

This is What a TPA Does and Why a Retirement Plan Sponsor Should Hire a Good One

By Ary Rosenbaum, Esq.

One of my favorite movies of all time is *The Deer Hunter*. It's a story about the Vietnam War and the post-traumatic stress disorder a group of friends from Western Pennsylvania who were drafted together and fought alongside each other suffer from after the war. There is a scene where Robert DeNiro's character threatens the character of John Cazale (who died shortly after filming and who appeared in only five movies, all nominated for Best Picture) by holding up a bullet and saying: "This is this. This ain't something else. This is this. From now on, you're on your own." The problem for retirement plan sponsors is that they don't know that this is this, so they don't what their third party administrator (TPA) does and why they need to make sure their TPA is a good one because this isn't something else and because a plan sponsor will pay the price in penalties, headaches, and increased liability by hiring a bad TPA. So this article is this, an explanation of what a TPA does and why they need to hire a good one.

What is a TPA and why only a good TPA should be used?

As discussed, a retirement plan TPA is a third party administrator for a retirement plan. Easy to understand? Not really because many plan sponsors forget that the TP (TP, not teepee) in TPA means third party, so the plan sponsor (unless they select someone else) is the plan administrator. What does it all mean? It means that no matter what a terrible job the TPA may or may not do the plan administrator is responsible for those errors. Sure, any

poor performing TPA can get sued by a plan sponsor, but the plan administrator (usually the plan sponsor) will still be sued by plan participants and/or the Department of Labor (DOL). I had a client who hired a TPA for their plan and the TPA never bothered to prepare any valuation reports or proper distribution forms, so the DOL sued the company and the plan trustees (personal liability) for \$3 million because the DOL claimed money was embezzled by the plan sponsor's owner. So that is why plan sponsors need to hire quality TPAs and review their work to ensure competence because the plan sponsor will be on the hook for any huge plan administrative errors. A plan sponsor shouldn't

larger 401(k) plans and some only handle defined benefit plans. Some may offer the administration of all different plans for the medium plan segment, while some specialize in cash balance plans. In addition, the role of your TPA may actually be split between two providers where one serves as the record keeper by processing the funding of the plan and the investment trades while the one identified as the TPA performs all the compliance testing and prepares the Form 5500. Whichever TPA you have, make sure it's the right fit for competency and cost.

Fees are important, but don't fully focus on them

Thanks to the fee disclosure regulations that were implemented in 2012; there has been an emphasis in the retirement plan industry to concentrate on fees. The reason is that with the



hire a TPA just because they also happen to be their payroll provider; they need to hire a TPA that will make their lives easier through competent administration, efficient plan design, and expertise at a reasonable cost. Plan sponsors only know how bad their TPA is when it's too late.

They come in all shapes and sizes and handle plans of all shapes and sizes

There are TPAs in the marketplace with thousands of employees and there are TPAs where the only employee is the owner and there is nothing wrong with that because no TPA is the answer for everyone because there is not one TPA who can handle plan of all different types and sizes. Some TPAs only handle

disclosure of TPA fees, there may be a sticker shock for many plan sponsors who assumed all along that they paid nothing or next to nothing for plan administration. While fee disclosure is sort of like Drew Carey revealing the price of a washing machine on the *Price is Right*, the Plan Administration Price is Right can only be determined by looking at what other TPAs charge to gauge whether the price is right or not. So while the responsibility is on plan providers like your TPA to disclose all their fees, it is your responsibility to gauge whether those fees are reasonable. The problem with that point is that some of the low cost TPAs have had plan sponsors consumed with cost. The regulations require plan administration fees to be

reasonable, but not the lowest cost. Having been an ERISA attorney for almost 16 years and working for TPAs for 9 ½ years, I can attest that the quality and competency of a TPA is far more important than cost. I have seen too many plan sponsors who have picked a TPA solely on cost, only to lose that savings by paying a new provider and yours truly to correct the errors set by these TPAs. Low cost TPAs are low on cost, but many are low in quality which means they make many administrative errors and/or they do not have the sophistication in plan design in creating retirement plans that fix the needs of the plan sponsor in maximizing tax deductible contributions. In addition, some of the larger payroll providers have entered the TPA business. It wouldn't be an issue if these payroll providers were performing quality work as a TPA, but as of now, they are not. Quality TPA work has very little to do with payroll, and these payroll providers are not very good in the nuts and bolts of proper administration and intricate plan design. This is not to suggest that payroll providers can never be good TPAs, it just means that currently they are not.

