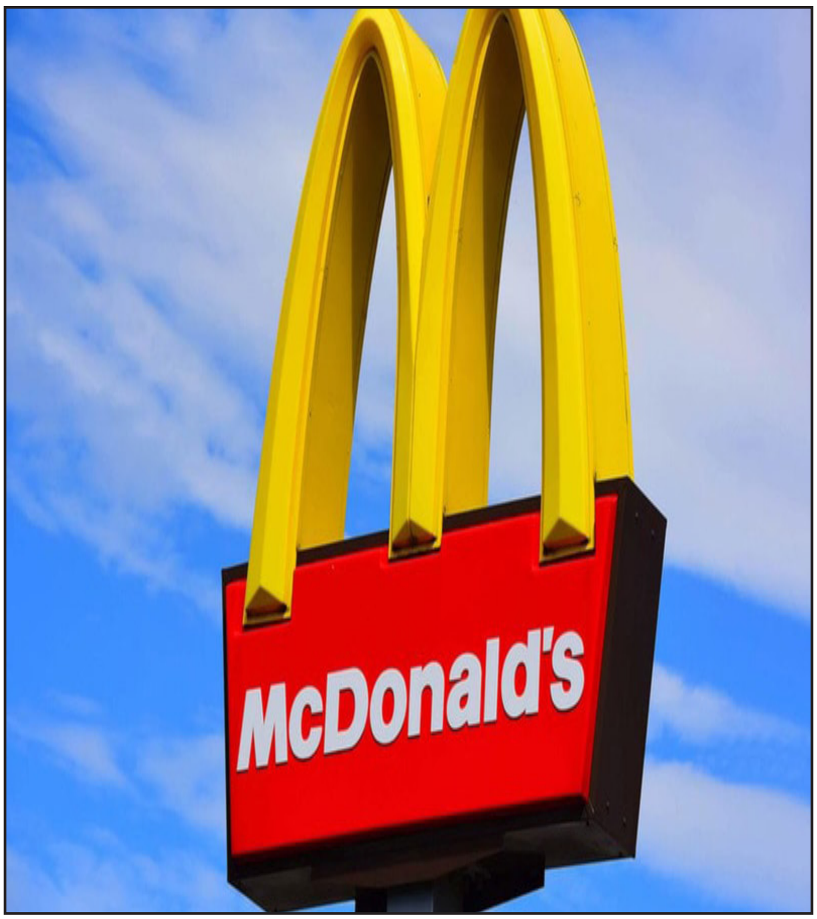
The Wrong Reasons For Changing Your 401(k) Plan Provider

By Ary Rosenbaum, Esq.

Change can be a good thing, but sometimes it's time. Change for the sake of change isn't good either. There are many reasons why as a 401(k) plan sponsor you want to change a retirement plan provider for someone new, but it should be for the right reasons. This article is about avoiding some really bad reasons as for why you need to change a plan provider, whether it's an ERISA attorney or third party administrator (TPA), financial advisor, or auditor.

Changing just because the other provider is cheaper

Fee transparency is a great thing for 401(k) plan sponsors because they get to understand how much the plan is being charged for administrative services, which is important because they are plan fiduciaries. With plan sponsors being fiduciaries, they have a duty to only pay reasonable expenses for the services provided. The only problem I have about fee transparency is that there are 401(k) plan sponsors who think they have to pay the lowest in fees, rather than just paying reasonable fees. There is a huge difference between cheap and reasonable because reasonable means you can pay more as long as you are getting a comparable level of service to justify the expenses. So it's an absolute mistake to switch plan providers just because someone else is just cheaper. There need to be other reasons to change providers other than just by saving a couple of bucks. Leaving a really great provider to save a couple of cents on the dollar isn't a great idea, I've seen too many times where it blows up in a plan sponsor's face. Change provider for other reasons, other than just price.

