

**MEMO# 28682**

January 21, 2015

# **GAO Issues Report on Automatic Rollovers and Recommends Changes to Permit Alternative Default Destinations**

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TO: PENSION MEMBERS No. 4-15

BANK, TRUST AND RETIREMENT ADVISORY COMMITTEE No. 2-15

OPERATIONS MEMBERS No. 4-15

TRANSFER AGENT ADVISORY COMMITTEE No. 3-15 RE: GAO ISSUES REPORT ON AUTOMATIC ROLLOVERS AND RECOMMENDS CHANGES TO PERMIT ALTERNATIVE DEFAULT DESTINATIONS

The Government Accountability Office (GAO) recently issued a report regarding automatic rollovers (referred to in the GAO report as “forced transfers”) from defined contribution plans. Among other recommendations, the report suggests changes to the current automatic rollover rules to permit alternative default destinations. [\[1\]](#) The report, titled “401(k) Plans – Greater Protections Needed for Forced Transfers and Inactive Accounts,” [\[2\]](#) was prepared at the request of Senator Elizabeth Warren and former Senator Tom Harkin. In the report, the GAO examined (1) what happens over time to savings of participants who are forced out of their plans; (2) the challenges 401(k) plan participants face keeping track of retirement savings in general; and (3) how other countries address similar challenges of inactive accounts.

The GAO states that its conclusions in the report are based on a review of relevant data from government, industry, and research sources, including data collected from a non-generalizable group of 10 providers of forced-transfer IRAs about their practices and outcomes. [\[3\]](#) The GAO also interviewed plan sponsor groups, 401(k) plan industry groups, and six federal agencies [\[4\]](#) about plans’ use of forced transfers and what challenges individuals and plans face related to inactive accounts and multiple 401(k) accounts in the U.S. Additionally, the GAO reviewed research and industry literature, relevant federal laws and regulations, ERISA Advisory Council testimony on missing participants, industry white papers on a proposed default roll-in system, and submissions in request to the 2013 Pension Benefit Guaranty Corporation (PBGC) request for information relating to a tracking system for distributions from terminating plans. [\[5\]](#) To examine how some counties are addressing the challenges of inactive accounts, the GAO selected six countries to study

(Australia, Belgium, Denmark, the Netherlands, Switzerland, and the United Kingdom) and interviewed government officials, service providers, and other stakeholders from all of the selected countries.

## Report Findings

The report includes the following findings with regard to forced transfers and inactive accounts.

1. **Current Law and Regulations Allow Sponsors to Force Certain Participants Out of 401(k) Plans Which Can Result in Reduced Retirement Income.** The GAO found that the current Department of Labor safe harbor regulations regarding automatic rollovers effectively limit providers to holding funds in forced-transfer IRAs in money market funds, certificates of deposit, or assets with similarly low investment risk, typically deemed appropriate for holding money on a short-term basis. The report states that, although such conservative investments generally insure that the money is liquid, they can result in low returns and potentially minimal growth over time. The GAO also found that most forced-transfer balances in accounts it analyzed will decrease if not transferred out of forced-transfer IRAs and reinvested, because the fees charged often outpace the low returns earned by the conservative investments prescribed by the Department of Labor's safe harbor regulations.
2.  
As you may recall, in response to the Department of Labor's proposed amendments to its abandoned plan program regulations, the Institute recommended that the PBGC implement a program to allow for the transfer of missing participant accounts to the PBGC. In the absence of the PBGC option, the Institute recommended that the Department amend the abandoned plan regulations to allow for the transfer of small accounts with \$1,000 or less to a bank or savings account, or state unclaimed property fund, even if the account balance meets minimum IRA balance requirements. [\[6\]](#)
2. **Current Law Limits Forced Transfer Options and Permits Plans to Force Out Some Participants with Balances Larger Than \$5,000.** The GAO report states that current law allows plans that are determining if they can force out a participant to exclude rollover amounts and any investment returns attributable to such rollovers that have been earned while in the plan. [\[7\]](#) The report further states that highly mobile workers who participate in 401(k) plans could have significant rollover balances that they have accumulated over time due to successive job changes; however, they may still have their savings transferred out of their plans into forced-transfer IRAs because they are unlikely to have accumulated \$5,000 vested balances at their new plans before they separate from employment.
3. **Low Wage Workers' and Young Workers' Vested Balances May Often Fall Below the Required \$5,000 Vested Balance Needed to Prevent Forced Transfers.** The GAO found that low wage workers and young workers are vulnerable to forced transfers since they may change jobs often, which can leave them with particularly low balances. According to the GAO, in 2011, about 40 percent of plans imposed a service requirement and such plan service requirements make it harder for a worker to build up a vested balance that will exceed the \$5,000 cap on forced transfers.
4. **Keeping Track of 401(k) Plan Accounts Can Be Difficult Because of Challenges with Consolidation, Communication, and Information, but the Social Security Administration (SSA) Is in a Position to Help.** The GAO found that some 401(k) savers find it difficult

