



FROZEN PENSION PLANS: THE WAY FORWARD

Administration considerations for a plan termination

What do plan sponsors need to know about the administration aspects of terminating a defined benefit plan?

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Terminating a defined benefit (DB) pension plan involves a significant amount of time and effort on the part of plan administrators.¹ Here are the key areas in which plan sponsors need to be prepared.

Participant data and benefit calculations

As part of a standard plan termination, each plan participant must receive a detailed benefit summary called the **Notice of Plan Benefits**. For participants who are already retired and collecting monthly pension checks, this notice needs to provide the details of the form of annuity the individual elected at retirement. For all other participants who have not yet retired, this notice needs to provide the details behind the calculation of their accrued benefit—this might include pay history, service credits, and the like—and must outline all of the benefit options the participant can elect now or will be able to elect once the participant is eligible for retirement. Preparing these notices therefore poses three separate and perhaps daunting challenges:

- Is all of the data that is needed to prepare the notices available in a **consolidated electronic form**? For instance, the pay history for someone who terminated employment long ago may not be available at all or may exist only in paper files. Similarly, if accrued benefits for active participants were calculated when the plan was frozen, can the files with the backup details be located now?
- **A lot of benefit details** will need to be coded and checked! Average earnings, service, accrued benefits, early retirement adjustments, late retirement adjustments, IRC 416 top-heavy minimum benefits, IRC 415 maximum benefits, lump sum amounts, optional forms of annuity, adjustments for benefits that are payable to alternate payees per qualified domestic relations orders (QDROs)—you name it! Anything that might possibly come up in the course of putting **one** individual into pay status is bound to come up in the course of handling **all** of the participants simultaneously.

¹ Note that some small plans are not covered by the Pension Benefit Guaranty Corporation (PBGC) and are therefore exempt from some of the notice requirements described in this article.

- Different participants are eligible for different benefits based on their age, service, and size of benefit, and their notices therefore will contain different information. A given plan is likely to need **different notice content** for retirees, alternate payees, participants with lump sums under \$1,000, participants with lump sums between \$1,000 and \$5,000, participants with larger lump sums who will never become eligible for early retirement, participants who will become eligible for early retirement once they are old enough, participants who are already eligible for early retirement but not normal retirement, participants who are at or beyond normal retirement, and so on and so forth.

Plan sponsors should consider conducting a **dry run** by going through the process of creating the Notice of Plan Benefits well in advance of the actual plan termination. This process can help pinpoint deficiencies in any of these three areas and allow time for the deficiencies to be corrected. This will ensure that the plan termination proceeds smoothly when the time comes.

Communications

It is important for plan sponsors to get out in front of messaging around the plan termination, to head off anxiety and provide reassurance. Some participants, for instance, may fear that the plan termination process will mean a loss of benefits. Others may be concerned that the termination signals the plan sponsor is facing financial problems. A thoughtful communications campaign might include short videos, newsletter content, flyers, and FAQ documents. Reminder postcards can also be deployed during the termination process to remind participants to complete and return their election materials in a timely fashion. Plan sponsors should consider whether providing these communication materials in multiple languages would help to spread the word to the entire plan community.

Sample communication to participants

Important pension plan documents enclosed.
Do not discard.
Los documentos importantes del plan de pensiones. Favor de no descartan.
Documents importants relatifs à votre régime de retraite ci-joints. Merci de ne pas jeter.
Bên trong có các văn bản quan trọng về chương trình hưu trí. Xin đừng vứt bỏ.

Required notices

In addition to the Notice of Plan Benefits, participants must receive a bewildering array of other notices that provide information about the plan termination process and their rights and responsibilities as a plan participant:

- **Notice of Intent to Terminate.** This notifies participants that the plan will be terminating and provides a brief overview of the process.
- **Notice to Interested Parties.** This notifies participants of their rights to direct comments to the IRS and the U.S. Department of Labor (DOL) concerning the plan termination.
- **Notice of Annuity Providers.** This lists the insurance companies from which the plan is considering purchasing annuities.

