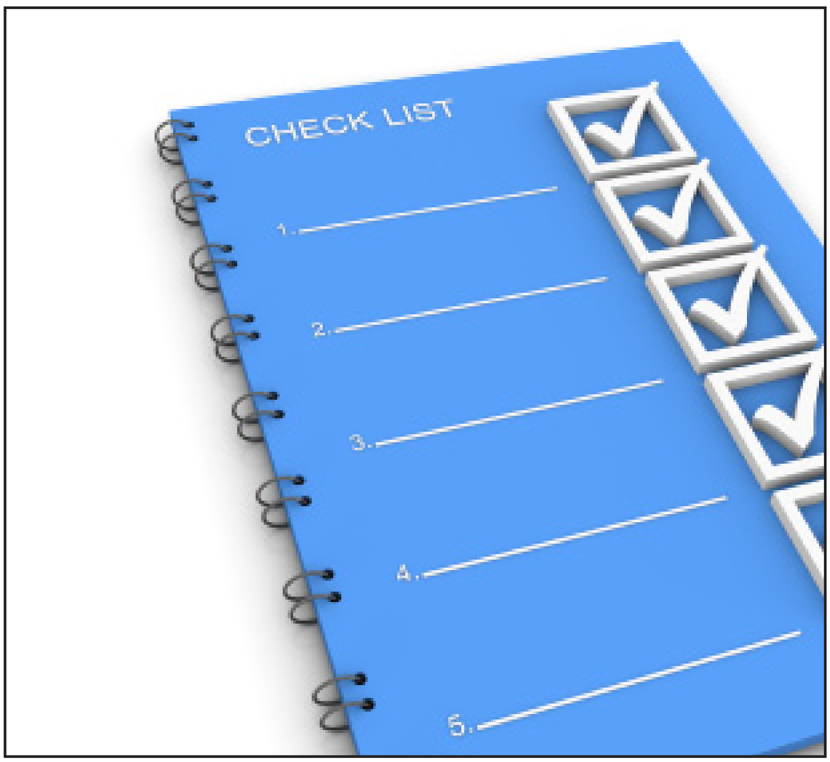
The Essential Plan Providers for a 401(k) Plan

By Ary Rosenbaum, Esq.

When people are sick, especially debilitating illnesses or diseases, it's natural for them to travel far and wide to get the best medical coverage possible. I live in Long Island, but my children were born in Manhattan because we felt the care there was better. People who are ill will try to find the best medical coverage possible; they won't hire a doctor because they're the lowest price. So it's kind of surprising that when it comes to the financial health for retirement plan sponsors, they skimp when it comes to hire their plan providers. To save a few hundred dollars, they may hire a third party administrator (TPA) who is incompetent and was only hired because they also happen to handle payroll. Plan sponsors need to make solid choices of retirement plan providers because it's their neck on the line if they don't. So this article is about the essential plan providers to hire and what to avoid when hiring them.



Why Plan Sponsors should care

If you hire a bad contractor (I've hired a few of those) to work on your home, you're the one who is going to suffer. As a retirement plan sponsor, you don't get off so easy. A retirement plan sponsor is a plan fiduciary and that's the highest of duty in law and equity. So if a plan sponsor hires an incompetent plan provider or one that is way too expensive for the services provided, it's the plan sponsor who is going to be on the hook for liability, So plan sponsors need to care about hiring their plan providers and developing a process to properly vet potential plan providers. Whether it comes through being sued by an aggrieved former plan participant or by an audit by the Department of Labor or a required plan adult (if the plan has the requisite number of participants), plan sponsors will have to demonstrate their was an actual process in selecting and evaluating plan providers, whether they were current, potential, or former plan providers. Simply hiring a financial advisor off the golf course or being best related to the TPA isn't an actual process.

Never go for the cheapest provider just because they are cheap (and vice versa).

While plan sponsors are supposed to pay reasonable plan expenses, plan sponsors misinterpret that they only have to use the cheapest plan providers. Plan sponsors forget that fees must be reasonable for services provided, so they can pay more if they get more. While paying more for the sake of paying more isn't a good idea for the plan sponsors, neither is paying less just for the sake of paying less. A plan provider might be expensive just because the owners want to drive a Porsche instead of a BMW and sometimes the cheapest provider is cheap because they don't do the requisite work that most competing plan provides will do. Sometimes you get what you pay for, so plan sponsors shouldn't pick a plan provider just based on cost.

