benefit cease to be a "plan asset:"** Aon Hewitt recommends the Department of Labor provide plan sponsors with further guidance to determine when an asset is no longer a plan asset. Today, this is discussed and determined by the ERISA attorney of the plan sponsor. The real gap in understanding is an issue with un-cashed checks. Many times the specific guidance is outlined in the plan document. Plan sponsors state "we believe that the asset is no longer ERISA protected, but we want to treat the process as if it is protected so that the FAB process is followed." Clarifying that the funds are no longer plan assets following a period of time after a check has been issued would provide plan sponsors with confidence in their approach and reduce unnecessary administrative burden and legal fees.

C. **Guidance on efforts to deal with small benefit amounts:** Aon Hewitt recommends plan sponsors should make a reasonable effort to search and communicate with those participants who have a small balance in their account. Typically a determination is made as to whether the cost of the search and mailing is worth the amount held in the account. However, Aon Hewitt believes that regardless of the balance in the account, a reasonable effort should be made to locate the participant.

D. **Reducing the number of lost participants:** There are currently no obligations/requirements that are helpful in reducing the number of lost participants. One best practice that Aon Hewitt has seen is a regularly scheduled twice-a-year scrub of the bad address data. It is a proactive approach that plan sponsors can take to improve management of the process and communication with participants. There are many mandatory communications required during a typical plan year such as Summary Annual Report/Annual Funding Notices. Consistent with item A, Aon Hewitt recommends the Department of Labor provide plan sponsors with further guidance and a safe harbor for searching for participants and keeping addresses of terminated participants up to date to prevent the missing participant population from growing and to reunite participants with their retirement funds.

Observations

A. **Fiduciary obligations surrounding the location of lost participants:** Aon Hewitt agrees, as many plan sponsors do, that it IS the plan sponsor's fiduciary responsibility to make a reasonable, good faith effort to locate lost participants, and it is appropriate to pay the fees from plan assets. Plan sponsors typically pay for the service out of plan assets particularly when the plan is continuing. There are some plan sponsors that choose to charge the fee back to the participant in account balance plans. This is typically the case in plan terminations where there are several required and costly steps and in situations where the employer is in the process of closing down the business and they no longer have the ability to pay the fees to process the termination.

B. **Applying state abandoned property and escheatment laws:** Few plan sponsors apply the state abandoned property and escheatment rules to their retirement accounts. Legal counsel often informs them that ERISA protected property is not due to escheat until the expiration of the dormancy period after the Minimum Required Distribution age (70 ½). Of course, many states have told us that they would take the money but because the funds are no longer invested, and many states do not proactively search for the account holders, many plans move the money over to a rollover provider as an alternative because they believe it is a better option for participants. As the GAO noted recently, not all rollover providers continually search for missing account holders.

C. **The benefit accounting issues involving lost participants:** Plan sponsors need additional guidance on managing un-cashed checks. The benefit accounting issues associated with lost or missing participants can vary by plan and participant. How to treat un-cashed retirement checks, whether to send checks to a known bad address and the inability to match participants with money that is rightfully theirs are common. Once required begin dates are met, the money no longer belongs in the plan, but without the ability to locate a participant, there is confusion on how to handle these funds.

V. Conclusion

Locating lost or missing participants is a growing problem for plan sponsors and participants because of the challenges of meeting required disclosures, fiduciary risks, participants' loss of flexibility to choose desired benefit in de-risking efforts, and the potential for participants to lose benefits all together. The council has an opportunity to encourage plan sponsors to locate lost or missing participants by clarifying the process and further defining plan sponsors' obligations.

We appreciate the opportunity to share our experiences and perspectives with the council. We would be pleased to provide our resources and expertise as you work towards a solution to this issue. Thank you.

Biographies

Rob Martorano

Rob is a vice president and the National Defined Benefit Practice Leader for Aon Hewitt's outsourcing business. In this role, Rob serves as the subject matter expert for the DB delivery model, best practices, capabilities, legislation, quality controls, and market trends. Rob is aligned to over 130 Outsourced and Co-Sourced Defined Benefit clients operated out of our North American Offices.

With over 22 years of Defined Benefit experience, Rob's career in Pensions began as a Certified Public Accountant auditing Pension and other benefit plans for Howard Levinson and Associates, a Chicago based accounting firm. He came to Hewitt in 1994 after becoming a CPA.

Rob's been with Aon Hewitt for 19 years working in a variety of roles including project manager, implementation manager, and a Benefits Delivery manager. He has worked on many large and complex clients in the large market outsourcing business. As a Benefits Delivery manager Rob gained experience in both Health and Welfare and Defined Contribution while maintaining deep roots in DB.

Rob earned a Bachelor of Arts Degree in Finance and Accounting from Augustana College in Rock Island, IL. Rob has earned awards in the areas of people management and customer focus.

Mary Steigerwalt

Mary is a partner at RCP Solutions and the Chief Operating Officer. As COO, Mary is responsible for the current and long term effectiveness of all financial, and Human Resources and Benefits functions of the organization as well as the Operations of the Retirement Plan Management Services group.

Prior to her role at RCP, Mary managed all critical client service functions as Chief Operating Officer of The Keane Organization. Her position included the oversight of and responsibility for operations in the Unclaimed Property Services Division, Consulting Services, Retirement Services Division, SEC Search Compliance, and Client Services for all corporate and mutual fund clients. In addition, as President, Mary launched the newly developed Keane Retirement Services leveraging her more than 20 years of experience managing and understanding the ERISA guidelines and Department of Labor requirements of retirement plans as a Plan Sponsor herself. Mary has held other positions managing various human resources, personnel, benefits and accounting roles.

Mary earned a Business Administration degree at La Salle University in Philadelphia, PA.