Retirement Plan Disasters And How To Learn From Them

By Ary Rosenbaum, Esq.

When a disaster happens, there is always a need for an investigation to see what went wrong and what can be done to avoid similar disasters in the future. We have learned so much from airline crashes to the point that it's much safer to fly than at any time in aviation history. While nothing close to disasters that cost lives, I have seen enough retirement plan disasters and what needs to be done in the future to avoid retirement plan disasters in the future. Here are some of the epic retirement plan disasters I've personally seen and what you can learn from the future.

When a story just doesn't add up

I heard of Matt Hutcheson and I think it should have been a warning when I was interested in speaking at one of his fiduciary seminars in New York City and his fiduciary partners wanted to charge me $1,5000 to attend. Matt Hutcheson become well known in the 401(k) industry because he was a focus of an episode of PBS' Frontline. Matt parlayed his fame into a set of multiple employer plans he set up with various plan providers. I thought nothing of it when he asked me to succeed as the fiduciary of one of his multiple employer plans (MEPs) since his time was being taken up with health care reform. It was 2012 and my firm was only 2 years old, so I was struggling and I thought working with him would be a financial boon to me. I never asked how big the plans were or what my fee would be. There were two warning signs that I neglected: he told me he was under consideration to be the next Department of Labor in an Obama or Romney administration (which I thought was a joke) and he told me that he had a falling out with his fiduciary partners, so I shouldn't get involved in a discussion with them. As part of a press release announcing my appointment, I lauded Matt for his work. An attorney representing a dentist reached out and claimed that the dentist's 401(k) balance was moving from another MEP to my MEP and that the assets never arrived. I thought that must be a mistake and Matt indicated that there was an issue concerning the liquidity of an investment made in the other MEP and that the dentist was being unreasonable. Matt also claimed he was in contact with Phyllis Borzi the head of the Department of Labor's (DOL) Employee Benefits Security Administration, so everything was fine. The only problem is that there was a DOL investigation since the dentist made a complaint about 4 months before I came on the scene. One of Matt's former fiduciary partners reached out, he was stiffed on money owed by Matt (there was litigation), and he just didn't feel he could tell me what was going on. The problem with continuing a fraud is trying to keep the story together and some critical details were coming out. Eventually, the DOL discovered about $3 million that was missing from the two MEPs that I didn't control as Matt was trying to use that money to save a ski resort in Idaho. Since I had fiduciary liability insurance, along with the two other fiduciaries running the MEP that Matt didn't steal from, I was still being sued until the insurance company cut the dentist a check for us to leave the case as Matt was convicted and sentenced to 17 years in federal prison. Matt complains to this day that he was set up by the President Obama administration, but Matt defrauded the people that entrusted him as a plan fiduciary. The lesson from this disaster is that if plan providers tell your stories that don't add up as to where your money is, ask the DOL for help.

The TPA that gives bad advice and gets you sued

A DOL audit is rarely good. Some are random and some are based on participant/employee complaints. About 10 years ago, I was recommended by a certain Third-Party Administrator (TPA) to help represent an owner of a defunct company that had a defined benefit plan being audited by the DOL due to complaints of employee complaints about why they weren't covered by the plan. While the DOL was examining the plan for one complaint, I realized the focus of the audit was changing. During that time, the owner of the

TPA died. The details of what happened with the plan died with him. Despite working on the defined benefit plan for 25 years, the TPA provided no valuations, no benefit statements, and no determination on which employees had accrued benefits. According to the owner, the TPA said that the owner had the bulk of accrued benefits. The TPA also told her it was OK for the owner to write a check from the defined benefit plan's checking account to another wholly owned subsidiary since it was the owner who had almost all the accrued benefits. It was probably the worst advice I have ever heard a TPA give. Since there were no valuations and the exclusion of the complaining employees didn't seem proper, the DOL assume that the owner embezzled millions from their plan. Rather than settle per my advice, the owner of the company listened to her long-time litigators and contested the lawsuit, which ended up costing the owner, millions plus who knows how much in legal fees. The lesson from this disaster is to make sure your TPA is doing its job and has proof to back up its work, especially annual valuation reports.

Thou shalt not steal

I was at that semi-prestigious law firm when I got a referral about a former business owner who was being contacted by the DOL. The business owner showed up at my office and said his family business of franchised restaurants went under and he was being contacted by the DOL for failing to file annual Form 5500s and for paying participants out. The former owner nonchalantly told me that used the assets from the defined benefit plan for personal use, including renovating his house. At that point, I brought in one of our criminal defense attorneys to consult him. The criminal defense attorney told him about the issues regarding federal sentencing guidelines and that it was advisable he comes clean to the DOL. I suggested he cooperate with the DOL because they were already on his tail and would likely discover the embezzlement quickly. The former business owner ignored my advice and walked out the door. Months later, he was arrested by the Department of Justice, convicted at trial, and sentenced to 3 years in jail. Stealing from a retirement plan makes no sense since trust statements would divulge all about the embezzlement. In addition, when seeking legal counsel after committing a crime, listen to advice because criminal activity isn't smart.

You can't your plan providers more than they are entitled to

A plan sponsor changed TPAs, so my services as an ERISA §3(16) fiduciary were no longer needed. I never take that personally, especially firing that TPA. Months earlier, the TPA paid the ERISA §3(38)'s fee to me. Recognizing I was overpaid, I held the fee in my attorney escrow account and returned it when the TPA recognized the error. A plan fiduciary can never accept more money than they are entitled to and a plan sponsor can never pay a plan provider more than they were contracted to. Well, that didn't stop someone. The advisor to the plan switched firms and that was after the advisor discovered that his former firm was paid 4 times the fee they were entitled to. Instead of a quarterly fee, the former firm was paid its annual fee for that quarter. The advisor switched firms and had the chutzpah (nerve or gall for those who don't know Yiddish) to suggest I pay for the error even though the TPA didn't alert me as to that fee payment. I suggested to the advisor that he simply can have his old firm return the fee since they were overpaid. Rather than take my advice, the advisor had the plan sponsor contact me and demand I refund the plan for the error. Notice, no one suggested the TPA pay for the error and I never did since the advisor's old firm had to return the money. Putting on the foil (obligatory Slapshot reference), I told point blank to the plan sponsor that the advisor's old firm committed a breach of fiduciary duty and a prohibited transaction by not returning the overpayment. I also told the plan sponsor that they will have helped commit a prohibited transaction by overpaying the advisor as well. I gave the advisor, the advisor's old firm, and the plan sponsor to rectify the prohibited transaction by the end of the week or I would report the matter to the DOL as a former plan fiduciary. Needless to say, the advisor's old firm, the advisor, and the plan sponsor played ball and the advisor's old firm agreed to refund the overpayment. As a plan sponsor, it is your fiduciary duty to pay only reasonable fees. Paying excessive fees knowingly is a breach of fiduciary duty and a prohibited transaction.

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