“Closing The 401(k)” - Human Resource Executive Magazine

A veteran HR professional shares her war story about handling a 401(k) plan closure during a company termination.

By Mary Steigerwalt

Imagine losing a company, a job, and a 401(k) plan -- all in one day. That's what happened to me in September 2005, when the small publishing firm where I worked (I'm withholding the name) was acquired. As vice president of operations, I became solely responsible for terminating 401(k) plans for 88 plan holders.

As HR executives know, 401(k) plan closure is a lengthy, complicated and daunting process. But the situation became more tangled when I was told I was losing my job, too -- yet still remained responsible for closing out the plans.

My experience taught me valuable lessons about plan compliance, plan closure and the importance of third-party expert help to streamline the process and sidestep common pitfalls.

And my discoveries can help other plan sponsors, no matter where they are in the termination cycle, and no matter how complex or expansive their company's cases are. By using all available resources at each step in the closure process, administrators can tap into turnkey solutions that close plans, save money and help everyone involved in the process get on with their lives.

First, some background. Our company's acquisition wasn't unusual, since the publishing industry regularly sees small firms change hands. Over my 15-year tenure, my former employer acquired eight other businesses and changed hands four times.

At the time of the final acquisition, I ran the internal workings of the company and ensured proper use of our resources to build the business. I sat on the three-member board of directors, supervised the IT department and managed the human resource, benefits, operations and payroll functions.

This comprehensive view of the organization gave me unique insight into, and experience with, transition processes, especially for the HR and benefits functions.

Tackling the Process

Traditionally, when the company ownership changed, the acquiring company would determine whether it was interested in taking on the risk of receiving plan funds from another employer. Some plans allowed the direct rollover to the new company's plan, but some acquiring companies preferred to let the previous owner terminate the plan and distribute the assets first -- a much longer and more complex process.

I hoped for a direct rollover during our final acquisition. Instead, it was our acquiring organization's policy not to take on the 401(k) plan of firms it bought. I was told I needed to start terminating my company's 401(k) plan immediately.

Before I could tackle the closure process, I had to verify that my plan was in compliance. Many companies neglect ongoing compliance efforts -- an oversight that will haunt them when plans are forced to close. With the appropriate measures up-front, however, administrators can maintain compliance, stay prepared for 401(k) closure and avoid costly, time-consuming mistakes.

One practice is to leverage record-keeper resources. I immediately called our record keepers when I found out our plan was closing, explained the situation and asked for guidance. They responded with a package of materials that outlined the steps for plan termination. They also advised me to consult an Employee Retirement Income Security Act attorney to ensure I met all the requirements.

Strong record keepers make administrators' jobs easier in the plan-management phase by keeping track of regulation changes and managing any necessary plan-document modifications. This ensures that each new regulation is fulfilled correctly, completely and on time.

However, record keepers don't monitor every plan detail, so administrators must remain diligent. A good example of how an administrator can fall short of keeping his or her plan compliant is by not making contributions on a timely basis, according to guidelines set by the Internal Revenue Service and the U.S. Department of Labor. This type of mistake can cause prohibited transactions, which further complicate plan termination.

In the event of a prohibited transaction, administrators are required to make up whatever money a person could have potentially lost. They must also report that information to the Internal Revenue Service on a form and pay a penalty. The task of processing a prohibited transaction can be costly, especially with any additional legal advice.

Maintaining testing requirements is another way to remain compliant during plan management. For example, administrators must conduct a lengthy calculation for the ACP/ADT test, which is based on employee compensation and contributions to the 401(k) plan. The test guarantees that a 401(k) plan does not benefit the highly compensated employees more than the non-highly compensated employees.

The final compliance practice: filing Form 5500 with the Department of Labor, which reflects the characteristics and operations of employee benefit plans, including 401(k) plans.

By following up on a regular basis and rigorously meeting requirements, administrators minimize their risk of disqualifying the plan, harming participants and further complicating 401(k) closure when the time comes.

Third-Party Support

Thanks to my long-term plan management, and the ongoing help of my record keeper, my plan was up-to-date and in line with government regulations. I was ready to tackle the plan-closure process. But managing the process for a defunct company while job hunting proved difficult and time-consuming.

My situation wasn't unique. The termination of a 401(k) rarely comes as a surprise to the people who manage the plan, as it's likely they're moving into a new company and new position, or out looking for work. And even if these administrators have the time and resources to spend on terminating the plan, they're considering their personal futures too.

To make matters worse, many plan sponsors are facing plan closure for the first time, and simply don't know what they're doing. Without any foresight, administrators often flounder in inefficiency, lack of compliance and incorrect termination, which wastes valuable time and money.

I went through plan closure during a previous acquisition, so I understood the challenges ahead. But I wasn't willing to undertake the entire process on my own. Doing so would likely complicate the procedures and increase the rate of plan abandonment.

I had also promised the company's former owners that I would help them through the termination process, even as I looked for another position. The issue was further complicated when one of the former owners was stricken with brain cancer and could not perform his trustee duties during his illness.

