

Hunting for Retirement Plan Participants? New IRS Guidance and the Expanded PBGC Missing Participants Program Should Help

By Brian G. Belisle, Esq. and Seth I. Corbin, Esq.

Plan administrators might feel it is the participant's responsibility to keep a plan administrator informed of their address changes; however, it is the view of the Department of Labor (DOL) that a plan administrator's failure to take reasonable steps to locate its participants is a breach of fiduciary duty. In addition, the IRS may disqualify a retirement plan that fails to make required minimum distributions to its participants or beneficiaries who cannot be located. Missing or non-responsive participants also create issues when trying to terminate a plan and distribute all of its assets.

The DOL has reportedly commenced a national audit campaign targeting plans with missing participants, and just last month, the Pension Benefit Guaranty Corporation (PBGC) issued final regulations expanding its existing missing participant program (previously limited to certain defined benefit plans) to a defined contribution plan.

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The DOL has been very aggressive in a number of plan audits, asserting not only breaches of fiduciary duty, but also prohibited transactions where, in accordance with plan provisions, the benefits due to unresponsive or missing participants or beneficiaries are forfeited. Although the IRS routinely approves plan language permitting forfeiture of retirement benefits of missing participants or beneficiaries, subject to reinstatement upon a subsequent claim for benefits, the DOL has the authority to determine a plan administrator's compliance with the fiduciary requirements of ERISA.

The DOL, in FAB 2014-01, provided some guidance on locating missing participants in connection with the termination of a defined contribution plan. In this situation, the DOL noted that a plan fiduciary must, at a minimum:

- Check the records of the employer and any related plans of the employer;
- Check with the designated beneficiary of the missing participant;
- Use free internet search tools; and

- If none of the foregoing is successful, then, after considering the size of the account balance and the cost of additional search efforts, consider use of commercial locator services, credit reporting agencies, information brokers, investigation databases, internet search tools and similar services that may involve charges.

Pending additional guidance from the DOL, a plan fiduciary should consider following the steps outlined by the DOL in FAB 2014-01.

The IRS addressed the issue of locating missing participants when auditing a plan's compliance with required minimum distributions following a participant's attainment of age 70½, or death. According to an October 19, 2017 IRS directive to its audit personnel, the IRS will not challenge a plan's failure to make required minimum distributions to a missing participant or beneficiary if the plan administrator has taken all of the following actions:

- Searched all of the records of the plan, related plans and the plan sponsor;



- Searched publicly available records or directories for alternative contact information;
- Used either a commercial locator service, credit reporting agency or proprietary internet search tool; and
- Attempted contact via United States Postal Service certified mail to the last known mailing address and through appropriate means for any address or contact information, including email addresses and phone numbers.

Plan administrators should routinely determine if there are missing or non-responsive participants or beneficiaries and attempt to locate them. If a third party performs these services, the plan administrator should review their processes to make sure they are adequate.

The recent expansion of the PBGC program should also be welcomed news for plan sponsors and plan administrators terminating defined contribution plans in 2018 and beyond (the expanded program is generally not available to plans terminated prior to January 1, 2018). The new PBGC program is only available to defined

contribution plans that are being terminated. Plan sponsors have two options when going to the PBGC: (1) elect to be a “transferring” plan, which means that the plan transfers *all* of its benefits to PBGC for distribution to participants; or (2) elect to be a “notifying” plan, which means that the PBGC is simply provided information regarding participants’ accounts. Further, plan eligibility is contingent upon the eligible defined contribution plan conducting a diligent search for each missing participant within the nine month period ending on the date application is made to the PBGC to participate in the program.

In order to take advantage of the expanded PBGC program, plans must file a form with the PBGC (Form MP-200 and either Schedule A or Schedule B, depending whether the plan is a “transferring” or “notifying” plan). There is an administrative fee for accounts in excess of \$250, which may be able to be paid from participant accounts and/or the plan’s forfeiture account.

Plan administrators need to be both proactive and creative in their attempts to locate missing

or non-responsive participants or beneficiaries. This may include searching social media sites, as well as contacting former employees who worked with the participant. Further, the steps taken to locate a missing participant or beneficiary must be documented and saved as proof of compliance with the administrator’s fiduciary duties under ERISA and the tax law requirements to provide required minimum distributions to participants and beneficiaries on a timely basis. Certainly, if a plan administrator is interested in applying to the newly available PBGC program, this evidence will be necessary to satisfy a plan’s eligibility requirements to participate in the program.

