Retirement Plan Sponsors Need To Be Careful About Buying "Fiduciary Services"

By Ary Rosenbaum, Esq.

Unlike other languages, English is full of deceptive words that entice people to purchase products and services they think they are getting when they are not. It happens a lot with food. Lemon flavored products have no lemons in them. Homemade food items are made in factories. Chicago style pizza isn't from Chicago. Kosher style catering isn't Kosher and there is nothing natural about natural food. It also happens a lot with retirement plan services, especially when it relates to "fiduciary services" because much of the time, fiduciary services offer very little fiduciary protection to plan sponsors. So this article will try to let plan sponsors know what the term fiduciary really means and what products and services out there don't offer the fiduciary liability protection that plan sponsors assume they are getting.

Being a Fiduciary is all about action and liability

Many of the actions involved in operating a retirement plan will plan make the person or entity performing them a fiduciary. The fiduciary status is based on the functions performed for the plan, not just a person's title. A plan sponsor is a fiduciary, so are the individual trustees. A fiduciary duty is the highest standard of care at either equity or law. A plan fiduciary is expected to be extremely loyal to the plan and a breach of that fiduciary duty may involve personal liability. Since the duty of a plan fiduciary is extremely important, plan sponsors need to hire plan providers that will help minimize that potential liability. One of the ways to minimize that liability other than best practices is to hire a financial advisor that will serve in a plan fiduciary role as well, so that the advisor will either stand in the shoes of or stand next to the plan fiduciaries. Having an advisor serving as a fiduciary is a great way for the plan sponsor to spread the blame and liability if they get sued by plan participants.

The Retirement Plan "F" Word that is so overused

When it comes to retirement plans, the use of the word fiduciary is so over used in the marketplace that it becomes as generic as the Band-Aid brand. So while plan sponsors are hearing the word fiduciary thrown around in products and services, it creates an expectation that may not be met because while they are toting fiduciary services, the product is missing the fiduciary protection that plan sponsors assumes that it has. So while plan providers can use the term as freely as they want, plan sponsors need to know that there is a difference between someone serving in a fiduciary role and someone who is not.

The 5 Part Test on who is a Fiduciary Advisor

Current law imposes a five-part test that must be satisfied in order for a person or an entity to be treated as a fiduciary by reason of rendering investment advice. Advice is considered "investment advice" if an adviser who does not have discretionary authority or control with respect to the purchase or sale of securities or other property for the plan:

1. renders advice as to the value of securities or other property, or makes recommendations as to the advisability of investing in, purchasing or selling securities or other property
2. on a regular basis
3. pursuant to a mutual agreement, arrangement or understanding, with the plan or a plan fiduciary, that
4. the advice will serve as a primary basis for investment decisions with respect to plan assets, and that
5. the advice will be individualized based on the particular needs of the plan.

Under the current definition, stockbrokers are not plan fiduciaries since providing advice on a regular basis is not considered the role of a stockbroker. While the Department of Labor is trying to change that fiduciary definition and require brokers to be fiduciaries, it should be noted that while they may called themselves retirement plan advisors, they will not serve the plan in any fiduciary capacity.

Registered investment advisors (RIAs) can serve in a co-fiduciary capacity, or as an ERISA §3(21) or ERISA §3(38) fiduciary. A co-fiduciary capacity means that the RIA will serve in a capacity alongside the plan fiduciaries and will share in the liability. An ERISA §3(38) fiduciary will assume the entire fiduciary process and therefore almost all of the fiduciary liability. A limited scope §3(21) fiduciary has no discretionary authority and offers the same liability protection as a co-fiduciary. A full scope §3(21) fiduciary has discretion and offers almost the same liability protection as an ERISA §3(38)

except the full scope §3(21) can hire and fire other service providers. When hiring an RIA, a plan sponsor should determine what type of fiduciary role that they will serve which shall determine the liability protection. Plan sponsors should always be wary of RIAs trying to disclaim any fiduciary role by hiding such language in their contracts. A good ERISA attorney (cough, cough) can certainly help in reviewing these agreements and breaking them down in English.

