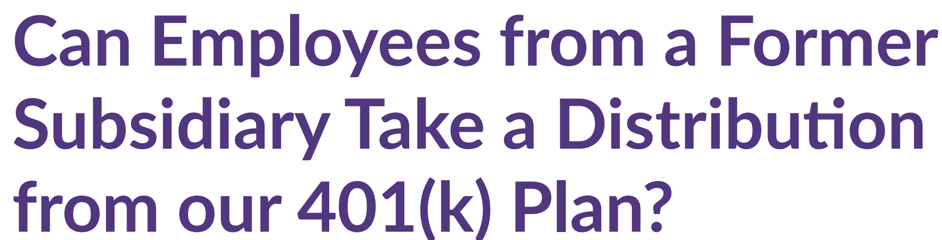


Facts

Our company has several wholly-owned subsidiaries, and each of them has signed onto our 401(k) plan as participating employers. We sold 100% of the stock of one of those subsidiaries – Glen's Fiddich, LLC – to an unrelated company. As a result of the sale, Glen's Fiddich is no longer related to us and has discontinued participation in our retirement plan as of January 1, 2019. The employees of Glen's Fiddich are now participating in the purchasing entity's retirement plan, and a few of them are eager to roll their accounts from our plan into the new plan.

Question

Can these employees take a distribution from our plan and roll those amounts into their accounts in the new plan?

Answer

Generally (I know, again), the answer is going to be no.

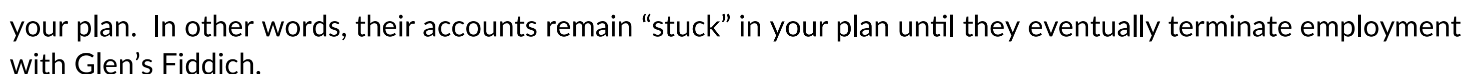
Before going further, let's quickly run through when participants are typically allowed to take distributions.

- Termination of employment
- Attainment of a certain age, usually 59 ½ (again, if the plan permits in-service distributions)
- Financial hardship (if the plan allows hardship distributions)

Next, we need to determine if the Glen's Fiddich participants have experienced any of these events. We'll start from the bottom of the list and work our way up. The rules do not allow a participant to rollover a hardship distribution, so even though that feature in your plan might allow certain participants to access their accounts, it will not help accomplish the objective of getting that money into the new plan.

That takes us to in-service distributions. Whether or not a participant is age 59 ½ is as straight forward as it gets. Assuming your plan allows those types of distributions at that age, that could do the trick for any participants that are at least that old. We should note, however, that it is fairly common for plans that offer in-service distributions as an option to limit them to only certain money sources such as only employee deferrals, so definitely check the details before proceeding.

Last but not least is termination of employment, and this is where things get a little counter-intuitive. In your situation, the employees worked for Glen's Fiddich when your company still owned it. Those same employees still work for Glen's Fiddich even though another entity now owns it. You can probably see where we are going here. The change in ownership and loss of participation in your plan do not cause the employees to be terminated from employment with Glen's Fiddich, so that does not trigger their ability to take distributions from



your plan. In other words, their accounts remain “stuck” in your plan until they eventually terminate employment with Glen’s Fiddich.

You’ve spent all of your time telling me what I can’t do. How about you tell me what I can do?

You got it! We’ve been discussing distributions, but a transfer could be just the solution. We know, distributions and transfers might sound like semantics, but there are some important differences.

Unlike distributions which participants elect to take on an individual basis, a transfer is made at the plan level and involves direct movement of money between plans without participants having a say in the matter. This is critical to our discussion here, because you (as the plan sponsor) can choose to “spin-off” the accounts of the Glen’s Fiddich employees and transfer them to the new plan (assuming the buyer is on board, of course) regardless of the age of the participants and without the requirement to terminate employment. There are no Forms 1099-R issued for transfers, and there is a separate line item on the Form 5500 to reflect such amounts as transfers rather than distributions.

There are a couple of caveats we should mention. One is that transfers are en masse rather than one-by-one for each participant, so you would send over the balances of all affected employees rather than asking each of them what they want to do. Second is that the characteristics of the transferred dollars must be preserved in the new plan. For example, if your plan provides for a 4-year graded vesting schedule, the vesting schedule that applies to those amounts in the new plan must be at least that generous at each step. That makes it important for you and the buyer to work together to ensure all those “Is” are dotted and “Ts” crossed.

A Final Note of Caution

You mentioned at the beginning that Glen’s Fiddich had signed on to your plan as a participating employer, which is not a problem. One thing that is sometimes overlooked, though, is that ceasing participation usually requires some sort of affirmative step. In other words, the fact that you sold Glen’s Fiddich to another company does not, in and of itself, automatically cause them to discontinue participation in your plan. It might seem like a picky detail, but you definitely want to be sure there is signed documentation of their cessation of participation in place before you stop withholding 401(k) deferrals from those employees’ paychecks.

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