How to Successfully Manage a 401(k) Plan Closure

Real-life advice and best practices from a veteran HR professional and retirement services consultant.

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 was acquired. As vice president of operations, I became solely responsible for terminating 401(k) plans for 88 plan participants.

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 a third-party expert's help to streamline the process and sidestep common pitfalls. 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.

Dealing with Transition

There are many reasons why a company may be forced to shut down its 401(k) plan. Sometimes a company simply cannot afford to keep the plan active, due to lack of monetary resources, time, and manpower. Other issues range from low enrollment and trouble passing nondiscrimination testing, to international relocation, going out of business or being involved in a merger or acquisition. Our company's acquisition wasn't unusual. 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, the transition processes — especially for the HR and benefits functions. My understanding of how various areas within the organization functioned proved invaluable when working to close a 401(k) plan. Maintaining effective communication between many different groups, both internally and externally, is crucial to successful plan termination.

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.

Tackling the Process

Before I could begin the closure process, there were a variety of challenges I had to face. First and foremost, I had to verify that my plan was in compliance. Many companies neglect ongoing compliance efforts — an oversight that can haunt them when plans are forced to close. Continuous, proactive due diligence is essential to the successful management of any company's 401(k) plan. 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 recordkeeper 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 (ERISA) attorney to ensure I met all the requirements.

Strong record keepers and third-party administrators 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. 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. However, 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, most plan sponsors are facing a plan closure for the first time, and simply don't know what they're doing. Without any foresight, administrators often flounder in inefficiency and lack of compliance, which wastes valuable time and money.

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

With such limited resources, I enlisted Keane Organization, Inc. to help me quickly terminate the plan.

Indeed, third-party expertise can help administrators of any experience level achieve a successful plan closure, by efficiently handling the three basic stages of the termination process:

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.

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 Participants

The next step is to reach plan participants with a comprehensive packet of information that states the plan term date, 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.

Communicating with the plan participants required more time and energy than I anticipated. Often, former employees are involved, which further complicates the process. I struggled with many logistical details, such as finding missing participants, updating records, and sending information.

Because 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. It is the responsibility of the plan sponsor to track down all of these individuals, through whatever internal or external means are necessary.

A common mistake of administrators is assuming that once you know where to find plan participants, 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, non-responses, and fielding follow-up mailing and phone calls with questions and concerns from plan participants. 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 participants 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 must remember that every cent must be distributed before the plan is closed. This proves difficult when not everyone responds to the mailing and notifications. And whether it is 1 or 100 participants who have not made an election or who cannot be found, the Department of Labor has outlined required steps for both the location of missing participants and the corresponding distribution of the account balance. The steps include:

- **Use certified mail** — This is one of the most effective and low-cost ways of determining whether the participant can be located.
- **Check related plan records** — While the 401(k) may not have current address information, payroll systems, medical, or life insurance policies may have more up-to-date information that was not included in the retirement plan documents.
- **Check with designated plan beneficiary** — If a participant has named a beneficiary, plan sponsors must request that the beneficiary pass along the information to the missing participant. Plan sponsors must also consider the use of other search tools at their disposal when attempting to locate a missing participant. These tools range from letter-forwarding services to Internet searches and credit reporting agencies.
- **Distribution options** — For the plan to be closed, sponsors must ensure that a distribution option is decided upon for every participant. These options include rollovers into individual retirement plans, establishing a federally insured bank account in the name of a missing participant, or escheatment to state unclaimed property funds.

I was fortunate in the process in that I didn't need to take all of those steps, as we were able to obtain distribution elections from many participants, and cash out those remaining who had under $1,000 in the plan. Following the four steps can be very cumbersome, requiring a number of sub-steps which can lengthen the process of terminating the plan- all the more reason for providers to remain in compliance and 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 me on my own. In the case of any plan termination, it is important to realize the many risks and challenges associated with the process. Attention to detail, comprehensive communication efforts, staying in compliance, reviewing all necessary documents and procedures, finding missing participants, and finally distributing all of the plan assets are all critical elements of a successful 401(k) closure.

For most HR professionals, the ultimate reward will be filing their final tax forms and officially closing the plans. The relief and satisfaction was palpable when I could rest assured that the company was compliant, assets were returned, and a thorny, expensive issue was resolved quickly and affordably. For me, there was duel relief. My 401(k) closure concerns and my job hunt both ended with Keane's arrival — I ended up joining their team shortly thereafter.

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