How Financial Advisors Can Use the 2012 Changes in the Retirement Plan Industry to their Advantage

By Ary Rosenbaum, Esq.

As Professor Barbay said in the movie, "Back to School", there are two types of people in business: the quick and the dead. The most successful businesses are those that either see where the future is headed or see opportunity when there is a fundamental change in their industry. Financial advisors who seek to increase their role as retirement plan advisors can take advantage of the changes in the retirement plan industry to increase their book of business. This article has some tips on how financial advisors can do just that.

The Fee Disclosure Regulations

With mandatory fee disclosure to plan sponsors in April and then plan participants in June, financial advisors need to be prepared to comply with and understand these new Department of Labor (DOL) regulations. First off, every financial advisor should work with an ERISA attorney in making sure their current client service agreements comply with the plan sponsor Section 408(b)(2) DOL regulation (I know a good ERISA attorney who charges a flat $1,000 fees for those). Second, whether it's through the client service agreement or another form of communication, the financial advisor must make sure all fees that they are directly or indirectly is disclosed.

In addition, financial advisors should make sure that the third party administrator (TPA) that their client is using is also making all of the required fee disclosures. Many financial advisors would ask why they have to make sure the TPA is doing their job. The reason that an advisor should keep tabs on the TPA is because they might have referred them and because a financial advisor should serve as an ombudsman for the client as part of its white glove service. The financial advisor should always review what the TPA is charging and help the plan sponsor determine whether the fees being charged are reasonable or not. Again, this is the plan sponsor's responsibility, but the best financial advisors out there are the ones that plan sponsors rely on for many of the facets of the plan that have nothing to do with the plan's investments. Happy clients never fire their financial advisor and simply keeping tabs on the plan will help make the clients happy.

Fiduciary Advice Regulations

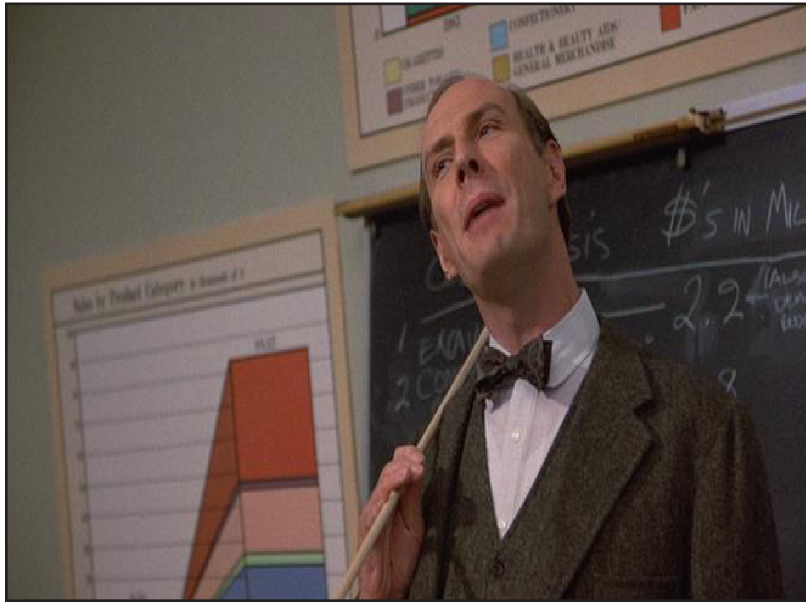
On December 27, 2011, a regulation was implemented by the DOL that finally allowed retirement plan providers to offer investment advice to plan participants and this can be a tremendous opportunity for advisors to consider. Before the new regulation, 401(k) retirement plan providers could not give advice to participants so either the provider or the plan sponsor was required to hire an independent provider to provide advice. That's because ERISA (the Employee Retirement Income Security Act) prohibited advisers from recommending investments to plan participants. Advisors have been able to provide investment education consisting of generic asset allocation models that are not tailored to a particular individual. So advisors could give education, but not advice. This was to avoid conflicts of interest because some advisors were receiving extra compensation by pushing specific investments. There was also concern about bundled providers namely mutual fund companies like Fidelity, Vanguard, and T. Rowe Price who were paid for plan administration but also were deriving revenue from their mutual funds that they offered on the investment menus for the plans they administered.

The reason for this rule change by the DOL is rather simple. Only the largest retirement plans could have afforded to hire independent third party providers to give individual investment advice to participants. So participants of smaller to medium sized plans didn't get advice which is a problem since they were the most likely ones making the investment choices in their 401(k) plan.