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Employers Who Didn’t Play (in 2015): Be Prepared To Pay

By Jessica Forbes Olson, Esq.

Applicable large employers (ALEs) with 50 or more full-time employees who didn’t offer good enough, cheap enough coverage (i.e., minimum essential coverage that is minimum value

and affordable) to enough of their full-time employees (70 percent in 2015) may receive Letter 226J from the Internal Revenue Service (IRS). The notification is sent to employers whom the IRS believes

may owe an employer shared responsibility payment (ESRP) (“pay or play penalty”).

If you receive Letter 226J, you will want to take the following steps immediately:

- Determine when your response to the IRS is due (it will be 30 days after the date of the IRS letter and should be listed on the first page of Letter 226J);
- Gather copies of Forms 1094-C and 1095-C and determine if you agree with the IRS' determination; and
- If you agree with the proposed ESRP, you will need to complete the enclosed Form 14764 (ESRP Response) and include the payment (or pay electronically).
- If you disagree with the proposed ESRP:
 - Complete the enclosed Form 14764;
 - Include a signed statement explaining why you disagree with the proposed ESRP;
 - Consider including documentation supporting why you disagree with the proposed ESRP (e.g., payroll tracking information to prove certain employees were not full-time employees);
 - If necessary, revise the Employee Premium Tax Credit Listing that sets forth employees who received a premium tax credit (that ultimately triggered the ESRP); and
 - Whether you agree or disagree, ensure that all documents submitted include the tax

year (2015) and employer ID number in the top right corner.

If in the process of responding to Letter 226J you determine that you made errors in the Form 1094-C authoritative transmittal or Forms 1095-C, you should not enclose corrected returns with your response. Separately, however, you will need to correct any filing errors and submit them to the IRS as soon as possible and furnish any corrected Form 1095-C to the applicable employee.

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A Better Business Succession Mousetrap: A New Way To Fund and Utilize Buy-Sell Insurance

By **Harvey M. Katz, Esq.**

One of the most commonly used techniques to provide liquidity for closely held businesses is to insure a buy-sell arrangement on behalf of its owners. Buy-sell arrangements typically come in two varieties: redemption and cross-purchase. Either type can be funded with life insurance, but both types of arrangements and the associated funding of those arrangements suffer from the same infirmities.

In the first case, the insurance purchased for either type of

arrangement is not a deductible corporate expense. Unfortunately, term insurance is not always the most appropriate vehicle to fund a buy-sell, as it is possible for the insured to outlive the policy term. The alternative, non-deductible universal or whole life, is simply too expensive in too many instances. As a result, too many arrangements are simply unfunded either at inception or as a result of a principal outlasting the term of affordable term coverage.

However, most buy-sell arrangements, particularly on behalf of businesses with two or three owners, suffer from a more fundamental defect. Few arrangements address the future of the business after the death of the second owner. In a sense, a funded buy-sell arrangement often masks the underlying problem: a lack of a true business succession plan.

In the author's experience, efforts to fund a buy-sell through a retirement plan are complicated and unwieldy.

For reasons beyond the scope of this article, use of a defined benefit plan for this purpose is unworkable. The only possible alternative is a profit-sharing plan where each employee has the option of electing purchase of life insurance with those funds in his or her account. However, these purchases are subject to the “incidental benefit” limitations, which limit the amount and types of funds that can be used to purchase life insurance. In general, less than 50 percent of a participant’s account may be used to purchase whole life insurance and no more than 25 percent can be used to purchase term or universal life insurance. In most cases, it is simply very difficult to fund a sufficient amount of buy-sell insurance with the amount of permitted under the incidental limitations.

However, there are exceptions to the foregoing limitations. Funds that have been “aged” in a profit-sharing plan for two or more plan years, rollover funds and funds that are subject to immediate in-service distribution may be used to purchase life insurance without limit. So virtually any effort to use profit sharing funds to fund a buy-sell must utilize one of these exceptions. Unfortunately, these days most profit sharing plans have a 401(k) component whereby participants, including the owners, defer part of their own salaries into the 401(k). In most cases, 401(k) elective deferrals cannot qualify for use

under these exceptions. In addition, many 401(k) service providers will not permit participants to purchase life insurance as part of their investment portfolio.

