The Growing Problem of **Un-cashed** Pension Distribution Checks

By Peter E. Preovolos, APA, AIFA, RIA

Un-cashed retirement benefit distribution checks present a growing problem for plan sponsors, institutional plan providers and third-party administrators. Current estimates place the total value of these un-cashed checks in the billions of dollars. And proper management of these assets represents but one of many problems – including 1099R preparations, tax withholding, recurring benefit payments, escheatment issues, and missing participant account balances – surrounding the larger issue of abandoned retirement plans. Within the last five years, financial services firms have finally recognized the complexity of the problem, and have begun exploring different methods of managing un-cashed pension check funds. Yet, the situation remains unsettled at best.

Several factors are contributing to the un-cashed pension plan check problem, some of which date back to pre-ERISA times. Others, more recent, include the lack of guidance for trustees and financial institutions that serve as custodian/record-keepers, and the propensity of today's highly mobile workers to leave money in a former employer's retirement plan as they move from one job to another. To succeed, any proposed solution will need to take all these considerations into account.

THE ROOT OF THE PROBLEM

Prior to the enactment of ERISA in 1974, many major banks and insurance companies annually reported the number of un-cashed checks to all plan sponsors. Plan sponsors with large plans would usually hire a third party to audit the plan's records, including movement of money in and out of the trust. But overall, many Fortune 2000 companies recognized they had some level of oversight with regard to the movement of plan money.

After completing the audit, the auditors sent the account's trust officer a letter that did three important things:

- Identified all un-cashed checks.
- Indicated how much interest the institution owed each participant, based on current rates and how long the money was held in the institution's general funds.
- Instructed the institution to credit the participant with the proper amount of interest and return the funds back to the plan.

This proactive approach to managing un-cashed checks took place during a period when mandatory tax withholding rules did not exist. Yet, financial institutions, particularly those in the trust industry, understood their fiduciary obligation and did not balk at paying interest to plan participants. In many cases, small- to medium-size plan sponsors were not as proactive. And since the passage of ERISA, changes in government regulations as well as in the financial industry have played a key role in reshaping the un-cashed check landscape.

THE PROBLEM GROWS

Over the last few decades, the rules governing the administration and management of retirement plans and their assets have grown extremely complex. It now takes a team of experts to ensure that plans meet all of the compliance, testing and reporting stipulations required to maintain their tax-exempt status. At the same time, the number of plans with less than 100 lives has multiplied exponentially, creating even more complexity.

The financial services industry probably wasn't prepared for these changes. Nor could the institutions in it have anticipated that people would walk away from money earned in a qualified plan. Add in the fact that, in general, today's financial services workers receive far more training on administrative aspects of the plan than on the fiduciary responsibilities of handling trust monies, and the problem grows worse.

The concepts of trust administration for qualified plans came out of the private trust arena. In fact, early plan documents read more like a private trust agreement than what we now recognize as a plan document and trust for retirement plans. Prior to ERISA, the people who administered these plans were trained as private trust administrators. As such, they understood the importance of staying on top of un-cashed checks and other plan issues – a situation lacking in today's retirement plan industry.

Without this training, many institutions have not recognized that plan sponsors need assistance in tracking and monitoring benefit payments that result in un-cashed checks. As a result, unless plan sponsors proactively ask the institutions housing the assets to provide the needed tracking, monitoring and reporting, they may not be able to fulfill their oversight responsibilities for the plan.

This doesn't absolve plan participants for their contributions to the problem. They have a responsibility to keep on top of their benefits, which includes providing proper contact information after leaving an employer and notifying the plan of changes to beneficiary designation. They also need to respond appropriately to all plan communications from their former employer.

A MULTI-FACETED SOLUTION

A solution to the un-cashed check problem will not come easily. In an industry already overburdened with complex rules and regulations – many of which add to the confusion and increase operating costs – the ideal solution will likely consist of several parts. A good place to start is by performing an annual audit in which auditors *automatically* review all funds leaving the plan. This should be followed by timely communication to the institution verifying all checks that have gone un-cashed. Once verified, the audit should identify the interest owed and inform the institution that they must pay interest on those funds.

For plans under 100 participants, a Third Party Administrator (TPA) makes the best gatekeeper because they are the first to know and adjudicate the benefits of terminated participants. As the gatekeeper, the TPA should prepare a letter on behalf of the plan sponsor (addressed to the institution) identifying and verifying all benefit payments that have cashed and cleared. For checks that have not cleared, the TPA should prepare a second letter instructing the plan sponsor to pay interest to the participants' accounts and, when appropriate, and provide new addresses for plan participants.

At this point, the plan sponsor needs to restore the taxes and issue a corrected 1099R. If the funds total less than $5,000, they can go into a default IRA or back into the plan. If they exceed $5,000, the only option is to put the money back into the plan. All un-cashed checks are time-sensitive with regard to restoring the taxes and the need to escheat the funds. However, if a check goes un-cashed for more than three years, the issuing institution cannot petition the IRS for restoration of federal withholding taxes.

Following these steps will resolve the un-cashed check problem while upholding the plan sponsor's oversight responsibility. However, if companies don't have the time or resources for this approach, perhaps the best alternative is to turn the un-cashed checks over to a company that specializes in the distribution of retirement assets. For a fee, the company will administer the process of locating and reuniting plan participants with their money, or if participants are not found, seeing that the funds are handled appropriately.

The growing un-cashed check problem stands out as a blemish on the retirement plan industry. Working together, we can find a workable solution that ensures institutions uphold their fiduciary obligations to plan participants while complying with all ERISA and other government regulations.

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Contact us or visit our website for more information:

Info@PenChecks.com | 800.541.3938

www.PENCHECKS.com