TESTIMONY ON BEHALF OF EMPOWER RETIREMENT BEFORE THE ERISA ADVISORY COUNCIL ON PERMISSIVE TRANSFERS OF UNCASHED CHECKS FROM ERISA PLANS TO STATE UNCLAIMED PROPERTY FUNDS AND OTHER METHODS OF DEALING WITH UNCASHED CHECKS

My name is William Jeffries, and I am Vice President of Operations for Empower Retirement. Empower provides recordkeeping and other services to approximately 38,000 plans and 9.2 million participants.[1] We serve plans of all sizes from startups to plans with over 220,000 participants. Our clients include ERISA covered plans as well as non-ERISA governmental or 403(b) plans. We appreciate this opportunity to provide testimony on a topic that is of great concern to us as well as the plan fiduciaries and participants we serve.

I understand that the focus of your inquiry is on how uncashed checks for missing or unresponsive participants are handled, and in particular, our experience with using state escheatment as a solution, and that you are not seeking testimony on efforts to locate participants. My comments will address your specific inquiry.

Empower's experience in general

I would like to start by defining the problem as we experience it at Empower. Uncashed checks occur almost exclusively in situations where either a participant has neither requested nor consented to a distribution, or the check represents trailing funds after the bulk of the account has been paid out (Unrequested Funds). Checks are sent without consent either because the amount is less than $1,000 and the plan document requires those amounts to be cashed out, due to the Internal Revenue Code's required minimum distribution rules, or because the plan document requires distribution of benefits at normal retirement age. Trailing distributions occur due to allocations made after an account has been distributed and come from a variety of sources, including forfeiture allocations, loan repayments made in error and earnings and other trailing allocations. In 2018, we processed over 3.5 million distribution checks to plan participants of which approximately 15% represented Unrequested Funds. Five percent of all the distribution checks issued are either returned due to an incorrect address or simply not cashed. Significate portions of these uncashed checks are associated with Unrequested Funds. The average dollar amount of checks returned or ignored is $348, however; 49% of the uncashed checks are less than $25.

Once it is determined that a check will not be cashed, a variety of steps are taken, some of which we implement automatically (such as not sending additional mail or checks to an address we know is no longer valid) and some of which are selected by the plan sponsor fiduciary. Due to the focus of this inquiry, I will not describe those processes, but will jump to what happens once it has been 180 days since a check was issued but remains uncashed.

We offer our plan sponsor clients three different methods for dealing with these funds, and I will now describe each of those methods and any information we have on their success in reuniting participants with their retirement accounts. We also offer clients the opportunity to use an alternative method of their choosing and some clients, particularly our largest clients, choose to implement their own solution.

The first two methods we offer both involve a solution where we maintain a plan level unclaimed property account where funds are held and data is maintained to allow repayment to the participant or beneficiary if they are found. These funds are invested in in the same investment option as the plan's forfeiture account unless the plan sponsor directs otherwise. The differences between the two unclaimed property account options we offer have to do with how frequently deposits are made and who is responsible (the client or Empower) for tracking and maintaining data on the accounts and is not directly relevant to your inquiry. Our success rate in reuniting participants to their benefits using either of these methods is 15-20%. The larger the value of the uncashed check, the more success we see.

Empower experience using state escheatment

The other method we offer is state escheatment. The vast majority of our small plan clients use this method as well as our non-ERISA plans. Approximately 28,000 of our plans utilize escheatment of which 20% represent non-ERISA plans.

While the process each state uses is different, we are typically required to send a notice to the payee prior to remitting funds to the state. Many states set a dollar limit under which notice is not required, typically $50. For the period January 1, 2013, through June 30, 2019, we processed 152,815 uncashed checks totaling $31,752,027 of which 39,266 or 26% met the dollar threshold requiring notice. When notice is required we conduct an electronic search using a commercial locater service and send a letter explaining what will happen if funds aren't claimed by a certain date. Of the payees receiving our notice, 26.6% are paid out and those tend to represent accounts with higher balances (44.22% of dollars involved). Out of the $31.7 million processed using the state escheatment method, only $17.7 million was escheated to the states treasuries, while the remaining $14 million was paid out to the original payees.

It is also significant to note that out of the 152,815 checks processed using the escheatment solution, 39% were for amounts under $5. The reasons why there are so many unclaimed checks for such small dollar amounts vary but often involve situations where a person's benefit was distributed and the check was cashed but there are trailing amounts due to earnings, forfeiture allocations, loan repayments made in error or other trailing allocations, and the participant doesn't consider the amount of the check worth the bother of cashing it.

Each state has different rules in terms of how long funds must be held unclaimed before they can be turned over, whether and what kind of notifications are required and their timing, what date the unclaimed funds should be submitted to the state, and what information in what format to provide to the state. While this presents potential complexities in using the escheatment method, we have built bridges between our recordkeeping system and the unclaimed property system (a third-party system), which allows us to handle the process in all 50 states so all of our clients, including those with a multi-state presence, can readily use it. We developed this functionality in part because we serve a high volume of non-ERISA plans and also to meet state insurance requirements.

The waiting period for funds to be escheated ranges from three to five years. Once funds are escheated to a state, we do not have data on the number of accounts that are restored to their original owner.

Tax withholding

On a final note in terms of describing our process, you asked about how tax withholding rules and the option to rollover works in the context of uncashed checks.

