Blunders That Can Cost A 401(k) Plan Sponsor

By Ary Rosenbaum, Esq.

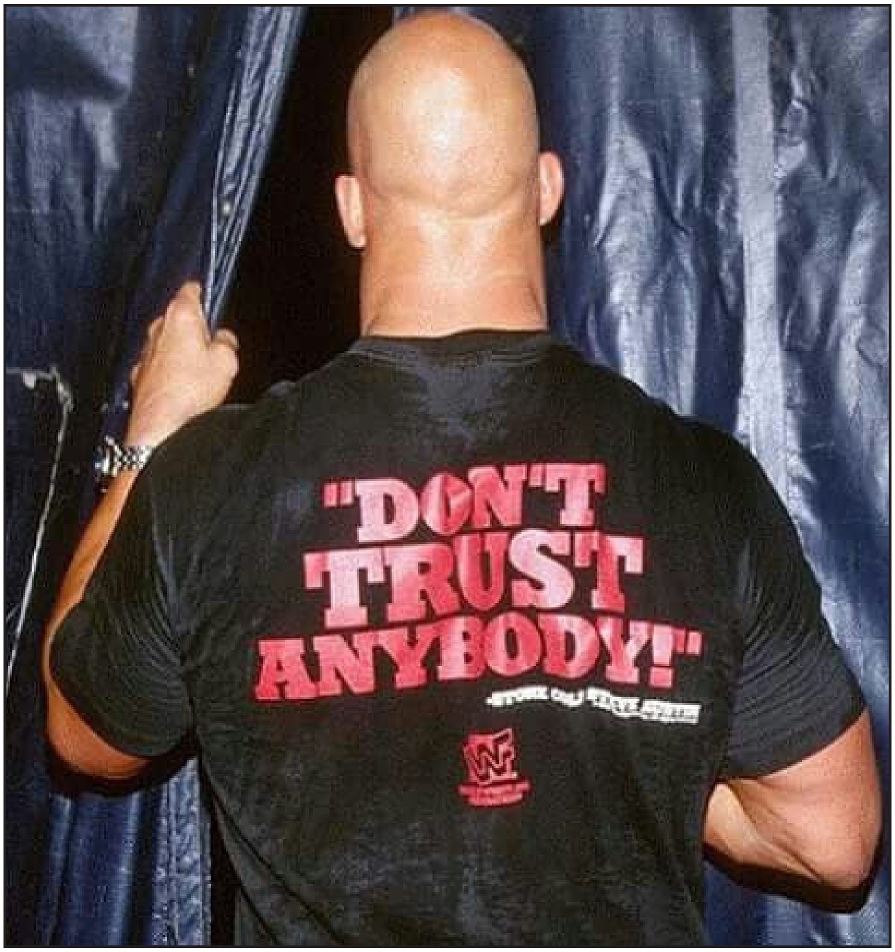
A blunder is a stupid and careless mistake. History is filled with well-known blunders, such as Excite not buying Google and Blockbuster Video not buying Netflix. In 1962, record label Decca was looking to sign an up-and-coming band. They auditioned two young bands at their studios in London, deciding to sign Brian Poole and the Tremeloes. The band they rejected? You might have heard of The Beatles. Blunders you make as a plan sponsor won't make the history books, they will just cause you headaches and possibly cause you financial harm. This article is all about the blunders to avoid now as a 401(k) plan sponsor.

Placing too much faith in your plan providers

My favorite professional wrestler (don't judge me) was Stone Cold Steve Austin. His famous motto was "Don't trust anybody." I'm not suggesting that you don't trust anyone, but I've seen way too many plan sponsors get into trouble because they trusted their plan providers way more than they should. How so? Not reviewing their plan providers for their service and competence and just sitting back and doing nothing. There is nothing wrong with having trust in your plan providers, the problem is when the trust is blind. Trust must be earned and you can't let your plan providers take it for granted. As I always say, you can't be a spectator of your own life, you must be an active participant in the running of your plan, even if you delegate some or all of the fiduciary duties to an ERISA fiduciary. You must always check on your plan providers to make sure they're doing the job that they're getting paid for. You can't take your plan provider's word that they're doing a great job because their opinion is likely self-serving (who says they're doing an awful job?) and your job as a plan fiduciary is to review them.

