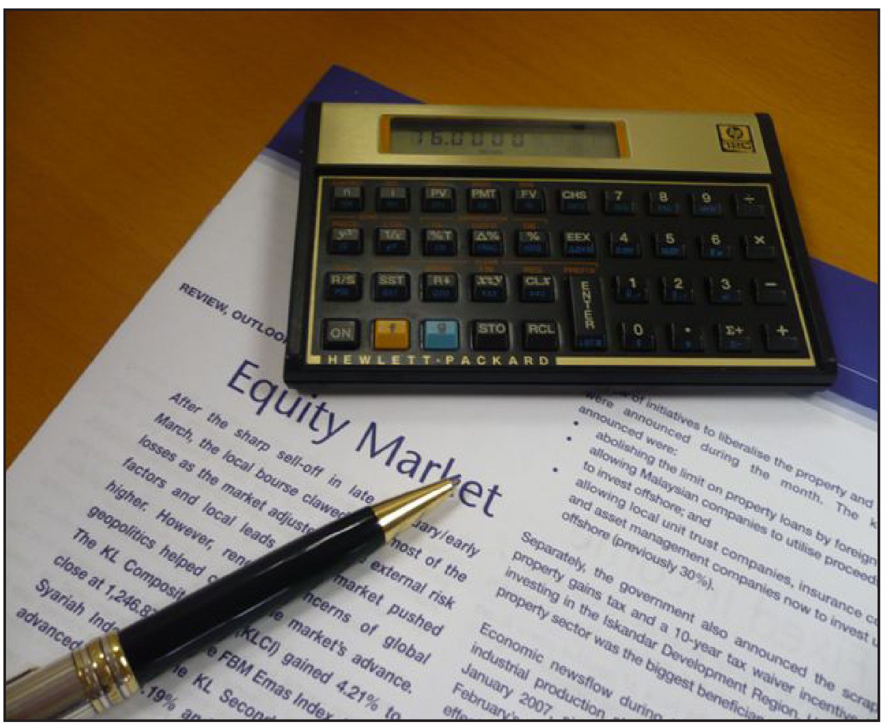
# Why Retirement Plans Need A Financial Advisor

**By Ary Rosenbaum, Esq.**

Thanks to the Internet, a lot of businesses have been decimated because technology has made their products or services obsolete. Back before the Internet, most people used travel agents for the purchase of any airplane tickets or most business travel. On-line booking has decimated the travel agent industry. The Internet has helped close down many video rental stores, bookstores, and record stores. So the Internet has made many types of businesses a shadow of their former selves.

Prior to the Internet, investors in the stock market had to hire a broker to trade stocks or they would purchase mutual funds over the phone or by mail. The Internet has allowed for the purchase of securities to be easier and less expensive. In addition, it has led to an explosion in the amount of participant, directed 401(k) plans because it allowed participants to direct and change their retirement investments on a daily basis. While the Internet has allowed individual investors to manage their own individual investments on their own without the use of a financial advisor, any retirement plan sponsor with employee participants need to hire a financial advisor. The Internet has not made the role of a retirement plan financial advisor obsolete. On the contrary, the Internet and participant directed 401(k) plans have created a greater need for financial advisors and their expertise in working with plan sponsors to minimize their fiduciary liability.

As an ERISA attorney for 13 years, I am amazed by how often I find participant directed 401(k) plans without a financial advisor assisting the plan sponsor and participants. I understand how solo 401(k) plans and owner/participant only plans don't have an advisor because individuals think they can do it on their own (and there is no chance they will sue themselves if they lose money). I have a solo 401(k) plan and I handle my own investments. I always say that the moment that I add an employee, I am going to hire a financial advisor and there is an easy reason why, it's called limiting my fiduciary liability (which is personal liability as plan trustee).




The reason that many 401(k) sponsors and other retirement plan sponsors don't hire a financial advisor is because of their lack of understanding on why they need one. Many employers that sponsor participant directed 401(k) plans think that all a financial advisor does is pick investments and they have a mistaken belief that role is obsolete in their minds because a participant is going to direct their investments anyway which limits their liability under ERISA §404(c).