The TPA

With apologies to other providers (including other ERISA attorneys), but the most important plan provider that a plan sponsor will hire is a TPA. Why? They do the bulk of the work when it comes to the day to day administration of a 401(k) plan and the fact is that the bulk of the problems that a plan sponsors will have with their 401(k) plan can be traced to poor plan administration. So that's why it's extremely important to hire the right TPA. The right TPA is a competent TPA that can handle a plan's administration with limited hiccups and the ability to analyze the plan to see whether it needs to be augmented to meet the ever-changing needs of the plan sponsor. The right TPA is proactive when it comes to handling their clients' plans, especially when it comes to plan design issues. Hiring a reactive TPA may cost the plan sponsor money by having too many errors in plan administration and not having a plan design that is cost effective to the plan sponsor. Hiring a TPA just because they are a popular mutual fund company or their payroll provider isn't wise if they aren't the right fit for that plan sponsor. TPAs come in all shapes and sizes and are dependent on the size and type of 401(k) plan that they handle. The TPA that charges a $7,500 for their services will be a great for the 401(k) plan with $10 million in assets, but would be too expensive for the plan with a $1 million in assets or less. A payroll provider that does a decent job in handling the administration of plain design 401(k) plans isn't the right fit for a plan that needs or wants an intricate plan design such as new comparability or safe harbor. Like a glove, the TPA has to be the right fit.

The financial advisor

Any plan that is subject to ERISA needs a financial advisor, whether that advisor is a broker or registered investment advisor. While plan sponsors need to hire a financial advisor that has some financial expertise, they also need to hire an advisor that actually works with retirement plans because plans are much different than handling the investments of individuals. Hiring the next Peter Lynch as a financial advisor for a 401(k) plan isn't a good idea if that advisor can't spell 401(k). The right advisor is someone who can help manage the plan sponsor's fiduciary process of developing an investment policy statement, selecting and replacing investment options based on these options, as well as providing investment education to plan participants. Plan sponsors need to hire advisors who handle retirement plans, not advisors who dabble in retirement plans. The right advisor is the one who understands their role and makes regular visits with the plan fiduciaries to review the plan and help plan participants enroll in the plan. The wrong advisor is the "milk carton" advisor who probably should have their picture placed on one since they have been missing form the offices of the plan sponsor for quite some time. Plan sponsors may consider hiring advisors who take on some of the burden of being a plan fiduciary. That maybe an advisor willing to take on some sort of a fiduciary role or an advisor serving as an ERISA §3(38) fiduciary who will assume the bulk of the responsibility and liability when it comes to manages the retirement plan's fiduciary process.

The ERISA Attorney

While not as required as a TPA or financial advisor, a good ERISA attorney can be an essential element in having a great retirement plan. Like TPAs, ERISA attorneys come in all different varieties. I know, I've been some of these varieties. There are attorneys who draft plan documents as an attorney for a TPA. I know because I did that for 9 years and I actually serve in that role for 3 TPAs now. ERISA attorneys who work for TPAs understand the nuts and bolts dealing with the day-to-day plan administration of a retirement plan. The only caveat is that TPA ERISA attorneys don't offer an attorney-client relationship with their clients, so they lack independence from the folks paying their bill (the TPAs). Law firm ERISA attorneys could be prohibitively expensive, based on their firm and the clients they handle. From experience, the most important criteria for any attorney who works for a mid sized or large law firms is billing by the hour and they traditionally hate to give clients some cost certainty by explaining what they think the fee maybe. That is why I charge a flat fee for most of my services, so plan sponsors never have sticker shock. An ERISA attorney is an excellent resource for making plan reviews, drafting plan documents, and any plan contractual work. In addition, they must be hired if the plan sponsors are being audited by the Internal revenue Service or the Department of Labor. If the government or a plan participant is suing the plan sponsor, then an ERISA litigator is essential.

The auditor

If a plan sponsor has the requisite number of plan participants (usually more than 100), they will need to hire an accounting firm to audit their plan as part of the required 5500 annual filing. Plan sponsors shouldn't hire their local accountant, especially if their accountant has absolutely no experience in drafting plan audits. The purpose of an audit is to make sure the assets of the plan are where the plan sponsors and providers say they are and to determine any issues that may jeopardize the paying of benefits to plan participants. So plan sponsors need to hire an independent auditor for their plan to prepare an independent audit. So hiring auditors that have their own TPA or financial advisor practice isn't independence. Plan sponsors should look for auditors who handle multiple audits and have enough auditors on staff to properly manage their audit workload. The best auditor is the auditor that is a check and balance against the TPA and financial advisor to determine whether the retirement plan is sound or not. The wrong auditor is the one who didn't fully examine the plan and let glaring issues and mistakes ready to be discovered by the government.

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