

# Retirement Plan Sponsors Have More to Fear Than Fear Itself

By Ary Rosenbaum, Esq.

In his inaugural address in 1933 amidst the Depression, Franklin Delano Roosevelt said that the only thing we had to fear was “fear itself”. 1933 predates ERISA by 40+ years, so FDR clearly didn’t understand the dilemmas of being a retirement plan sponsor. Even today, too many plan providers and too many professionals who have no background in retirement plans calmly tell retirement plan sponsors that the issues regarding fiduciary liability are overblown because they rarely affect retirement plans of similar size. While Chicken Little isn’t telling plan sponsors that the sky is falling, there are enough issues out there that retirement plan sponsors can clearly avoid by reviewing their plans and hiring retirement plan providers that take great care of them. This article is about the actual fears that retirement plan sponsors should anticipate and how good practices can help minimize the threat of those fears.

## It’s all About Fiduciary Duty

Being a retirement plan sponsor is all about being a fiduciary because it’s the highest duty under equity and law which means that you have to treat retirement plan assets better than you should treat your own assets because the bulk of those retirement plan assets belong to your employees. That’s why when you hire retirement plan providers; you’re still at fault when they’re at fault. You have a

broker that shows up every few years and doesn’t help you with your plan; you’re on the hook. The third party administrator (TPA) has failed to do the proper compliance including filing Form 5500s on time, you’re on the hook for the bill for fixing it up. FDR’s successor Harry S. Truman had a sign on his desk that stated “The Buck Stops Here”. Maybe Truman had a retire-



ment plan for his haberdashery business back in Missouri with his friend, Edward Jacobson. Kidding aside, the buck stops with the plan sponsor and so no matter how you try to get rid of your fiduciary liability, you can only minimize it because you can never eliminate it even if you hire an ERISA 3(16) or ERISA 3(38) fiduciary since hiring them is a fiduciary function.

## Don’t let the non-experts fool you.

Have you ever gone to a dentist for an opinion on colon cancer? Have you ever asked an allergist for an opinion on back pain? Of course, you wouldn’t, so why would you ask advice about retirement plans from professionals who have no experience in that space. I’m an ERISA attorney; I’m not going to render an opinion on a criminal matter or a litigation matter. Yet I find many non-ERISA attorneys who tell clients that plan sponsors of their size are rarely the subjects of litigation. That might be true, but litigation from an aggrieved plan participant is just one of many threats to a plan sponsor’s role as a plan fiduciary that can incur substantive pecuniary damage. A retirement plan is like your teeth. If you neglect them, you’re going to suffer a lot of pain and needless expense. Just like your teeth, a retirement plan is going to need checkups and proper care. Don’t overblow the threat to your role as a plan sponsor, but more importantly, don’t neglect it.

## The IRS/DOL Compliance Threat

While litigation from plan participants are the greatest fear for plan sponsors, the more realistic fear is oversight from the Internal Revenue Service (IRS) or Department of Labor (DOL). As a tax qualified plan and a plan subject to ERISA, your plan can be under review of the IRS and DOL at anytime. The IRS looks at plan qualification rules and adherence to the Internal Revenue Code

while the DOL looks at participant's rights under ERISA. You can be under review by the IRS or DOL based on a complaint from an aggrieved participant, but you are most likely under review because of a random plan audit, which is based on you filing the required tax return of your plan, Form 5500. An audit is when many plan errors are discovered such as failed discrimination tests, late deposit of salary deferrals, and missing plan documents. If you are caught with errors during your plan audit, you may be subject to a penalty and/or excise tax. If your errors are substantive, the IRS may disqualify your plan, which may disallow your previous deductions for employer contributions as well as subjecting all retirement plan assets to immediate taxation. DOL's enforcement of ERISA has ramped up over the last few years and will increase because of the fee disclosure regulations. What plan sponsors like you should be aware of is that while fee disclosure regulations help you receive transparency in the fees being charged against your plan, it puts an added burden on you to be more vigilant in your fiduciary duty of paying reasonable plan expenses. The DOL did not enact fee disclosure regulations for the heck of it; they did it to enforce it. They will enforce it through plan audits and make sure that plan sponsors like you review your fees and benchmark them to determine whether they are reasonable for the services provided. Consider litigation from a plan participant as root canal; consider DOL/IRS audits as cavities. That means they are more likely and can cause further decay that can lead to a root canal.

#### **Plan Provider Errors**

As discussed earlier, you end up being on the hook for your plan provider's errors. While you are less likely to be involved in a class action lawsuit by plan participants, you are more likely to have more plan compliance errors because smaller plans generally have more issues with plan provider service than larger plans. So while plan participant litigation costs are quite high, they are more manageable if you have fiduciary liability insurance. There is no such thing as plan provider insurance, so while you may pursue action against your provid-

ers for negligence, you are the one who ends up having to foot the bill to clear up plan errors. Failed discrimination tests, failed compliance tests, and other poor recordkeeping mistakes can set you back

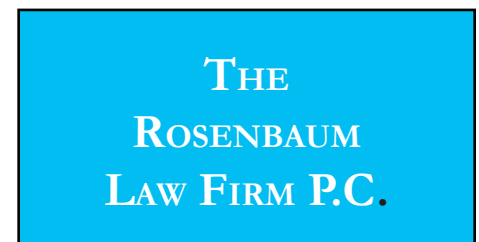


thousands of dollars in compliance costs. A big part of my ERISA practice has been representing clients in the IRS' Voluntary Compliance Program to fix a failure of updating plan documents. The minimum penalty from the IRS is \$750 and increases with the plan's number of participants. I knew a plan sponsor who was sued millions of dollars by the DOL because their TPA did such a poor job of recordkeeping (no valuation reports and no distribution forms) that the DOL assumed they were embezzling money. While plan provider errors aren't as costly as litigation matters, you'll feel differently if you end up being charged thousands of dollars for compliance penalties, excise taxes, and legal costs for fixing plan provider errors.

#### **Plan participant litigation**

Again, many of your non-retirement plan "experts" will tell you that you have

nothing to fear about a lawsuit from plan participants because your plan has a small amount of plan assets. While you are less likely to have a major class action lawsuit, you still have that threat of a lawsuit from and aggrieved plan participant. While your "experts" will claim that no one will go to court for a few thousand dollars worth of damages, some of the threat of litigation from people is not to take you to court, but just get a quick settlement from you (what I call a smash and grab). I remember working at a TPA where an Orthodox Jewish administrator was terminated for cause; he lied about showing up for work on Sundays when the front door records indicate he never was there. This administrator sued the TPA for religious discrimination against two Jewish owners who had bent over backwards for him and netted a \$4,000 settlement because the owners felt that fighting it would cost more money. So while you may avoid a class action lawsuit, a retirement plan with a host of liability issues can be a way for an employee who was terminated for cause to use your failing plan as an excuse to get a quick settlement of thousands of dollars. While you may have been justified in firing this troublesome employee, you still may have to shell out a settlement if your plan is not up to snuff. Regardless of what you do with your plan, always make sure that you have fiduciary liability insurance to insulate against any plan litigation expenses.



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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