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EXECUTIVE DIRECTOR

To: **Supplemental Retirement Board of Trustees**

From: **Reid Chisholm, Assistant General Counsel**

Date: **March 8, 2017**

Re: **Resolution of beneficiary roll-in error**

The NC 401(k) and NC 457 Plans prohibit beneficiaries from rolling in assets from other plans. However, from 2007 to 2016, Prudential incorrectly allowed eight beneficiaries to roll in a total of approximately $1.15 million of assets from other eligible plans.

As discussed with the Board at its December meeting, the original approach to addressing the error was to allow the beneficiaries to retain their rolled-in funds in the plans. As a result, the plans would file with the Internal Revenue Service's Voluntary Compliance Program (VCP).

Contrary to staff's initial understanding, a VCP filing would require multiple, retroactive plan amendments. After further consideration, SRP staff has decided to pursue an alternative approach and remove the remaining rolled-in funds from the plans. This approach utilizes the IRS's Self-Correction Program, which does not include retroactive amendments.

Scope of the issue

Of the eight remaining accounts, only three are both Bailey-vested and have a large amount of rolled-in funds; two of these have received distributions as well, and the other will require retroactive RMDs.

However, the impact of removing funds from the remaining five accounts will be less significant.

1. One of the beneficiaries already has received a full distribution of the rolled-in funds and therefore, has no funds that need to be removed.
2. Three of the beneficiaries rolled-in less than $13,000 each (or less than $27,000 in total). While two of these accounts are Bailey-vested, none of the three has received any distributions yet.
3. The remaining beneficiary rolled in a significant amount and has begun receiving distributions; however, the account is not Bailey-vested.

Next steps

SRP staff will initially contact the affected beneficiaries, and Prudential will be responsible for working with the beneficiaries on rolling out the funds and, if necessary, restating taxes.

A communication plan will inform the affected beneficiaries of the issue, including the deadline to take action. The beneficiaries will be provided a period of 180 days to initiate the removal of the affected amounts (*i.e.*, the rolled-in funds and any earnings attributable to those funds) to another qualified defined contribution plan or to an IRA. They may – but are not required to – roll over their entire account balances from the NC 401(k) and NC 457 Plans.

For the beneficiary who must satisfy required minimum distributions from prior years, the transaction will be processed prior to the rollover of funds out of the plan. Prudential will reimburse the beneficiary for any IRS penalty assessed for the late processing of the RMD.

For the two Bailey-vested members who have received distributions, Prudential will determine the distributed amounts that were attributable to rollover funds. Prudential will reimburse the beneficiaries for their North Carolina state tax liability (estimated to be $11,487) in the event they file amended tax returns.

Beneficiaries will receive follow-up communication by telephone and/or letter throughout the 180-day response period, including assistance in the rollover process. Once the 180-day response deadline has passed, the affected amounts (*i.e.*, the rolled-in funds and any earnings attributable to those funds) will be transferred to a Prudential IRA.