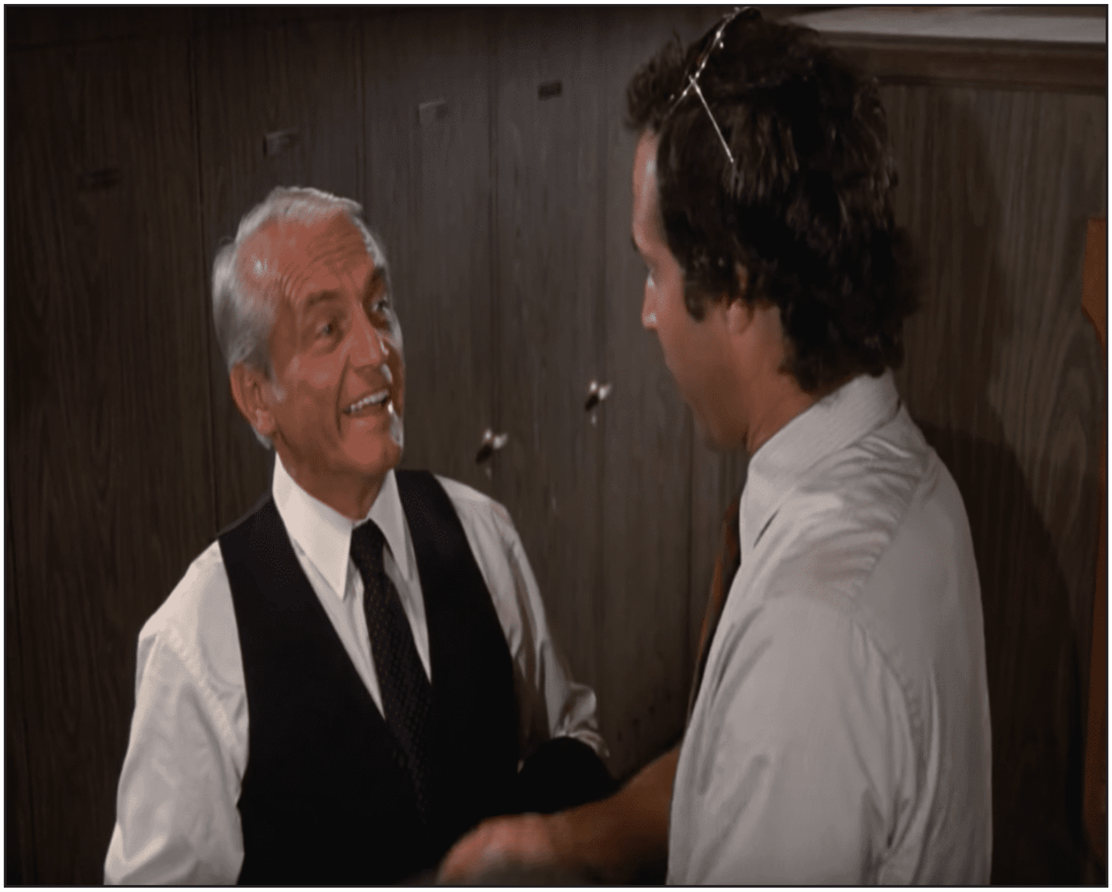


Changing the provider because another provider says so

When you change a provider, such as a financial advisor, the new advisor may suggest changing the TPA. The advisor may suggest a new TPA because their block of plans is with 1 or 2 specific TPAs. Changing to please another provider does nothing for you if the provider they want to replace is doing a great job. A plan provider should have the capability to work with other providers, it's important to have plan providers that can play well with other providers. Technology can allow your plan providers to integrate services with each other, we've come a long way from doing everything via pen and paper. Change for the sake of change is a bad idea, changing just to please another plan provider is even worse. As a plan sponsor, you need to do what's best for plan participants, not what's best for your other plan provider(s).

