

Pension Plan Fix-It Handbook

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Simple Beneficiary Designation Forms Problematic if Not Maintained

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Just another form in an enrollment package, yet the consequences of inaccurate completion or failure to update it can be devastating. Participants either ignore it or complete it and never update it. Plan administrators can have so many of them, they don't know what to do with them, yet they are critical and must be maintained. We are talking about beneficiary designation forms.

The 2012 ERISA Advisory Council is examining "Current Challenges and Best Practices Concerning Beneficiary Designation in Retirement and Life Insurance Plans." The council has received written comments, heard oral testimony and held a public hearing on the topic so far.

Regarding beneficiary designations, the council will focus on:

- preemption of state laws that affect beneficiary designation and powers of attorney, for example,

divorce, community property laws, slayer statutes and survivorship determination;

- interrelationship of spousal consent and beneficiary designations;
- responsibility of plan administrators and service providers when there is a participant life change, change in service provider or regulatory changes;
- reviewing current service provider practices; and
- methods for resolving disputes over beneficiary designations.

Plan service providers, professional groups and advocacy groups submitted comment letters; many comments related to electronic beneficiary forms and the role of service providers in maintaining them.

While we did not review all of the comment letters, specific issues generated divergent comments, depending on the market segment. Advocates for the small- to mid-size plans say they believe the plan administrator should be aware of life changes and therefore is in the best position to follow up regarding changing beneficiary designations. Another comment indicated that the recordkeeper could more easily maintain the beneficiary designation and include reminders in quarterly statements regarding the need to revisit beneficiary designations periodically. A larger service provider indicated that it offers on-line beneficiary services to clients for an additional fee. Joint comments by two advocacy groups indicated that use of electronic technologies beyond what is currently permitted "poses a threat to spousal rights." In order to reduce

Tip

While comment letters were asking for guidance regarding locating lost plan participants, IRS announced in Revenue Procedure 2012-35 that it was discontinuing its letter-forwarding program for lost participants. IRS said that several missing-person locators have become available to seek out lost participants since the agency's letter-forwarding program began in 1994. The IRS letter-forwarding service will be limited to locating taxpayers for humane purposes, or in an emergency situation. Humane purposes include serious illness, imminent death or death of a close relative and when people are being sought for medical study.

See Andersen, p. 2

the possibility of fraud, spousal consents (electronic or paper) to waive benefits must be made in the presence of a notary or plan administrator. Removal of the physical presence requirement increases the possibility of fraud and jeopardizes the lawful spouse from obtaining a benefit.

The need for more guidance was a common theme. Comment letters requested guidance in these areas:

- including reminders about beneficiary designations on benefit statements (many service providers already send reminders to participants regarding the need for beneficiary reviews);
- defining the minimum amount of information needed to verify and locate participants (see box below);
- requiring automatic revocation of exiting beneficiary designation in the case of divorce (see ¶745 in the *Pension Plan Fix-It Handbook*);
- defining the fiduciary's responsibility for searching for a beneficiary;
- providing a user-friendly electronic process; and
- applicability of slayer or killer statutes.

Let's ask "what if" as we review two of the many court cases that resulted from out-of-date beneficiary designations.

The first is *Herring v. Campbell*. A participant designated his wife as primary beneficiary in 1990 and 2001. The beneficiary died in 2004 and the participant did not designate a new beneficiary. The plan provided that when a participant dies without designating a valid beneficiary, benefits are distributed to one of five classes, in the following order of priority:

- member's surviving spouse;
- member's surviving children;
- member's surviving parents;
- member's surviving brothers and sisters; and
- executor or administrator of the member's estate.

After the participant passed away, the plan administrator distributed the participant's benefits to his six siblings because the participant spouse had predeceased him, he had no surviving parents and no biological or legally adopted children. The plan she was administering made no provisions for stepchildren who had not been legally adopted, as was the case with the deceased. Two years later,

the stepsons challenged the distribution, stating they were the participant's "children." The 5th U.S. Circuit Court of Appeals upheld the plan administrator's decision.

What if the plan in this case had had a procedure to remind the participant to update the beneficiary form upon the death of his spouse? Would it have made a difference and saved time and court expenses? We will never know if the participant would have returned the form, but a gentle reminder on a quarterly statement might not be a bad idea. In fact, many plan service providers do send reminders.

Cajun Industries, LLC 401(k) Plan v. Kidder, et al. is another example in which failure to update a beneficiary designation ended up in court. A participant named his spouse as beneficiary; the spouse passed away, then the participant named his three children as beneficiaries. The participant remarried and died shortly after the second marriage. The plan administrator decided that, based on the terms of the plan, the benefit was payable to the participant's second wife, not the children. The children subsequently sued. The company took action to determine the beneficiary, deposited the funds with the court registry and the dispute between the participant's children and his second wife went to court.

The plan in that instance provided that upon the death of a participant, the automatic form of payment is a lump sum of the participant's vested account balance to the participant's spouse. "Spouse" is defined as someone who was married to the deceased for a year or more. The court found that the plan was clear that the current spouse at the time of the participant's death was the beneficiary, in the absence of any spousal waiver. The court also ruled that it was up to the plan administrator's discretion to determine whether a six-week marriage trumped the deceased participant's beneficiary designation.

What if the plan administrator sent a beneficiary form to the participant upon remarriage and the participant completed another beneficiary form? We will never know if the participant would have kept his children as beneficiaries or whether the second spouse would have waived her rights.

What this Means

The bottom line on the beneficiary conundrum is that it is up to the participant to submit the beneficiary designation, review it periodically and update as needed. Reminders from plan sponsors and recordkeepers may help. Guidance, if issued, should help to make the process easier for participants while conforming to existing

See *Andersen*, p. 3


Andersen (continued from p. 2)

statutory requirements (for example, those on spousal consent).

There are no easy answers to this situation other than that plan administrators must be cognizant of plan provisions regarding beneficiary designations. Plan administrators may want to consider establishing a procedural requirement for obtaining a new beneficiary designation

in the case of death of a beneficiary (if known) or qualified domestic relations order.

Finding out More

To read the ERISA Advisory Council paper, “Current Challenges and Best Practices Concerning Beneficiary Designation in Retirement and Life Insurance Plans,” go to this link: <http://www.dol.gov/ebsa/pdf/2012ACIssuePaper1.pdf>. 



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