There is another disadvantage to the use of incidental benefit life insurance in a qualified plan: the “economic benefit” costs, formerly known as P.S. 58 costs. Under the so-called “economic benefit rule,” participants on whose life insurance is maintained must report, as current taxable income, the value of the life insurance protection maintained on their behalf. These costs are generally determined by use of IRS Table 2001, which applies the one-year premium term rate or the insurance company’s alternative term rates. This requirement, in effect, renders a portion of the cost of the arrangement an after-tax expense to the participant.

The mechanics of an arrangement require that the arrangement among partner/shareholders be structured as a “cross-purchase” arrangement. Each “key” employee maintains insurance on the life of others and upon the death of one of the key employee, insurance proceeds are paid to the accounts of the other key employees. Distributions from those accounts to those individuals can be used to purchase the shares of the deceased key employee.

Key person life insurance is simply a better alternative, which is permitted in qualified plans under Revenue Ruling 54-51. The insurance is a

general investment of the trust, not dedicated to the account of any participant. As a consequence, there are no economic benefit costs to be paid. There are no incidental benefit limitations, although investments are generally limited to employer contributions (as opposed to employee elective deferrals). Clearly, the combination of fewer restrictions on the amount of insurance that may be purchased and better tax treatment makes key person strategies a better choice.

However, different mechanics are required to monetize the proceeds of a profit-sharing plan. Because the insurance proceeds are allocated to the accounts of all participants, it is the profit-sharing plan that will purchase the proceeds. Under Section 407 of ERISA, any profit-sharing plan that is an “eligible individual account” plan may invest up to 100 percent of its assets in employer securities. The only restriction is that the qualified plan pay no more than fair market value for the shares purchased.

A casual observer may have concerns over the purchase of part of the company by a profit-sharing plan, effectively converting it into an employee stock ownership plan (ESOP). However the profit-sharing purchase is, in reality, a beneficial element of a true business succession plan. It is a key opportunity for a business owner to begin the process of transferring leadership of the company to a new generation, while simultaneously

realizing a fair value for the business. The bottom line is that acquisition of the remaining shares by one or two individuals with a presumably short career is simply not a viable business succession strategy. While a discussion of the advantages of ESOPs as a tool to incentivize employees is beyond the scope of this article, it is sufficient to say it could lead to a far better result than the use of insurance proceeds to fund a purchase by a one or two surviving partners/shareholders model.

The sale of a significant percentage of the business to the profit-sharing

plan presents a golden opportunity for the company to develop new talent and reward and incentivize employees. This talent will be in place after the death of the first key employee and ideally will be able to take over operation of the company upon death of the second (or third) owner, after sale of the remaining shares of the ESOP. More importantly, an employer who shares these plans with its employees can use plans for an eventual sale of the company to employees as a tool to recruit and retain key talent.

The final and perhaps most valuable advantage is that once the entire

company is sold to the ESOP, it may be able to elect subchapter S corporation status and operate as a tax-free company. In doing so, the future of the company and the employment of its employees is assured. In effect, the company is creating its own buyer, which is the best way to ensure its future.

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Avoiding the Accidental MEWA

By **Stephanie M. Moscetti, Esq.**

MEWAs, or Multiple Employer Welfare Arrangements, are plans that cover the employees of two or more unrelated employers but do not include plans operated by employers under common control or are maintained pursuant to a collective bargaining agreement. While MEWAs occupy a small segment of employer-sponsored health plans, plan sponsors can easily and inadvertently create a MEWA that is subject to increased regulation and enforcement. This article discusses the history of MEWAs and highlights plans that should be reviewed closely to avoid being unintentionally classified as a MEWA.

History of MEWAs

MEWAs originated to provide small employers access to affordable health care coverage for their employees. By pooling risk across multiple employers, MEWAs have a lower underwriting risk and are eligible to purchase a more affordable policy from a health insurer. Historically, promoters of these arrangements have argued they were subject to ERISA and exempt from state insurance regulation. As a result of ERISA preemption, MEWAs avoided state reserve and contribution requirements. While many MEWAs provided

the promised benefits, others were unable to pay claims due to insufficient funding or reserves. In some circumstances, employers realized too late that the promoters drained the plan's assets through excessive administrative fees or embezzlement.

