The Buck Stops For Retirement Plan Sponsors

By Ary Rosenbaum, Esq.

"With great power, comes great responsibility." These words are attributed to Ben Parker, uncle and surrogate father to Peter Parker, the alter ego of Spiderman. One would think that instead of launching the career of a superhero, Ben Parker was talking of the role of a fiduciary of a qualified retirement plan because with that great power, comes a lot of responsibility.

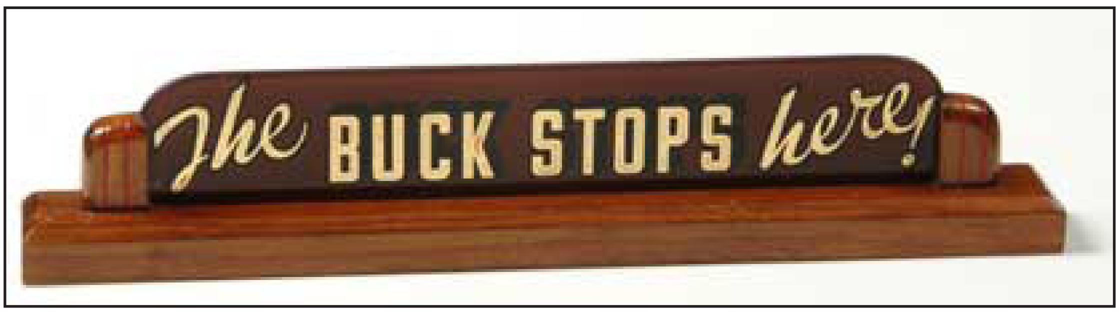
Whether as a plan sponsor or as an individual trustee, employers and their hierarchy have tremendous responsibility in their roles as plan fiduciaries.

The problem with this great power is that often plan sponsors and plan trustees are unaware of all of their responsibilities and by ignoring these unknown responsibilities; they unwittingly subject themselves to potential civil liability. As individual plan trustees, that liability may be personal liability.

The problem with fiduciary responsibility, is that not only is a fiduciary concerned with their job, they also are responsible for the jobs they delegated to third parties, and may be liable for things that they may be unaware of and that were done without malice to plan participants.

I represented a client who had sponsored a couple of defined benefit retirement plans for almost 30 years. The client was being investigated by the Department of Labor because two former employees complained that they were denied a retirement benefit that they were entitled to. While the initial focus was on the missing pensions, it grew to include a review of the administration of the plans' and the work of the plans' actuary/third party administration (TPA) firm.

Having been an ERISA attorney for 12 years and having once worked for a TPA that is currently under criminal and civil investigation, I thought I saw everything until a review of the administration of the Plans by this TPA who was the actuary for the plan for over 20 years. Plan participants who terminated were not offered their legally required normal form of annuity benefit and were paid in a lump sum. The plan sponsor never received proper valuation reports from the TPA that would detail the participants, salaries, and normal



retirement benefits. Participants were never distributed their legally required, annual benefit statement. The TPA's calculation of the required minimum distribution amount to the owners of the Plan sponsors (who were past the age of 70 ½) was in a broad range of hundreds of thousands of dollars instead of an exact dollar amount. In the worst form of administration I have ever seen, the TPA did not require copies of trust statements to determine the assets of the Plans, they merely took the word of the client as to what the assets were on a sheet of loose leaf paper. In the world of defined benefit plans where there are minimum funding requirements, this could open up to fraud by unscrupulous Plan sponsors who want to avoid paying a large contribution when they can't afford it.

While the TPA was completely incompetent and the Plan sponsor relied on this TPA to their detriment, the Plan sponsor and the individual owners who were trustees were ultimately legally responsible for the poor administration of their retirement plans. As plan fiduciaries, they breached the fiduciary duty of prudence in ensuring that the TPA was doing their job correctly. What could this plan sponsor have to done to ensure that the actuary they were using for more than 20 years was doing their job? Perhaps hiring an independent ERISA attorney, or plan consultant, or hiring a financial advisor with a strong retirement plan background to act as a check and balance on the TPA. Perhaps the easiest way was for the plan sponsor to ask for annual reports that dictated the status of the plans. At the end of the day, simply relying on a plan provider's word isn't good enough. Plan sponsors need to have a process to select and monitor all their plan providers.

The TPA is not the only retirement plan provider that can go wrong. I have had a number of defined benefit plans that suffered millions of dollars of losses because they invested all retirement plan assets with a financial advisor known as one Bernie Madoff. While Madoff was running a Ponzi scheme that defrauded these plans, these plan sponsors breached their fiduciary liability because they failed to diversify plan investments and failed to document investment decisions including the selection of Madoff. While Madoff will spend the rest of his life and then some in jail, the plan sponsors bear the losses in their defined benefit plan and the liability in making their plan participants whole in their defined retirement benefit.