to keep track of their savings, particularly when they change jobs, because (i) individuals who accrue multiple accounts over the course of a career may be unable to consolidate their accounts by rolling over savings from one employer's plan to the next; (ii) maintaining communication with a former employer's plan can be challenging if the companies are restructured and plans are terminated or merged and renamed; and (iii) key information on lost accounts may be held by different plans, service providers, or government agencies, and participants may not know where to turn for assistance. The report also found that, although SSA provides individuals with information on benefits they may have from former employers' plans, the information is not provided in a consolidated or timely manner that would be helpful to participants.

5. Other Countries Have Taken Actions to Protect Forced Transfers and Track Retirement Accounts. The report discusses the manner by which six other countries (Australia, Belgium, Denmark, the Netherlands, Switzerland, and the United Kingdom) address inactive accounts and the GAO found that Australia, Switzerland, and the United Kingdom use forced transfers, and Australia, Belgium, Denmark, and the Netherlands use tracking tools. According to the officials the GAO interviewed, the three countries that use forced transfers have legislation that (i) consolidates transferred accounts, either in a participant's new plan or with other forcibly-transferred accounts, and (ii) enables these accounts to grow, either at a rate comparable to participants' current retirement accounts or at least in pace with inflation. The report also states that Australia, Denmark, and the Netherlands provide pension registries to participants on all of their workplace retirement accounts, Belgium is scheduled to do the same by 2016, and the European Union is developing a pan-European pension registry.

## **Report Recommendations**

The GAO includes the following recommendations in the report:

1. Matters for Congressional Consideration. To better protect the retirement savings of individuals who change jobs, while retaining policies that provide 401(k) plans relief from maintaining small, inactive accounts, the report recommends that Congress consider amending current law to:
  - Permit the Secretary of Labor and the Secretary of the Treasury to identify and designate alternative default designations for forced transfers greater than \$1,000, should they deem them more advantageous for participants, and
  - Repeal the provision that allows plans to disregard amounts attributable to rollovers when determining if a participant's plan balance is small enough to forcibly transfer it.
2. Recommendations for Executive Action. The report includes the following agency recommendations:
  - To ensure that 401(k) plan participants have timely and adequate information to keep track of all their workplace retirement accounts, the GAO recommends that SSA make information on potential vested plan benefits more accessible to individuals before retirement;
  - To prevent forced-transfer IRAs from decreasing due to the low returns of the investment options currently permitted under the Department of Labor's safe harbor regulations, the GAO recommends that the Secretary of Labor expand the investment alternatives available. As an example, GAO states that the forced-transfer IRA safe harbor regulations could be revised to include investment options currently available under the qualified investment alternatives regulation

applicable to automatic enrollment, and permit forced-transfer IRA providers to change the investments for IRAs already established; and

- To ensure that individuals have access to consolidated online information about their multiple 401(k) plan accounts, the GAO recommends that the Secretary of Labor convene a task force to consider establishing a national pension registry.