In response, Congress amended ERISA in 1983 to grant states the power to enforce state insurance laws against MEWAs, regardless of whether the MEWA was self-funded or fully-insured. Even with the amendment, MEWAs often remained underfunded and susceptible to promoters' fraudulent practices. Because of

the high propensity of abuse, the Patient Protection and Affordable Care Act, among other things, expanded the Department of Labor's (DOL) reporting program (Form M-1) and gave the Secretary of Labor additional enforcement authority when confronting a fraudulent or severely underfunded plan.

Accidental MEWAs

To become a MEWA, a plan needs only to cover employees of two or more employers. Because intent is irrelevant, an employer can find itself inadvertently creating a MEWA if it allows employees of other employers or non-employees to participate in its welfare plan. For example, if an employer allowed its independent contractors to participate in its welfare plan, the plan would be classified as a MEWA. Or, in the context of a corporate transaction, an employer could create a MEWA if it allowed employees who were transferred to an unrelated buyer to stay on the seller's medical plan.

Once a MEWA, a plan can face penalties of more than \$1,500/day for failing to timely file the DOL's Form M-1, regardless of whether the plan administrator was aware of the requirement. Further, the plan would be subject to state laws and state enforcement, leading to a greater administrative burden requiring the reconciliation of federal and, potentially, multiple states' laws.

Professional Employer Organizations (PEOs), Staffing and Leasing Companies

Often businesses look to Professional Employer Organizations (PEOs) and/or staffing and leasing companies for cost-effective labor or to outsource certain business functions.

Generally, the leasing firm is responsible for paying the leased employee and providing benefits. In many circumstances, however, the recipient business controls and directs the work performed. Depending on the extent of the relationship, the recipient business may be considered the common law employer of the leased employee. The leasing company would then be providing benefits not only to its own employees but to employees of other employers (e.g., the recipient business). If the leasing company is not a common law employer or joint employer of the leased workers, the leasing company's plan would be covering employees of two employers, so it would be classified as a MEWA and subject to M-1 filing and state regulation.

Given that these types of arrangements can quickly turn a single-employer plan into a MEWA, PEOs, staffing and leasing companies should periodically examine their plans, including eligibility criteria, as well as the relationships between their leased employees and recipient businesses. This situation is not limited to organizations explicitly

defined as PEOs, staffing or leasing companies. Other similarly structured businesses should also consider reviewing whether their plans fit the criteria of a MEWA. The consequences of maintaining a MEWA without knowing it can be expensive with no opportunity to remedy late filings.

Associations

Association Health Plans (AHPs) are another arrangement where employers inadvertently enter into a MEWA. Originally devised as a way for small businesses to obtain affordable health care coverage for themselves and their employees, AHPs are receiving more attention due to a recent [Executive Order](#) (October 12, 2017) and [Proposed Regulations](#) (January 5, 2018). In these arrangements, small businesses purchase health insurance by banding together through bona fide trade and/or professional associations. Many professional or trade associations were created to further common interests and incidentally offered AHPs as a benefit to their members. Other associations were created for the purpose of selling health insurance. Generally, member-employers pay premiums/contributions to the association and the association either purchases a fully-insured health plan from an insurer or self-funds a plan. However, since the AHP would be covering employees of multiple employers, the AHP would be classified as a MEWA, and subject to the additional regulation.

For Your Benefit

The recent proposed regulations reiterated that AHPs would retain their MEWA status and be subject to state insurance laws, pending further guidance. Until DOL issues additional guidance, employers and associations should review their plans and confirm they are complying with applicable state and federal laws, including the Form M-1 filing.

While MEWAs can certainly be a useful arrangement, they should be entered into knowingly, with full understanding of the increased scrutiny and administrative burden. Plan sponsors should review their plans and eligibility requirements to confirm their status as either a single-employer plan or MEWA. Plan sponsors concerned with or unsure about

their status should contact legal counsel to determine how to best structure their plans.

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