The "Fiduciary" Warranty

The word warranty in business carries great importance such as a 5 year /50,000 mile warranty for new cars. Of course, as with any warranty, there are terms and conditions that limit that warranty that people who don't read the fine print find out in most unfortunate circumstances that they won't be covered. Many insurance companies who operate as retirement plan providers have been offering what they call a "fiduciary warranty".

When plan sponsors will hear the term "fiduciary warranty", they will assume that these plan providers will either serve in some sort of a fiduciary capacity or indemnify the plan sponsor in any lawsuits brought by plan participants for any claim for a breach of fiduciary duty. Of course, these providers go out of their way to make sure that they are not identified as serving in any fiduciary capacity and the fine print in these warranties indicate that the providers will only defend plan sponsors in only in rare instances. The warranties only protect the plan sponsor under the ERISA §404(c) requirement of offering a "broad range of investment alternatives", and that the investment strategies provide a suitable basis for plan participants to construct well diversified portfolios. To comply with the simple broad range requirement, the plan fiduciaries must first decide on the asset classes (e.g., stocks and bonds) and styles (e.g., large cap U.S. equity growth fund, small cap U.S. equity value) for the "core" investments of the plan. So plan sponsors need to offer a diverse group of investments.

Guaranteeing that the investments offered in the plan are part of a broad range of investments and are prudent is just one of many ways where a plan fiduciary can be sued for an ERISA Section §404(c) breach. A plan sponsor and fiduciary can still be sued for not formulating an investment policy statement or offering investment education to plan participants. That whole broad range requirement is rather broad; I am unaware of any plan fiduciaries ever being sued on that requirement. A fiduciary warranty is almost absolutely no protection for plan fiduciaries, it's like buying car insurance that only covers you in a head on collision or a life insurance policy that only pays on accidental death. Since insurance companies are in the business of insuring risk for a fee, what does it say about the fiduciary warranty if they give it away for free?

Payroll providers offering fiduciary services

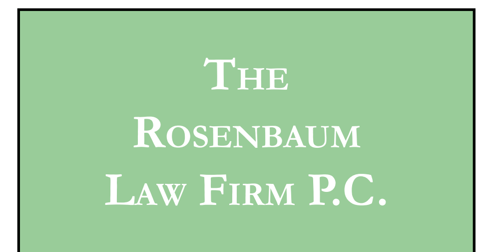
Many plan providers such as payroll provider TPAs are also now offering "fiduciary services" being provided by a third party. What are these services? Are they really serving in a fiduciary capacity or are they just providing services to a fiduciary? Providing services to a fiduciary could be just assistance in managing the fiduciary process such as helping with education to plan participants with the investment policy statements. Fiduciary assistance is different from being a fiduciary, just like juice is juice and a juice beverage is watered down juice. When it comes to any provider adding anything to the back of the word fiduciary, it probably means what they are offering is not any fiduciary role which means that plan sponsors are getting less liability protection than they think.

§3(16) Fiduciaries

Plan providers such as yours truly and third party administrators (TPAs) are offering ERISA §3(16) administration where they assume the liability of the day-to-day administration of a retirement plan from the plan sponsor. As with any retirement plan services, it's important to review the contracts for the services the §3(16) fiduciary will assume and what it still leaves the plan sponsor in holding the plan.

Best protection is reviewing what you're getting

Having a retirement plan provider serving in a fiduciary role does minimize the liability that plan sponsors and trustees have as since the provider will share or assume all the fiduciary liability that was originally intended for them. The plan sponsor needs to get beyond the marketing and deceptive terms that some providers are touting services that are well short of a fiduciary role. Plan sponsors need to know what they are getting because nothing is worse than suing a plan provider and a court ruling that the provider was never a plan fiduciary.



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