What do TPAs do?

TPAs are the most important cog in the retirement plan machine because they handle the nuts and bolts in making sure that the retirement plan remains qualified under the Internal Revenue Code which means that they help preserve the tax deferral status of the contributions set aside for the retirement of the plan participants. The rules of qualified plans are quite intricate, they require important mathematical calculations called compliance testing to ensure that the retirement plan being tested was not set up to discriminate against non-highly compensated employees by placing limits on how much highly compensated employees can benefit as compared to the non-highlys. In addition, the TPA completes a Form 5500 for the plan sponsor's electronic filing. This Form 5500 is an annual tax return required for all retirement plans that are subject to ERISA. In addition, TPAs often draft plan documents whether they have an ERISA attorney on staff or not. However, the most forgotten role of a TPA is plan design. Good TPAs understand the limits set forth by the Internal Revenue Code and can craft plan designs that can maximize contributions to highly compensated employees within the limits of the law. Good retirement plan

design is an art form that should not be discounted if you are a plan sponsor that has the wallet to support contributions to your employees.

Garbage in, garbage out

For its annual compliance testing, a TPA will ask you for information including a census of all employees which typically includes the participant's name, date of birth, date of hire, date of termination (if any), and compensation. In addition,

they will ask you for information about the ownership of the plan sponsor and who may be identified as a key employee (not a key to the success of the company but a key employee as defined under the Code). In order for the compliance testing to be correct, the data you submit as part of the census needs to be correct as well. The reason is that except for the good TPAs, the information on the census is not checked and incorrect data leads to incorrect compliance testing. So while a good TPA will check data that seems flawed, many TPAs do not. So while plan sponsor get up in arms that their TPA didn't check whether the data the plan sponsor submitted is correct, many TPAs state in their contract that they are not responsible for any incorrect information that you provide. So while they should check to see if the data is correct, the onus is on you to provide complete and correct data on the TPA's census request form.

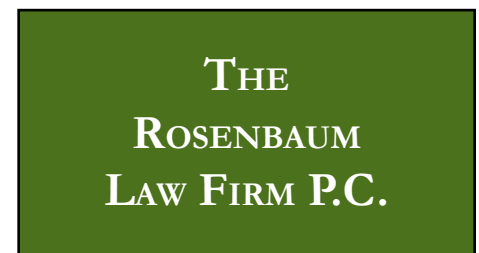
Conflicts of interest for the TPA can exist

Some TPAs not only perform retirement plan administration, they also are involved in ancillary services such as plan document drafting and offering investment advisory services. These other services can lead to conflicts of interest for the TPA which may impact the level of service and duty owed to you. While many TPA legal departments are staffed by ERISA attorneys, it should be noted that they owe

you no attorney-client relationship. So if there are issues that the TPA caused that leads to costly compliance fixing, their initial role is to protect their employer, the TPA. As stated, some TPAs have affiliated companies that offer investment advisory services. A conflict of interest can always occur when the affiliated advisory service offers an investment lineup that was created mostly to offer the highest revenue sharing payments paid by the mutual fund companies to the TPA to offset expenses. This action helps the TPA, but may cause plan participants to suffer by offering lesser quality mutual funds who just got on the fund lineup because of the higher revenue sharing payments they offer to the TPA. This is not to suggest that you should not hire a TPA that offer legal document and investment advisory services, this is just a warning that conflicts of interest may arise from time to time with some TPAs.

How to spot a quality TPA

How to find a good TPA? Ask for referrals, check the credentials of the principals and top people behind the TPA, ask for recommendations from their clients, find out what their client base is, and find out what they know about plan design. Check their fees by comparing what's out there in the marketplace, but based on the services that they provide. Make sure that they are properly insured for any errors and find out if there have been any claims made against their insurance or through litigation, as well as any issues with the IRS and DOL. It may be work to find out a good TPA, but it's better to be safe than sorry.



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