Plan sponsors will also breach their

fiduciary responsibility when it comes to selecting mutual funds for participant directed retirement plans. Plan sponsors are under the mistaken notion that liability is limited under ERISA Section 404(c) as long as they provide a list of mutual funds for participants to invest in. As I always say ERISA 404(c) is ot a suicide pact, it is a process that limits a plan sponsor's fiduciary liability measured by the amount of education offered to plan participants so they can make informed decision in the direction of their retirement account. The plan sponsor must develop an investment policy statement (IPS) with their investment advisor to document how plan investments are chosen. The plan sponsor must also review their mutual fund lineup with their investment advisor on a semi-annual or annual basis to make sure that the investments remain consistent with the terms of the IPS. All decision making on plan investments by the plan sponsor in conjunction with their investment advisor must be documented in writing.

I have also had to assist retirement plan sponsors through the Internal Revenue Service (IRS) voluntary compliance program because the plan sponsors' ERISA attorney failed to properly advise the sponsor of the need to amend and restate their plan document in the timeline and deadline set by the IRS. These plan sponsors were forced to pay thousands of dollars in legal fees and IRS compliance fees to correct the failure to properly amend and restate their plan document. So while this error was malpractice of this ERISA attorney, it is the responsibility of the plan sponsor to correct this error which left uncorrected, may have subjected the plan to disqualification by the IRS.

While errors and malpractice by plan providers may be remedied by legal action to seek damages, it will not limit or eliminate a plan sponsor's liability as a fiduciary because they bear responsibility as a plan fiduciary to remedy these breaches.

Plan sponsors do not simply breach fiduciary responsibility because of errors or malfeasance by plan providers or by themselves through embezzlement or prohibited transactions. Innocent mistakes and oversights by the plan sponsor can unwittingly expose them to liability for a fiduciary liability. The road to hell is paved with good intentions, so is the road to a breach of fiduciary responsibility.

The duty to act prudently is one of a plan sponsor's main fiduciary responsibilities under ERISA. One of the major concerns with retirement plans these days and one of the most highly litigated points is plan costs. It is the plan sponsor's fiduciary responsibility to make sure that plan expenses are reasonable and it is almost impossible to do when plan providers are

not legally required to disclose fees to plan sponsors. This will change with the implementation of fee disclosure regulations in July 2011, but it will not absolve plan sponsors of the potential liability today. With fee disclosure regulations or not, it is incumbent on plan sponsors to gauge whether the fees they are paying for plan services is reasonable as to what is offered in the marketplace. Plan sponsors do not have to go with the lowest cost provider; they just need to make sure that they are paying a reasonable fee based on the services provided to the plan. Plan sponsors can avoid this potential pitfall by working with an independent ERISA consultant or ERISA attorney to gauge fees in the retirement plan marketplace.

A recent court decision in California federal court added another wrinkle to a plan sponsor's fiduciary responsibility. The large California utility, Edison International was found by a Federal judge to have breached their duty of prudence because they chose retail mutual funds for their plan investments, when they could have chosen, less expensive institutional class shares of the same mutual fund. So Edison International was liable because they paid retail, instead of buying at a discount. There was no malfeasance by Edison, just laziness in not bothering to understand that an institutional share class of mutual funds were available and would have saved plan participants in mutual fund expenses. It's just another pitfall that plan sponsors have to avoid as plan fiduciaries.

Plan sponsors can always minimize fiduciary liability; they can never fully eliminate it. How can a plan sponsor minimize fiduciary liability? First step is fiduciary liability insurance to protect the plan sponsor and individual trustees from liability. Of course, good practices implemented with an independent financial advisor, TPA, and ERISA attorney will help. The retention of a trust company as the plan's trustee won't minimize liability, but will drag someone else in for potential liability as a plan fiduciary. The newest form of limiting fiduciary liability is the retention of an ERISA 3(38) fiduciary, where the plan sponsor delegates fiduciary responsibility to an investment advisor, bank, or insurance company to make decision on the plan and bear the liability for making that decision. This gives the plan sponsor significant cover and limitation in liability. Of course, fees charged by ERISA 3(38) fiduciaries may be higher that investment advisors who won't take that 3(38) role because with great power, comes greater responsibility and higher liability policies.

Plan sponsors can blame the problems of their plans on others, but ultimately they bear the brunt of liability as plan fiduciaries. A plan sponsor must be aware of all their fiduciary duties or at least, hiring several plan providers that do. Great liability is avoided by understanding the great responsibility as a retirement plan sponsor.

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
Follow us on Twitter @rosenbaumlaw