

**STATEMENT OF THE PENSION RIGHTS CENTER
ON PERMISSIVE TRANSFERS OF UNCASHED CHECKS FROM
ERISA PLANS TO STATE UNCLAIMED PROPERTY FUNDS
BEFORE THE ERISA ADVISORY COUNCIL**

AUGUST 28, 2019

Good morning. I am Jane Smith, Policy Analyst for the Pension Rights Center. The Pension Rights Center is a nonprofit consumer organization that has been working since 1976 to protect and promote the retirement security of American workers, retirees and their families. We applaud the ERISA Advisory Council for studying the issue of uncashed checks distributed by retirement plans. Thank you for inviting us to testify.

The problem of uncashed checks is part of the larger issue of missing participants which, in turn, relates directly to the challenges the faced by the Pension Rights Center and the pension counseling projects in locating lost retirement plans. For the past 25 years, we and the six federally funded regional counseling projects have helped tens of thousands of individuals obtain the retirement benefits they have earned. However, we often first have to help participants locate their plans, a process which can be very difficult and time consuming.

For this reason, the question before the Council, whether voluntary transfers of uncashed checks to State unclaimed property funds would be an optimal way of connecting people with their retirement money, is of great interest to us.

Background

Distribution checks from retirement plans remain uncashed when they are sent to old or wrong addresses because the participant moved and the plan does not have a correct address or the individual has died. Occasionally participants may fail to cash a check because they overlooked it, particularly if the amount is small. Also, they may not realize the significance of a letter from a company where they worked long ago or may not recognize the name of the sender of the check if an employer or service provider has changed names. This is particularly true for checks sent to a beneficiary of a deceased participant.

There are three principal sources of uncashed checks where the distribution is usually made without the consent of the participant.

- Plans are required to commence distributions at normal retirement age under section 401(a)(14) of the Internal Revenue Code or in the year after the year that the participant attains age 70 ½ under section 401(a)(9) of the Internal Revenue Code. (Required Minimum Distributions are not required for Roth accounts.)
- Plans are permitted to send checks to separated participants who have account balances of \$1,000 or less without their consent.

- A terminating 401(k) or other defined contribution plan is required to distribute all assets to participants and beneficiaries in the plan. Unless all assets are distributed, the plan cannot be terminated.

The agencies have provided some guidance in these situations, but it has not been sufficient to address most missing participant or other uncashed check situations.

- For uncashed distribution checks at age 70 ½ Treasury regulations say that whether benefit payment checks are returned or not, plans can forfeit the benefit if the participant or beneficiary cannot be located. (Treasury regulations section 1.411(a)-4(b)(6)) The regulations requires that the participant's or beneficiary's benefits be reinstated if he or she makes a claim at a later time. (These forfeiture/reinstatement rules apply only if they are included in the plan document.)
- The Labor Department's safe harbor for mandatory distributions of small account balances of \$5,000 or less requires a rollover to an IRA for balances over \$1,000. Account balances of \$1,000 or less may be rolled over or a check may be issued to the participant. (See section 2550.404a-2(c) of the Labor Department's regulations.) There appears to be no guidance from either the IRS or the Labor Department encouraging preservation of benefits if checks in the amount of \$1,000 or less are not cashed.¹
- The Labor Department has a safe harbor for terminating defined contribution plans that sets forth the fiduciary duties applicable to the termination of a plan that includes missing participants. (Field Assistance Bulletin 2014-01) The safe harbor requires that a series of search steps be taken and states that a missing participant's account should be then rolled over to an IRA. However, if the fiduciary is unable to do a rollover or chooses not to do so for a compelling reason, then the fiduciary may consider two other options: opening an interest-bearing account in a federally insured bank or transferring the account balance to a State unclaimed property fund.² However, the FAB does not require that the fiduciary report where the money was sent. As a result, there is no easy way for participants and beneficiaries to later find their benefits.

Under the PBGC's new missing participants program, employers in terminating defined contribution plans have been given a new option. They can send money in the accounts of missing participants to the PBGC. The accounts will earn interest and the participants or beneficiaries can find a listing of the accounts on the PBGC's website. However, participation by employers in this program is voluntary.