We initiate income tax withholding as required by state and federal laws at the time a check is issued. We also prepare Form 1099s to report funds distributed and any amounts withheld in the year the check is issued. We follow the same process regardless of whether the check is cashed. If a participant objects to paying tax on money they did not receive and/or did not cash, they address this issue directly with the IRS. This approach is consistent with recently issued IRS guidance in Revenue Ruling 2019-19. It is also the method least likely to add significant costs to be borne by other participants, as I will explain.

After a disbursement is completed, our recordkeeping system sends the data to our tax reporting system. Specifically, after money goes uncashed we do not track sources (pretax, Roth, after tax, etc.), cost basis, or other data necessary for accurate tax reporting. The money is moved into an omnibus account and just the value is tracked. To handle any other way would add expense and detailed recordkeeping on a completed transaction with uncashed money. Another reason for our approach is, as I stated previously, some of these transactions are required minimum distributions where delaying the taxation and reporting would result in a significant tax penalty to the participant and potential qualification issues for the plan.

The need for a roadmap

All of the processes I've described today deal with what happens to uncashed checks and not the efforts that plan fiduciaries and others engage in to try to either locate people whose addresses are no longer valid or motivate people to cash checks they've chosen to ignore. Those efforts vary by plan at each stage of the process for dealing with uncashed checks and may include certified letters, phone calls, emails, next of kin search, use of locator services and other methods. A large segment of our small clients, (80%-90%) do not ask us for any search assistance, which may indicate they are satisfied using their own methods, with our methods or possibly that they are doing nothing. The degree of variety in what we believe we need to offer in terms of both efforts to avoid uncashed checks and methods for dealing with them is a testament to how confusing and troublesome this whole area is for plan fiduciaries. It also means that we must invest in myriad solutions in order to satisfy the wide array of legal advice our clients receive due to the lack of guidance in this area.

Plan fiduciaries need a compliance roadmap for what the Department of Labor (DOL) and Treasury consider acceptable and expected actions when dealing with missing or unresponsive participants and uncashed checks. I know that the DOL is reluctant to establish a safe harbor and concerned that it will let fiduciaries off the hook when continued efforts might have proven successful. It might also consider the fact that many fiduciaries who engage in minimal or no efforts would likely ramp up their efforts to meet the standards of an officially sanctioned safe harbor.

We believe the roadmap should support both the use of escheatment and the use of plan level unclaimed property accounts as these are the primary methods used by plan sponsors and record keepers today. State escheatment programs are designed to reunite people with funds due them and are much better positioned than employers, particularly in small companies, to deal with this issue.

The need to address small checks

Everyone's goal is obviously to pay every participant 100% of amounts due them from their retirement plan. However, there are significant costs involved in trying to accomplish this, usually in situations where a participant has either not kept their address information current or chooses to ignore checks sent in the mail. That cost is usually borne by other participants in the plan as part of a plan administration fee. When Empower conducts a search it typically consists of doing an electronic search and, if we find an address, sending a letter. If we do not find an address, we will usually look for a next of kin and send a letter to them. The cost of that search is approximately $25 per search, per participant. One of our larger clients in an industry that has experienced significant consolidation (which contributes significantly to the missing participant/uncashed check problem) has 21,951 uncashed checks of which approximately 30% are for less than $25. Each time a search is conducted the cost to the plan is approximately $675,000, which is borne by plan participants. While our smaller clients do not experience these volumes, they are very sensitive to added costs and the impact of those costs on their plan participants.

According to the SPARK Institute's study submitted to the DOL in September 28, 2018, 78% of uncashed checks are for less than $100. Plan fiduciaries owe a duty of loyalty to every plan participant, and they need guidance on how to balance the need to pay benefits against the cost to remaining plan participants. The following is a suggestion for what might provide an appropriate balance:

1. Establish a dollar amount under which no search effort is required for an uncashed check. The funds are placed in the plan's forfeiture account and allocated according to the terms of that account. No tracking is required and the participant would not have the ability to reclaim those funds. A logical threshold might be $25 since that is the cost of a search, but even a $5 or $10 threshold would significantly reduce the uncashed check problem. Text could be added to the check stub indicating that failure to cash this check will result in forfeiture of the funds.

2. Establish a second dollar amount under which a single search is conducted after which the money is placed in whatever account the plan uses for dealing with uncashed checks. The funds are tracked and can be reclaimed by the participant if they come looking for it. A logical threshold for that may be $200, which is the threshold for offering a direct rollover.

3. For all other amounts, permit plan fiduciaries to take into account the value of the benefit when determining the degree of cost and effort to incur in trying to get a check cashed.

The need to coordinate with Treasury and state unclaimed property rules

I know that the DOL has been coordinating with the Treasury Department on this issue and we encourage continued cooperation to develop standards that are, if not identical, at least non-conflicting. Plan fiduciaries need and deserve a compliance roadmap that satisfies the rules for both agencies.

We also encourage the DOL to incorporate what it has learned about state unclaimed property rules into its roadmap in order to facilitate better coordination and make it easier for plans to use the escheatment option.

Thank you again for this opportunity to testify and I remain available both today and at any point in the future to answer any questions you may have.

1 As of March 31, 2019. Information refers to all retirement businesses of Great-West Life & Annuity Insurance Company and its subsidiaries and affiliates, including Great-West Life & Annuity Insurance Company of New York, marketed under the Empower Retirement brand.

Empower is a marketing name of Great-West Life & Annuity Insurance Company

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