Only 2 Things A Retirement Plan Sponsor Needs to Limit Their Liability

By Ary Rosenbaum, Esq.

People in the professional services industry (legal, financial, or accounting) have a propensity to make something sound more important than it is. Those folks think that by making something sound more important than it is, it might justify their high fees. I don't have the issue because my fees are reasonable and I don't bill by the hour, so I can afford to break down hard concepts into ideas that retirement plan sponsors can understand in managing their retirement plan. So to continue that trend, I am going to show you that there are just two things that will help a retirement plan sponsor avoid fiduciary liability; vigilance and finding the right plan providers. That's it, no brain surgery. If you read this article and take the advice, you'll have a great retirement plan and limited liability exposure as a plan fiduciary.

Vigilance

"In Vegas, everybody's gotta watch everybody else. Since the players are looking to beat the casino, the dealers are watching the players. The box men are watching the dealers. The floor men are watching the box men. The pit bosses are watching the floor men. The shift bosses are watching the pit bosses. The casino manager is watching the shift bosses. I'm watching the casino manager. And the eye-in-the-sky is watching us all." – Robert DeNiro as Sam "Ace" Rothstein in Casino. Sam "Ace" Rothstein would probably say that when it comes to retirement plans, it's the plan sponsor that is the eye in the sky.

As an employer, there are certain functions you want to delegate such as payroll, accounting, and health insurance. Delegating these employer functions will lower your costs and headaches. By delegating these functions to those providers, you also delegate most of the liability that goes with payroll, accounting, and insurance. If those providers make a mistake, their errors & omissions policies will help take care of their errors. The problem with sponsoring a retirement plan is that a plan sponsor doesn't have that luxury. Being a plan fiduciary comes with great responsibility because by sponsoring a 401(k) plan, you are responsible for the retirement assets of your employees. So there is more to being a retirement plan fiduciary than you just simply dumping off your responsibilities on to a retirement plan provider.

What are the responsibilities of being a plan fiduciary? The responsibilities include:

- Acting solely in the interest of plan participants and their beneficiaries and with the exclusive purpose of providing benefits to them;
- Carrying out your duties prudently;
- Following the plan documents (unless inconsistent with ERISA);
- Diversifying plan investments; and
- Paying only reasonable plan expenses.

These responsibilities look simple on paper, but most plan sponsors are unaware of these responsibilities and even when they do, they don't do a very good job of exercising them. They don't do a very good job of exercising them because they think that hiring plan providers is all they really have to do and they don't realize that the buck stops with them as plan sponsor and plan fiduciary. If the financial advisor pulls a Bernie Madoff or the third party administrator (TPA) doesn't understand basic retirement plan administration, they're still the ones holding the bag and getting the blame from plan participants, the Internal Revenue Service and/or the Department of Labor. If one of your providers is rogue, making excuses isn't going to cut it. You're going to have to hang yourself out to dry because you are at fault.

Plan sponsors have to be prudent in exercising those duties and that duty takes a wide variety of different tasks. For example, plan sponsors have been held to have violated their duty of prudence just by having retail fund shares classes of mutual funds when less expensive, institutional share classes. So paying retail when wholesale pricing was available is violating that duty of prudence.

Thanks to fee disclosure regulations, plan sponsors no longer have any excuses as to not knowing how much the plan is paying in fees to their plan providers. However, just getting fee disclosures from plan providers isn't when your job is done. You have to take those fee disclosures and benchmark those fees and the services you are getting against what is out there in the retirement plan industry. It should be noted that fees need to be reasonable and not the lowest. Hiring plan providers just because they charge the lowest fees is a recipe for disaster. They just have to be reasonable for the service provided.

Again, plan sponsors need to be the eyes in the sky. So no matter how great your plan provider seems to be, you need to review their work and make sure that they are doing their job competently. Otherwise, you're going to be the one holding the bag (as discussed above). How do you do that when you have very little knowledge of how retirement plans work? Have it reviewed by an independent retirement plan consultant or ERISA attorney (cough, cough).

Vigilance is all about a careful watch for possible danger or difficulty. Too many plan sponsors are in a coma when it comes to their fiduciary duty, If you are alert about what you need to do, you've won half the battle.

Hiring good plan providers

Most of the time, the difference between retirement plans that run well and the ones with lots of compliance problems is the choice of plan providers. Finding a financial advisor and TPA that know what they're doing goes a long way to making sure that the plan is compliant with all the rules and regulations to minimize your liability as a plan sponsor/fiduciary.

Hiring a great retirement plan provider doesn't mean you have to be less vigilant in your role as a plan fiduciary because we all make mistakes and so do even the best retirement plan providers. These great plan providers will make less mistakes and actually own up to them rather than the not so good plan providers who make every excuse in the book why the error was made.

There are too many financial advisors in the retirement plan space who have very little experience in helping plan sponsors effectively manage their retirement plan. That experience is troubling because these advisors don't understand their role. Helping a retirement plan sponsor is less about picking investment options for the plan and more about helping the plan sponsor manage the fiduciary process. Picking an all star lineup of mutual funds for a retirement plan is nice, but not as important if the financial advisor doesn't help the plan sponsor develop an investment policy statement (IPS) and offer investment education to plan participants (when the retirement plan's investments are directed by plan participants). Then there are those financial advisors who simply collect a fee every quarter without doing anything for their plan sponsor client. A good financial advisor will go along way in minimizing your liability as a plan sponsor because having an advisor who helps you develop an IPS, helps you memorialize the investment choices for the plan, and helps you educate plan participants will eliminate the bulk of that liability risk.

Hiring a good TPA can help you make you sleep better at night as a plan sponsor and perhaps putting more money in your pocket and less money in the government's. While many plan providers will talk about how plan sponsors are getting sued by plan participants, the fact is that most of the plan sponsor's headaches come from compliance issues. Retirement plan administration involves a lot of intricate testing, reporting, and accounting. Unfortunately, errors often occur as a result of a mistake by the TPA and/or plan sponsor. If these mistakes are not detected and corrected early by the plan sponsor and/or the TPA, they become costlier when detected by a government agent on audit. Self-correction program fees are low, when compared to the sanctions government agents get for these very same errors on audit. So a good TPA makes less mistakes that can hurt plan sponsors in the pocketbook.

In addition, good TPAs are very good at augmenting a plan sponsor's ability to save more money for retirement for their employees (especially their higher paid employees). Good retirement plan design is about utilizing the Internal Revenue Code that limit discrimination of contributions to benefit highly compensated employees. A good TPA can utilize safe harbor 401(k) contributions, cross testing/new comparability profit sharing contributions, and the aggregation of a 401(k) plan with a defined benefit plan that could set aside more money for the highly compensated employees than a TPA that didn't have a vast knowledge of intricate plan design.

Coupled with your vigilance, hiring good retirement plan providers will go a long way in curbing your potential liability as a retirement plan sponsor.

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