The problem of uncashed distribution checks is significant. A January 2019 Government Accountability Office (GAO) report states that in 2016, \$22.4 million was transferred from defined contribution plans

¹The Labor Department's safe harbor for a rollover to an IRA applies only if Code section 401(a)(31)(B) applies, but Code section 401(a)(31)(B) applies only to a distribution in excess of \$1,000 (but not in excess of \$5,000).

² EBSA Field Assistance Bulletin 2014-01. "If a plan fiduciary cannot find an individual retirement plan provider to accept a direct rollover distribution for a missing participant or determines not to make a rollover distribution for some other compelling reason based on the particular facts and circumstances, the fiduciary may consider two other options. These two options are: 1) opening an interest-bearing federally insured bank account in the name of the missing participant or beneficiary, or 2) transferring the account balance to a state unclaimed property fund. Before making such a decision, however, the fiduciary must prudently conclude that such a distribution is appropriate despite the potential considerable adverse tax consequences to the plan participant."

to 17 State unclaimed property funds.³ The GAO also reported that a survey of seven large service providers showed the majority of plan savings transferred by the service providers to States in 2016 was from terminating plans. Although the average retirement savings amounts transferred were relatively small, these amounts when invested can grow over time.⁴ The GAO also reported that one service provider indicated that individuals with transferred accounts were often younger than 70 ½, the age for required minimum distributions.

Discussion

Although State unclaimed property programs are a very useful repository for dormant bank and insurance accounts, for unclaimed stock and bond certificates, utility company rebates, contents of safe deposit boxes, unused gift cards and many other tangible and intangible items, they do not provide ERISA protections to retirement plan participants and beneficiaries.

Unlike arrangements within the ERISA framework, funds transferred to State unclaimed property programs are no longer protected by ERISA's fiduciary rules. These rules require that plans be operated solely in the interests of participants. The Labor Department, IRS and PBGC have several criteria for diligent searches when participants or beneficiaries cannot be easily located. In contrast, unclaimed property programs will accept participant accounts from employer plans when participants do not respond to a letter sent to the last known address.

This minimal search is far less than the searches required by the agencies.

Additionally, the Labor Department has standards for disclosures and procedures for challenging the correctness of the amounts credited to an account. Employer plans are responsible for maintaining participant and beneficiary information and providing benefits when they are due. And importantly, money must be prudently invested. By contrast, none of these ERISA protections apply to funds transferred to State programs, which typically do not credit interest to an individual's account.

Once money is transferred out of the ERISA system, employers are no longer required to maintain the records of former participants and their beneficiaries. As a result, participants who locate a former employer could find that there is no longer a record of their account. Employers have beneficiary information and insurance records for participants that could get lost in a transfer to a State fund. In addition, beneficiaries, such as widows and former spouses, have rights under ERISA that may not be recognized by all States.

Equally important, the ERISA agencies have established rules for tax-free rollovers between employer accounts and between employer plans and IRAs. This enables participants who are able to find their benefits to combine those savings with other employer accounts or IRAs without paying taxes. Combining accounts can reduce fees and charges and improve investment returns. Accounts transferred out of ERISA plans into State programs could be subject to several types of federal and state taxes, including the 10% federal penalty tax for early distributions.

There are important practical drawbacks to reliance on State unclaimed property programs. Typically, the first place participants look to find their benefits is with their former employers. Relatively few

³ Government Accountability Office, RETIREMENT ACCOUNTS: Federal Action Needed to Clarify Tax Treatment of Unclaimed 401(k) Plan Savings Transferred to States, GAO-19-88, January 2019, page 13. <https://www.gao.gov/assets/700/696525.pdf>

⁴ GAO p.32. With a reasonable interest rate an account of \$2,643 of a younger worker aged 18 to 20, can grow to \$85,857 by retirement age.

individuals think to look to a State unclaimed property fund for retirement benefits earned under a federally regulated retirement scheme. Our experience is that participants who cannot find their former employers are likely to contact the Labor Department, the PBGC, the pension counseling projects, or our office.