With such limited time and resources, I recognized the need for help, and wanted to take advantage of expert assistance through a qualified third-party solutions provider -- an encouraged best practice for plan closure. I enlisted Keane Organization Inc. to lend its resources to help me quickly terminate the plan.

Indeed, third-party expertise can help administrators of any experience level achieve a successful plan closure, and smooth out the termination process at each stage:

1. Terminate qualified plans. Plan sponsors can determine termination eligibility of idle plans in two ways. They can get an IRS opinion on a plan's eligibility or their company's board of directors can mandate the termination, with or without IRS approval.

Sponsors must also review any available documents, including signed plans, board resolutions and joint survivor benefits. This ensures all dates and terms are clear and accurate, and that all required testing and filing has been conducted over the years.

My due diligence with compliance efforts saved us some work when the board of directors and I chose not to file for the IRS determination letter. Based on my ERISA lawyer's advice, we decided that the compliance issues were fully addressed and that filing for the letter would extend the already long process.

If sponsors aren't already compliant, third-party solution providers can step in and manage the review process. They can implement assessment questionnaires at the outset to create a snapshot of what problems and situations exist for the plan sponsor. Keane, for instance, provides a proprietary product that helps measure, manage and monitor the requirements of a compliant 401(k) plan.

This crucial step also helps the third-party provider complete the document review process faster. If important items such as board resolutions are not in place, third parties can provide consulting services to obtain the documents.

All bases are covered by the end of the review, and sponsors have an accurate, compliant foundation for the rest of the closure process.

2. Contact residual plan holders. The next step is to reach plan holders with a comprehensive packet of information that states the plan blackout date, and to request a response regarding desired asset distribution. Mass mailings are usually the only way to locate plan participants with remaining assets, and inform them of the decision to terminate.

In my case, I also reviewed the plans for outstanding loans and sent notification letters. These included information on paying back the loans, collecting assets or allowing the loans to default, which creates tax issues for employees with outstanding loans during plan termination.

However, communicating with the plan holders required more time and energy than I anticipated. I struggled with many logistical details, such as finding missing participants, updating records, sending information, getting new addresses and filing unclaimed property reports to the states.

Since I worked directly with many of the plan participants for years, I foolishly thought I knew where every participant in the plan lived. I failed to recognize that some employees and former employees did not update their address information as required.

A common mistake of administrators is assuming that once you know where to find plan holders, they will immediately complete the paperwork and request their distribution. Finding the participants was only half the battle; the other was getting people to complete their paperwork. Even people with large balances ignored the mailings and notifications, and had to be called.

Other common problems included undeliverable mail and non-responses, and fielding numerous follow-up mailings and phone calls with questions and concerns from plan holders. Moreover, I was devoting 15 to 20 hours a week (many on nights and weekends) to plan-closure activities.

Keane eliminated this burden by managing the mailing, compiling the necessary information and fielding all distribution requests. Herein lies solution providers' value: They have the resources to track down correct addresses or non-responding plan participants.

In addition, they can handle all participant communication, answering any questions, and walking the holders through the distribution elective process. This accomplishes the task in significantly less time than a lone plan sponsor ever could.

3. Distribute the assets. In this final step, not everyone involved is under the same pressure to terminate the plans. Some record keepers leave their billing system turned on, regardless of long periods of inactivity or large numbers of missing participants. They can charge an annual fee as long as they hold on to the assets. Thankfully, our record keeper was interested in helping with the transition, and was not focused on retaining the assets or fees.

Plan sponsors then have to consider what is in the best interest of the participants and the plan. In my case, the terminating company decided to pay the costs of closing the plan directly from the assets of the company, and not from the assets of the participants. It was always our philosophy that the plan was created to benefit the employees. Therefore, it made sense to have the fees paid by the company.

This stage also requires cooperation among record keepers and asset trustees to distribute the money after receiving all distribution directions and electives. Sponsors must remember that every cent must be distributed before the plan is closed. This means companies shoulder the burden to make sure all checks are cashed, including any for residual interest.

Here, a third-party solutions provider helps prevent any logistical nightmares in coordinating all the different groups and ensuring that checks are cashed. If the checks are not cashed within a certain time period, providers can leverage their legal expertise to escheat the assets to the state as unclaimed property. This protects the money in the name of the plan holder for perpetuity, and lets the record keeper close the plan.

In either case, providers must keep meticulous, detailed records of the account, because if even one penny is owed, they cannot terminate the plan.

In Closing

Remember those 88 accounts I had to close? Thanks to outside support, I wrapped up the process by January 2006. That's only four months -- nearly a quarter of the time it would have taken on my own.

As it turned out, the 401(k) closure process and my job hunt ended with Keane's arrival. (I ended up joining Keane toward the end of the process.) For me, getting a job through plan closure was a bonus. For HR professionals, the ultimate reward will be filing their final tax forms and officially closing the plans. The relief and satisfaction will be palpable when they can rest assured that their company was compliant, assets were returned and a thorny, expensive issue was resolved quickly and affordably.

Mary Steigerwalt is executive vice president of business solutions for Wayne, Pa.-based Keane Organization Inc., a provider of compliance and risk-management solutions to large corporations, mutual funds and financial institutions.

February 1, 2007