Changing the provider because a friend or family member wants the gig

If you run a closely held business, nepotism is a practice especially if it's a family run business. As a plan sponsor, you have a fiduciary duty in selecting plan providers and it has to be done through a rational process and review. Selecting a friend or family as a plan provider is a bad idea for many reasons. Hiring a relative or friend as a plan provider may be considered a prohibited transaction if it directly or indirectly benefits you as the plan sponsor. Obviously, hiring a wife or your child as a plan provider would directly benefit you and any prohibited transaction will be hit with an excise tax of 10% as well as possible action by the Department of Labor. (DOL) Even if you hire a friend or another relative as a plan provider that isn't a prohibited transaction, any delineation from a rational process of selecting plan providers will cause a presumption that something unethical is occurring. Hiring one f your employee's relative as a financial advisor who doesn't have any 401(k) plans on the books clearly creates a presumption that a rational process of selecting financial advisors didn't take place since your hired someone without the experience of working on 401(k) plans. Hiring your bank as a TPA who decides your line of credit may be considered a prohibited transaction if that TPA change increases your credit line. Like in high school, you do need to keep up appearances. It's a lot easier to please the clique at high school then it is an Internal Revenue Service (IRS) and/or DOL agent. Charity might start at home, but you shouldn't use your 401(k) plan as a hiring hall for your family and friends.



Changing the provider just because you already do business with someone else

Being a retirement plan provider is considered an ancillary business for those whose main lines of businesses are something else. Some of the biggest retirement plan providers can be payroll companies, broker-dealers, mutual fund companies, insurance companies, and banks. These businesses saw retirement plan services as a natural outgrowth of what they do. Mutual fund companies went into the TPA businesses because it would help them with the distribution of their mutual funds. There are 401(k) financial advisors that might be associated with a bank or a broker-dealer. There are insurance companies that may serve as the TPA, custodian, or recordkeeper. Two of the biggest TPAs are the two biggest payroll providers. There are TPAs and accounting firms in the financial advisory business. So there are many plan providers that may wear multiple hats. It's an absolute mistake for you to just change plan providers because you work with a business that also happens to be in the retirement plan business. I constantly mention how it's a bad idea to use a payroll provider (I'm talking about the large two) as your TPA because there is a lack of dedication to the compliance end of being a TPA. I think selecting a mutual fund company as a TPA just because you like their proprietary mutual funds isn't a great idea. Picking a broker because they're associated with your bank isn't great either. There are many reasons why you should change providers, but perceived synergy with an existing service provider shouldn't be the only reason One roof shopping at places like Target, Wal-Mart, and Costco are great in life they may not be the best fit for every client. The two biggest payroll providers in the TPA business tout their seamless payroll integration. If seamless payroll integration is such a big deal, why do these payroll providers offer that same integration to other TPAs? Synergies in the retirement plan business may be a mirage if you look really close. Having all retirement plan provider under one large roof operated by one company can be a problem because it eliminates the checks and balances that normally accompany a scenario where each plan provider is independent of each other.

Changing the provider because another provider is bigger

Ted Knight's character Judge Smails asked Chevy Chase's character Ty Webb in Caddyshack on how he could measure himself against other golfers if he didn't keep score. Ty said that he could measure by height. One of the most useless statistics in the retirement plan business is how many plans and/or assets that a certain retirement plan provider has under their control/management. Bigger doesn't necessarily mean better. What's better, a burger from McDonalds or In-N-Out? There are some great plan providers who are big, but the reason they're good is not because of their size. Picking a plan provider is all about picking someone who could provide a competent service at a reasonable cost. Picking someone just based on size is silly because I've seen some of the poorest services from some of the largest providers. Getting rid of a good provider for someone else because they're bigger is just size discrimination and you may get an inferior service that you didn't expect.

The Rosenbaum Law Firm P.C.

The Rosenbaum Law Firm P.C.
734 Franklin Avenue, Suite 302
Garden City, New York 11530
(516) 594-1557

http://www.therosenbaumlawfirm.com
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