Even if participants are advised by a government agency or a counseling project to contact a State unclaimed property program, there is no clear process for determining which State fund may have a participant's account. Usually, the residence of the person at the time the property was transferred controls. But a former employer sending an account balance to a State fund may send it to a State where the participant no longer lives. Alternatively, employers may transfer accounts to the State of the employer's address. However, employers also change names and addresses. A current address for an employer could be different from the employer's address at the time a participant separated from service. This is particularly true of small businesses. Employers can also have a legal address of incorporation that is different from their locations making it difficult for a former participant to find them.

Finally, the 51 unclaimed property funds are varied in their rules and practices. Although the National Association of Unclaimed Property Administrators (NAUPA) is attempting to establish uniformity in the State funds according to earlier statements before this Council, the fact remains that important variations in State funds remain. For example, ten States do not participate in the MissingMoney.com database established by NAUPA.⁵ Similarly, State success rates and methods for locating missing account owners vary. The Council heard in earlier testimony that recovery rates for missing account owners in 42 States varied from as little as 2.27% to 88.8%.⁶

There is a better solution to the uncashed check problem

After studying the challenges presented by uncashed checks, reviewing the statements of other witnesses, consulting with counseling project attorneys, and talking with NAUPA officials, we have concluded that, although State unclaimed property programs are very helpful to individuals who have lost track of non-retirement assets, they are not the best arrangement for people who have earned 401(k), pension, profit sharing and other retirement plan benefits. A far better approach would be if a federal agency were designated as the repository for uncashed checks. The PBGC is the logical choice since the agency already has extensive experience managing its successful programs for terminating plans and has a website that is very user friendly.

The recently adopted PBGC program for missing participants in terminated defined contribution plans could easily be expanded in the following manner:

- Employers terminating a defined contribution plan who are unable to find a participant after a diligent search could be required to transfer the account balance to the PBGC.
- Employers with missing participants from active defined contribution and defined benefit plans could be required to list the names of persons missing after a diligent search. However, employers of active plans could be given the option of keeping the missing participant's account balance in the plan or transferring the money to the PBGC. Participants searching for benefits would be able to check the missing participant database for the location of their

⁵ Testimony of Mark William Bracken, Assistant Treasurer, Commonwealth of Massachusetts

⁶ Testimony of George Sepsakos and Kevin Walsh, Groom Law Group.

benefits. Participants who are not listed on the database would know that their former employer is still in business and will likely be holding the benefits for them.

- Employers making distributions of small account balances of \$5,000 or less could be required to report the names of missing participants and the locations of their account balances to the PBGC. The PBGC could be authorized to receive amounts equal to uncashed checks resulting from forced transfers of \$1,000 or less, and to list the names associated with the small accounts on the PBGC's missing participant searchable database.⁷

The PBGC would be the best location for a comprehensive missing participant database since it already maintains both a mandatory database for participants in terminated defined benefit plans and a voluntary database for missing participants in terminated defined contribution plans. An expanded PBGC program could be authorized by legislation or by guidance from the agencies.

The costs of running the expanded program could be covered by investment earnings from the money in the accounts (over and above specified interest payments to participants and beneficiaries) plus forfeitures resulting from account balances that are never claimed.

In a 2014 report, the GAO noted that many other countries have registries that address not only the problems plans have in locating missing participants, but also the problems that participants and beneficiaries have in finding their lost plans.⁸ A national retirement plan registry with a searchable database for locating employers and their plans would complement an expanded PBGC missing participant program. The GAO recommended that the Labor Department establish a task force to consider establishing such a registry. We second that recommendation and suggest that the task force also include representatives from the PBGC and IRS.

I would be happy to answer any questions you may have.

⁷ Such a program could also be helpful to the Labor Department's efforts to encourage third party administrators to voluntarily undertake to distribute assets from abandoned 401(k) plans. TPAs would be more likely to agree to take on this responsibility if they could simply transfer the assets together with a list of participants and their contact information to the PBGC.

⁸ Government Accountability Office, 401(k) PLANS: Greater Protections Needed for Forced Transfers and Inactive Accounts, GAO-15-73, November 2014 GAO-15-73