Section §404(c) protection is a sliding scale, the more management that a plan sponsor has over the fiduciary process and the more education given to plan participants, the more protection from fiduciary liability they will get. There are too many plan sponsors who don't manage the fiduciary process with a financial advisor to guide them who think that the fact the plan is participant directed is protection from liability. Section 404(c) is not a suicide pact, the plan sponsor and trustees have to get involved in the selection of participant directed investments to get any liability protection.

When it comes to participant directed 401(k) plans, the main role of a financial advisor in my opinion isn't picking mutual funds. While some providers are touting their "fiduciary guarantees" about the funds they have selected to satisfy the broad range of investment requirement under ERISA §404(c), I believe that with all due respect to Commander Montgomery Scott from Star Trek III, that a monkey and two trainees can pick a mutual fund lineup to meet that broad range requirement. Picking investment options under a retirement plan is only a small part of what a financial advisor brings to the table, it's their expertise and background in monitoring investments and investment education that are their most important roles in serving plan sponsors and trustees for their retirement plan needs. In addition, some of these financial advisors offer themselves as independent ERISA §3(21) and §3(38) fiduciaries which can greatly mitigate a plan sponsor's and trustee's fiduciary liability.

I worked at a semi-prestigious (sorry, Lois) law firm on Long Island and there was no financial advisor on the 401(k) plan for a review of the mutual funds for 10 years. The plan trustees had no investment policy statement (IPS) to guide themselves in the monitoring of plan investments. There was no investment education offered to participants, a participant got profiles on the funds from Morningstar and that was it. I knew we needed a financial advisor when someone on the office staff stated that he only invested in the mid-cap mutual fund offered under the plan because "it represented the middle of the market." That is why you have to have a financial advisor.

The value of a financial advisor is not in picking mutual funds or the financial advisor's rate of return (which is irrelevant in a participant directed 401(k) plan since participants have their own individual rate of return by choosing investments). The purpose of a financial advisor is having them as a part of the fiduciary process, which would help limit a plan sponsor's liability because of the financial advisor's expertise. The fiduciary process that a financial advisor can assist in is the drafting an IPS, developing and reviewing the investment fund lineup and most of all, employee education. This process will greatly increase the plan sponsor's fiduciary liability protection.

Even 401(k) plans that offer index funds or exchange traded funds need a financial advisor because while index investing beats most of the active funds on a consistent basis, participants still need investment education in order to make an informed decision that will get the plan sponsor ERISA §404(c) protection. Index funds and ETFs are great, but what about asset allocation and risk tolerance? Index funds and ETFs won't solve those issues on their own. So a plan that is offering a passive approach to investments still needs a financial advisor.

Many sponsors of participant directed 401(k) plans don't have a financial advisor because they assume their third party administration firm (TPA) or the bundled retirement plan provider is handling that role. This usually happens when the provider is a payroll company or a provider that is either an insurance company or a mutual fund company. While these providers offer mutual fund lineups for a plan sponsor to choose from, they make it clear (at least to themselves) that they are not giving any financial advice and they are not serving in any fiduciary capacity. I had a client who had a 401(k) plan who invited me to a meeting with their payroll provider TPA. The representative from the TPA brought a financial representative to only offer "suggestions" on what to add to the fund lineup because the TPA didn't have the proper licensing to give financial advice or serve in any fiduciary capacity. I called this tactic, the "wink and no promise" because the provider is winking to the plan sponsor on what investment options to select, but the plan sponsor cannot legally rely on these suggestions. Why should a plan sponsor select an imitation advisor that they can't legally rely on when they can get the real thing?

Even if a retirement plan sponsor has a financial advisor, the plan sponsor is required to make sure that the financial advisor is doing their job. There are too many financial advisor who "mail it in" by not assisting the plan fiduciaries in developing an IPS, in reviewing plan investment options, and offering education to plan participants. A retirement plan with a financial advisor that is not doing their job is the same as a retirement plan with no financial advisor because in both cases, the plan sponsor is not being protected. Would you still go to a dentist who never bothered to check your teeth? So why still use a financial advisor who doesn't help drafting an IPS and/or offer education to plan participants?

A person can't be their own personal doctor without having a medical degree. A retirement plan sponsor can't be their own financial advisor for their plan without having a securities license. A retirement plan needs a financial advisor to enable plan participants to increase their retirement savings and to minimize the plan fiduciaries' fiduciary liability.

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