Being on the cutting edge

When it comes to health situations, especially when it relates to life and death, there isn't anything wrong with seeking medical procedures that are on the cutting edge. I know people who are still alive today with grim medical outlooks because they sought the best of the best in cutting-edge cancer treatments. Unlike grim medical conditions, you can't afford to be on the cutting edge of retirement plan features. I have a defined benefit plan client that terminated their plan years ago but has been audited by the Internal Revenue Service (IRS) for the past year and a half because their TPA pushes defined benefit plan structures to sell life insurance that has been cutting edge for so long that the IRS is once again clamping down on them. Luckily, my client doesn't seem to be on the hook for any sanctions on the value of the life insurance, but so many of the TPA's clients might. As far as cutting edge these days, avoid the hoopla of Bitcoin as some providers will tout them. As a crypto investor, I see the value of it, using my own money. The fact that Bitcoin is well over 50% from its highs is my problem, but it would be a bigger problem if I was a plan sponsor that offered it. I'm a buy and hold investor, most plan participants don't have that patience or understand dollar cost averaging and will sell off as soon as prices go south. I also don't think it's smart to offer an unregulated investment in a heavily regulated 401(k) plan. Note that these observations are before I even talk about the Department of Labor's (DOL's) take on it. The DOL published a Compliance Assistance, which was full of deep reservations about plan fiduciaries that offer it. Included was a grim forecast that they may investigate plan sponsors that offer it. As someone who deals with DOL audits all the time, I wouldn't want a client of mine going through an investigation, just because they wanted to offer Bitcoin, despite the DOL's published misgivings. While the plan providers that offer Bitcoin are still plowing through with their offering, despite the DOL's opinion, it's something I would strongly recommend against. While the DOL's guidance doesn't have the same weight as a regulation and a provider is suing them on this issue, risking a client of mine with the potential hammer of a DOL audit is not something I would do. While one of my favorite Aerosmith songs is "Livin' on the Edge," it's not something I'd recommend to my plan sponsor clients.



Not. being properly insured

Dealing with ERISA-covered plans can be hazardous, to plan fiduciaries. There is always the potential for litigation that could expose a plan trustee or plan fiduciary to personal liability. That's why fiduciary liability insurance is a well-known product and recommended for all plan sponsors. Despite what people think, fiduciary liability insurance isn't legally required, so many plan sponsors don't opt for that coverage. I recommend any plan sponsor with participants that are employees, to get coverage. Unlike car insurance coverage in Brooklyn, it's not crippling. Unlike fiduciary liability insurance, an ERISA bond is required for any ERISA-covered plan. An ERISA bond is to protect plan assets from theft by a plan fiduciary, it is no liability protection for plan fiduciaries. It is legally required and if you answer that you don't have an ERISA bond on Form 5500, I will attest that may be an error that the DOL will use to conduct a random plan audit. Even if you have an ERISA bond, one of the issues is that since plan assets increase, your coverage no longer fits the applicable coverage. The bond must provide coverage for persons handling plan funds in an amount no less than 10% of the number of funds handled by the person in the previous year. The bond amount cannot be less than $1,000 and does not need to be more than $500,000 per plan official per plan (or $1 million for plans that hold employer securities). Make sure the bond you have is an actual ERISA bond, as I know several plans that discovered on audit that their bond was really a crime policy. I hate surprises and as plan fiduciaries, you should too.

Not reviewing fees

If you overpay for services as I've done for home contracting work, that's on you and your problem with what you do with your own money is your own business. What you do with the money belonging to plan participants, well that's something else. As a plan fiduciary, you have the duty to only pay reasonable plan expenses. How can you determine reasonableness? Well, any plan provider that directly or indirectly receives $1,000 or more from your plan must furnish you with a fee disclosure. The problem with the fee disclosure is most plan sponsors take the form and throw it in the garbage or put it in the back of the drawer. Reviewing fees means you need to take that fee disclosure and benchmark those fees against what other plan providers would charge for similar services. You need to remember that fees are about reasonableness, so that means you don't have to hire the cheapest plan provider out there. I will say that hiring a plan provider, just because they're the cheapest is a recipe for disaster too.

Thinking they know it all

Arrogance is an attitude of superiority manifested in an overbearing manner or in presumptuous claims or assumptions. After almost 24 years in the retirement plan space, I can attest that some plan sponsors are just arrogant. The arrogance is manifested in a know it all attitude and the assumption that everything about their plan is fine. Unless they are the greatest plan provider out there, they are just presuming everything is fine. Most plan sponsors aren't plan providers, so if they're not diligent in what they do, there is no confidence that their assumptions about the plan being in order are true or not. As a plan sponsor, it's important to know what you don't know about retirement plans and surround yourselves with good plan providers that do know a lot about retirement plans.

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