

# The Mid Atlantic Chapter Annual Spring Conference



Distribution Dilemmas

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# Let's Tackle Some of the Possible Headaches

- Missing or lost participants
- Uncashed checks
- Incorrect SSN
- Participant dies, no beneficiary form
- Distributions to minors
- Distributions while the ESOP loan is outstanding
- In-kind distributions
- Distributions to alternate payees
- Distributions from a terminating plan
- Distributions to foreign participants

# Missing or lost participants

- Responsibility to locate
- How to locate
  - Other benefit plan/ company records
  - Through current employees
  - Check with beneficiary
  - Internet search services
  - Social media
  - See guidance for terminating plans – DOL FAB 2014-01
  - Check plan provisions (search on “lost”, “missing”, “unlocatable”); follow any required search methods outlined in your plan

# Missing or lost participants

- At employment termination, remind participants of responsibility to provide new address data
- If participant is unlocatable after all required searches are completed, the plan *may* provide for account forfeiture (must reinstate if participant shows up later)
- In a 2017 field directive, the IRS told examiners not to challenge plan qualification due to required minimum distribution violation if the company can document that it has completed a required list of search efforts

# Missing or lost participants

- PBGC's Missing Participants Program now covers defined contribution plans (e.g., ESOPs, 401(k) plans) that are terminated on or after January 1, 2018
  - PBGC locates participants who were missing when their plan was terminated
  - Once these participants are located, PBGC either provides their benefits to them or informs them where their accounts are being held
  - There are two ways to use the program:
    - Transfer the missing participants' account balances directly to PBGC, or
    - Provide PBGC with information about where the missing participants' account balances were transferred

# Uncashed checks

- Review uncashed checks periodically
- Check for new address
- Force out per plan consent provisions or convert to other investments if plan has segregation language
- May need to stop payment/reinstate account – check plan terms
- Outside paying agents – will they escheat?

# Incorrect SSN

- Need to obtain correct SSN and ask for payment back if cashed by incorrect participant
- If SSN is thought to be invalid or stolen, you do not have many choices unless you can prove identity theft
- If participant is fired and unlocatable, revert to Missing Participant process
- If participant is locatable, you must pay him the benefit when eligible, as you would any other participant

# Participant dies with no named beneficiary

- Plan provisions determine who is the beneficiary
- What if participant was unmarried and the plan says the estate is the beneficiary and no estate was opened?



# Distributions to minors

- Confirm death and named beneficiary
- Determine legal Guardian
- Obtain payment instructions from Guardian
- Check payable to Guardian fbo Minor beneficiary; use Minor's SSN for tax reporting

# Distributions while the ESOP loan is outstanding

- Plan may say distributions of amounts related to stock acquired with an exempt loan may be delayed while the loan is outstanding
- Certain rules override any loan hold
  - Required minimum distributions at age 70 ½, death
  - Diversification payments
  - IRC Section 401(a)(14) – Distribution must commence no later than the 60th day after the end of the plan year in which the latest of the following occurs:
    - Earlier of age 65 or the plan's normal retirement age
    - The 10th anniversary of the date on which the participant began participating in the plan
    - Termination of the participant's service

# In-kind distributions

- If the choice is made to redeem rather than recycle, how does distribution change?
- The participant receives his benefit in company stock (theoretically, but not practically)
- The ESOP is not required to liquidate stock in order to pay the 20% withholding (if not rollover)
- So if a participant receives his entire balance in stock, no withholding will apply
- The participant can grant the trustee the power to transfer the shares of stock to the company for redemption by completing a stock power section on the distribution form (required for S corps)

# In-kind distributions (cont.)

- The company issues a check to the participant (or rollover provider) for fair market value of shares redeemed (no withholding)
- ESOP issues 1099R for value of shares distributed
- If C corp., participant may be able to keep shares and have them redeemed the following year
- Allows participant to use net unrealized appreciation (NUA) tax advantage
- Company may grant the ESOP the ability to buy back the shares, and provide a loan to the ESOP to fund the buy back

# Distributions to alternate payees

- Read and follow plan document and Qualified Domestic Relations Order Policy (if separate from plan document)
- Once a domestic relations order is approved, alternate payee can be eligible immediately or may need to wait
- Need to separately track portion of participant's account awarded to alternate payee
- Spouse alternate payee may roll over distribution
- If spouse does not roll over, subject to 20% withholding, but not early tax penalty

# Distributions from terminating plan

- Consent is not needed for payment upon plan termination, but you do have to provide a rollover opportunity
- Determine how funds will be paid if participant does not consent to distribution (normally single sum)
- Lost participant – follow DOL FAB 2014-01 guidance for location efforts and options for payment if participant cannot be located

# Distributions to foreign participants

- An alien is an individual who is not a US citizen
  - US citizen residing in foreign country after providing services in US – normal tax rules
  - Resident alien's income is generally subject to tax in the same manner as a US citizen
  - Nonresident alien is subject to income tax on US source income

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# Distributions to foreign participants

- Assume nonresident alien performed services in US for ESOP company, then retires
- Provides foreign mailing address along with request for cash distribution
- W-8BEN is completed-shows country of citizenship
- Federal tax is withheld –up to 30% or amount stipulated in treaty with foreign country
- Payment made
- Form 1042-S reporting by withholding agent

Questions?