- **Qualified Joint & Survivor Annuity (QJSA) Notice, Relative Value Notice, Notice of Failure to Defer Distributions, and Special Tax Notice Regarding Plan Payments.** These are the normal notices that are provided to any participant when they are making a benefit election, so they must be provided as part of the plan termination process to all of the participants who are not yet receiving their benefits.
- **204(h) Notice.** This notice is required when a plan freezes benefit accruals. Many plans that are contemplating a termination now have frozen benefit accruals some time ago, so the 204(h) notice would have been provided at that time.

In addition to these notices, each participant who is not already receiving their benefits must be provided with an **Election Form**, along with instructions on how to complete and return it.

In order to not have participants be overwhelmed by the volume of paperwork, most of which is written in technical or legal language, plan sponsors should consider crafting additional materials such as cover memos to help participants:

- Be aware of what they can expect to happen during the plan termination process, including a timetable
- Make sense of the notices and understand what actions they need to take (see example in box at right)
- Know where they can go to get help (see "Fielding questions" below)

Sample call-out language

Notice of Annuity Providers

All Plan participants receive this required notification listing the names and addresses of several insurance companies, from one of which the Plan will purchase insurance contracts.

Action/Response required by you: None.

Plan sponsors should also think about what information should be put on the outside of mailing envelopes to make sure that participants don't accidentally discard them.

Fielding questions

Because participants will be receiving such a volume of information **and** they will be asked to make important decisions about their pension benefits, most plan sponsors set up a series of meetings for participants to learn about the plan termination process and to see what the notices and forms look like. The best timing for these meetings is usually **before** the notices arrive—participants often absorb information about the plan termination more readily when they do not have the distraction of their own details and numbers in hand.

Even with lots of meetings and high-quality communication materials, participants will be asking a **lot** of questions! Plan administration personnel deal with pension matters all the time, but plan participants typically only retire once. And participants who have to decide between monthly benefits and lump sum payments may understandably have a lot of anxiety about the choice. While some participants may be financially savvy or able to get answers through their own research or by reading a FAQ document, others will want to talk things over with a live person. So it is important to provide resources to handle

a large volume of calls, particularly just after the notices are received and just before the deadline for returning election forms. Plan sponsors may also want to set up the ability for participants to schedule one-on-one meetings with plan representatives.

Reviewing completed election forms

Each returned election form must be carefully reviewed to make sure that it has been completed properly. Participants have been known to check multiple boxes rather than just one, or fail to have their spouse consent to their election, or forget to complete a tax withholding election, or not provide account information for an IRA. When an error is found, the participant will need to be contacted and arrangements made for the election form to be revised. It is common for there to be numerous election forms that still have not been completed correctly as the deadline for distributing benefits approaches. At a minimum, therefore, plan sponsors need to ensure there are plans in place to:

- Review returned election forms
- Contact participants with invalid election forms
- Track the status of incomplete election forms

Compiling payout instructions

Once election forms have been judged to be complete, the details of all of the benefit distributions must be compiled so that all of the benefits can be distributed:

- For benefits that will be distributed via the **purchase of annuity contracts** from an insurance company, a file must be created that contains all of the information the insurance company will need to price out the annuities and administer the benefits on an ongoing basis: name, Social Security number (SSN), date of birth, gender, benefit amount, form of annuity, beneficiary information, mailing address, tax withholding, and so forth.
- For benefits that will be distributed via a **lump sum payment**, a separate file must be created so that the trustee can make the appropriate payments. Some of the lump sum distributions may take the form of direct transfers to a 401(k) plan, some may be direct transfers to individual IRA accounts, and some may be cash payments that are sent directly to the participant. Somewhat different information is needed for each of these situations. The trustee may require that the payment instruction file be structured in a particular way, so it is important to talk over the process with the trustee and obtain their file template well in advance.

Tackling these steps systematically in the years leading up to the plan termination will enable the termination process to proceed smoothly. Your Milliman consultant can help you navigate this tricky terrain on *The Way Forward* to a successful plan termination.

This article in the *Frozen Pension Plans: The Way Forward* series was written by Becky Sielman, FSA.

To see other articles in the series, [click here](#).

Do you have a question about your defined benefit pension plan? Write to us at frozenplan@milliman.com

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