This rule change is a win-win for financial advisors who take their role as a retirement plan advisor seriously because being able to provide advice can augment their practice and allow them to stand out among the competition. A retirement plan advisor who understands the change that is going on in their industry can use that to their own advantage.

The costs to provide financial advice under this exemption can be prohibitive and the regulations make it clear that there is no obligation on a plan fiduciary to offer, provide or otherwise make available any investment advice to a participant.

So while a financial advisor does not have to offer advice to plan participants because of its cost, an advisor should make that option available as a marketing tool to maintain and increase their base of retirement plan costs. So if an advisor cannot afford to abide by this exemption, a financial advisor would be wise to use the way advice was used before these new regulations, by having a third party perform that function. Using an on-line advice tool company like the folks at rj20 (rj20.com) can make sure that the financial advisor is getting participants the financial advice they need to make informed investment decisions. This will help participants get a better return on their retirement savings as well as help plan sponsors minimize their potential liability for sponsoring a participant directed plan. Regardless of the approach a financial advisor takes, it would be smart for them to seize the opportunity that this new regulation gives them in letting them stand out among the competition.



The Potential Fiduciary Rule Change and ERISA §3(38) Fiduciary: To Be or Not To Be

In 2011, the DOL withdrew a proposed regulation that would have changed the definition of a retirement plan fiduciary. The significance is that the change would have required brokers who work on retirement plans to become fiduciaries and have a fiduciary duty to those plans. While congressional and Wall Street pressure convinced the DOL to withdraw the regulation, they stated that it is still their intent to promulgate a new fiduciary definition and even applying that definition to individual retirement accounts.

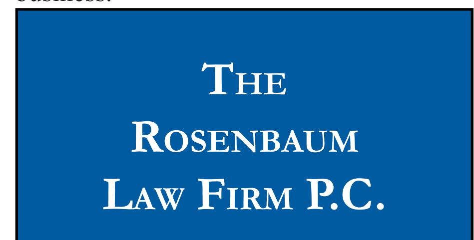
What is the significance of a change in the definition? While retirement plan advisors that are registered investment advisors (RIAs) were always plan fiduciaries, the change would offer brokers three choices on how to proceed if they were considered plan fiduciaries. Brokers would either become fiduciaries, partner up with RIAs and ERISA §3(38) fiduciaries to handle non-fiduciary functions (plus still getting paid on a plan), or leave the retirement plan industry altogether. So there is a significant amount of opportunity for both RIAs and brokers if the rule change is made because many small broker dealers may decide to fold up shop when it comes to retirement plans because of liability concerns if they were considered plan fiduciaries. While the change has not been made, it would be wise for all types of retirement plan financial advisors to pay attention to any changes proposed or made to the fiduciary definition.

In addition, concerns about fiduciary liability for plan sponsors has created a large demand for ERISA §3(38) fiduciaries who are defined as "investment managers" and who assume almost all of the plan's liability in the fiduciary process of selecting plan investments. While brokers can never be a §3(38) fiduciary since they are not an RIA, bank, or insurance company, they can certainly partner up with one. For the RIA, whether to become a §3(38) fiduciary or not depends on whether the advisor is interested in adding that option to their services and whether they have the interest in learning to become one. RIAs shouldn't become an ERISA §3(38) fiduciary overnight and should consider getting training through an organization like CEFEX or being an "apprentice" by partnering up with a §3(38) fiduciary like Loring Ward, Advisors Access, and Millenium Investment and Retirement Advisors. It should also be noted that the ERISA §3(38) service is just an option and may not be a good fit for all plan sponsors.

Partnering Up with the Right Team

I always say that you are only as good as your team, so a retirement plan advisor would be wise to surround themselves with a good support staff. That good support staff should include a couple of TPAs and an ERISA attorney who can help the advisor and their clients in navigating the tough terrain of retirement plan administration. Good TPAs will help design plans that are administered correctly and efficiently by charging reasonable fees and designing plans that help maximize the use of employer contributions. A good ERISA attorney (cough, cough) will serve as a check on the TPA, as well as acting as a sounding board for any legal issues since a retirement plan is a legal entity based on a legal document. Like a shootout in an old Western movie, a retirement plan financial advisor is not wise to go out alone.

Like Eastern Europe after the fall of the Berlin Wall, the retirement plan industry is going through some unchartered waters. The wise and ambitious retirement plan financial advisor will see this as an opportunity to grow their retirement plan business.



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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