## Agency Responses

Department of Labor. According to the report, the Department of Labor agreed to evaluate the possibility of convening a taskforce to consider the establishment of a national pension registry, but noted that it does not have authority to require reporting of the information needed for a registry or to arrange for consolidation of retirement account information from multiple agencies. The Department also stated that an expansion of the PBGC's missing participant program to include defined contribution plans could address some of the issues raised in the report regarding lost accounts. The report further states that the Department of Labor disagreed with the GAO's recommendation to expand the investment alternatives available under the safe harbor for plan sponsors using forced transfers. According to the report, the Department's response stated that the limited investments under the safe harbor are appropriate because Congress' intent for the safe harbor was to preserve principal transferred out of plans.

Social Security Administration. SSA disagreed with the GAO's recommendation to make information on potential private retirement benefits more accessible to individuals before retirement. According to the report, SSA was concerned that the GAO's recommendation would place SSA in the position of having to respond to public queries about ERISA, and SSA has no firsthand legal or operational knowledge of pension plans or the private pension system.

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## endnotes

[1] Internal Revenue Code (IRC) section 401(a)(31)(B) requires that mandatory distributions of more than \$1,000 (but not more than \$5,000) from a plan qualified under IRC section 401(a) be paid in the form of a direct rollover to an individual retirement plan (an individual retirement account or individual retirement annuity). Department of Labor regulation section 2550.404a-2 provides a fiduciary safe harbor for automatic rollovers to individual retirement plans if certain conditions are met. Regulation section 2550.404a-2(c)(3)(1) requires that the rolled-over funds must be invested in an investment product designed to preserve principal and provide a reasonable rate of return, whether or not such return is guaranteed, consistent with liquidity. Regulation section 2550.404a-2(c)(3)(ii) requires that the investment product selected for the rolled-over funds seek to maintain, over the term of the investment, the dollar value that is equal to the amount invested in the product by the individual retirement plan. Additionally, regulation section 2550.404a-2(d) provides that the safe harbor contained in regulation section 2550.404a-2 also applies to mandatory distributions of \$1,000 or less provided there is no affirmative participant election and the fiduciary makes a rollover distribution of such amount into an individual retirement plan on behalf of such participant in accordance with the conditions of 2550.404a-2(c).

[2] A copy of the report is available here: [www.gao.gov/assets/670/667151.pdf](http://www.gao.gov/assets/670/667151.pdf).

[3] In the report, the GAO acknowledged that it found no comprehensive data on the number of IRA accounts opened as a result of forced transfers or other data relevant to their use and management.

[4] The report states that the GAO interviewed the Consumer Financial Protection Bureau, Department of Labor, Department of the Treasury, Pension Benefit Guaranty Corporation, Securities and Exchange Commission, and Social Security Administration.

[5] As you may recall, the Pension Protection Act of 2006 amended ERISA section 4050 to allow terminating defined contribution plans to transfer assets of missing participants to PBGC, effective upon PBGC's prescription of rules for such a program. In June 2013, PBGC issued a Request for Information (RFI) to gain an understanding of the demand for a PBGC administered program for missing participants of terminating individual account plans. The Institute responded to the RFI and, noting that the challenges associated with locating missing participants also extend to active plans, encouraged PBGC to ensure that any program it established covers missing participants in active plans as well. See [Memorandum](#) to Pension Members No. 39-13, Operations Committee No. 38-13, Bank, Trust and Retirement Advisory Committee No. 23-13, Transfer Agent Advisory Committee No. 62-13 [27481], dated August 21, 2013.

[6] See [Memorandum](#) to Pension Members No. 12-13, Operations Committee No. 11-13, Bank, Trust and Retirement Advisory Committee No. 6-13, Transfer Agent Advisory Committee No. 21-13 [27050], dated February 26, 2013.

[7] Internal Revenue Code section 411(a)(11)(D) generally provides that, for purposes of calculating the \$5,000 amount with regard to mandatory distributions, the present value of the nonforfeitable accrued benefit may be determined without regard to any portion of such benefit which is attributable to rollover contributions, and earning allocable to such contributions.