What You Should Be Worried About When You "Divorce" Your 401(k)'s TPA

By Ary Rosenbaum, Esq.

The MTV reality series The Real World ends their opening intro with "to find out what happens… when people stop being polite… and start getting real." As an ERISA attorney working with retirement plan clients, I often find that what determines a good third-party administrator (TPA) from a bad one is when we find out what happens when the TPA gets fired, and we start getting real. This article is all about contemplating, divorcing your TPA.

Remember the kids (the plan and the participants)

Divorce isn't easy. I don't know personally since I'm almost 20 years married to wife number 1. For friends and relatives who went through it, I understand the problems, headaches, and expenses, of dealing with divorce. If you have kids, the rule of thumb of a divorce is to not forget the kids. The same can be said about firing your TPA. While you may want to end a relationship with the TPA, don't forget about the plan and the participants. As a plan sponsor, you are a fiduciary, so your main concern should be the effect of any TPA termination and the effect on your plan and the participants.

TPAs get fired for lots of reasons

Why you may want to change TPAs has nothing to do with me. It's your call and it's something you thought about. TPAs get fired for multiple reasons and for a good chunk of the time, it's not for a lack of competence. TPAs can get fired for higher fees, a change of advisors/brokers (who want to make the change), or because the brother of the law firm's partner works for the mutual fund company that will now be the new TPA. So it's business, not personal.

It might be personal to them

While hopefully, the reasons for terminating the TPA aren't personal (you are a fiduciary, with the task of being careful with plan assets), they may be personal to the TPA you are going to fire. I fired a TPA a few years back for a variety of reasons on a multiple employer plan I run. The owner of this Florida TPA was a TPA owner in New Jersey and probably paid multiples on the revenue that the Florida TPA made on my plan. This TPA owner took it personally and tried to steal money from the plan through duplicative fees and excessive deconversion costs. Two years later, the matter is still under Department of Labor (DOL) investigation. Just because you're trying to move on and be civil about it, they may not.

The Good TPAs and the bad ones.

It's easy to determine who the good TPAs are from the bad ones. The good TPAs will not take their firing personally and will try to make the transition to a new provider as seamless as it can. I think reputation means everything and since it's such a close-knit industry, making it easier for a former client to transition business away from you will only help a good TPA's reputation. Also, there is always the chance that the former client may be the TPA's client once again, especially if the new TPA fouls things up. I know a local TPA that was fired by a plan sponsor that wanted to save a couple of bucks by signing with their payroll provider for TPA services. After that failed, the plan sponsor client went back to the former TPA because there were no hurt feelings. I always believe in the concept of paying it forward, that making it easier for former clients to leave will only make it easier for new clients to come in. The good TPAs will also spell out in their original service agreement with the client, the exact cost (if, any) of the de-conversion when the TPA is replaced. The bad ones are easy to spot. They take things so personally and they feel the need to take out the frustration of being fired on the former client. Again, it's business, not personal. I had a client who changed TPAs a few years back. During the change to a new TPA, an Internal Revenue Service (IRS) audit discovered that the Top Heavy test was done incorrectly because a couple of law firm partners were misidentified as non-key employees. Rather than admitting the error, the TPA placed blame on the client for the error and then whined that the client still did not pay all their invoices, forgetting that the client had spent thousands in legal representation to correct that Top Heavy error.

The deconversion fee

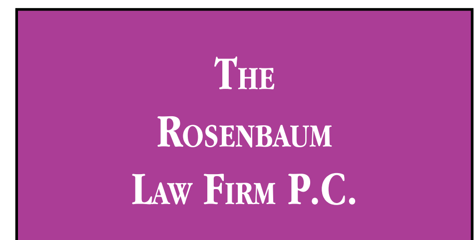
A deconversion from one TPA to a conversion at another is time-consuming and it might dredge up some compliance issues. Going from one TPA to another TPA brings up one of the dirtiest secrets in the retirement plan business that the DOL will eventually tackle: the deconversion fee. If you change lawyers, doctors, or accountants, there is no termination fee set out by the professional you fired. Yet, the retirement plan industry custom is that the TPA being fired has the right to charge and assess a deconversion fee. The problem with the deconversion fee is that most of the time, that charge is not specified in the contract you signed when you hired the TPA. I worked at one TPA where the deconversion fee was silent and it was eventually decided by a co-owner on a whim, dependent on the relationship they had with the advisor on the plan. An advisor who had multiple clients would have their plan sponsor client get a break on it, while other advisors with little business with our TPA, would have the plan sponsor client pay through the nose on deconversion fees once when were. fired. As a plan fiduciary on a multiple employer plan, the TPA wanted to charge us an exorbitant fee to deconvert, as well as try to gouge us to do the valuation and Form 5500 that we had paid for, in our annual fee. While that complaint is still under DOL investigation, I anticipate that the abuses of deconversion fees as well as fees for work past the termination date will eventually be resolved. A well-respected retirement plan industry leader advised that most fee disputes with TPA revolve around these deconversion fees, as well as fees for an annual valuation and Form 5500 where the TPA was compensated on an annual basis.

Know the blackout period

I've gone through two New York City blackouts including the one in August 2003, when. I had to walk 12 miles home. As a plan sponsor, you need to know that a change of TPAs means there will likely be a blackout period. A blackout period is a time when participants will not be able to access their 401(k) accounts because of a change of TPAs and/or plan custodians. During this time, plan participants aren't able to direct their investments, change their contribution rate or amount, make transfers, or take loans or distributions. However, plan assets remain invested during the blackout period. In addition, participants can continue to make contributions and loan repayments, which will continue to be invested according to the latest elections on file. Participants will be able to see these inflows and any earnings in their accounts once the blackout period has ended. A blackout period usually lasts about 10 business days, it could take up to a month. If your blackout period is going to last for more than three days, you're required to send a written notice of the blackout period to all of your plan participants and beneficiaries. The notice must be sent at least 30 days, but no more than 60 days, prior to the start of the blackout. Your new TPA will let you know how long the blackout period will be, as well as provide you with the required participant blackout notice.

Find out who covers what

When firing one TPA and hiring a new one, make sure both TPAs are involved in the process and identify who will do that. In baseball, a flyball needs to be called by a fielder and that call is respected, otherwise, there may be a collision between players or the ball will be dropped. When it comes to compliance testing, the annual valuation, and Form 5500, make sure you and those TPAs can identify who will cover what. There is nothing worse than making a TPA change in the middle or end of the year and realizing that the former TPA isn't doing any of the work they were paid for because they weren't delegated that duty. As a plan sponsor and fiduciary, you can't afford to have any TPA duties, to fall through the cracks.



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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