Why Your 401(k) Plan Should Get A Tune-Up

By Ary Rosenbaum, Esq.

Cars are built better today and the engine tune-up that was needed after 50,000 to 75,000 miles isn't needed until later on to replace spark plugs and timing belts. However, there are still little preventive things that need to be done to a car to avoid more costly headaches later. When it comes to my cars, I always know that there are certain things I need to do on a timely basis to keep them running. That means changing their oil every 5,000 miles and getting the required state inspection where they usually discover I need new brakes after about 20,000 miles (I'm very generous with the brakes with the exception of my current 2012 Toyota Prius V). I know that if I don't take the car for its timely maintenance to my mechanic Ralph, then I may incur more costly repairs later. If I don't change the oil filter, I can burn the engine and a failure to replace the brake pads timely can chew up my car's rotor (I've done that twice).

Taking care of a retirement plan is like taking care of a car; as a plan sponsor, you have to perform maintenance of your retirement plan. Too many plan sponsors have a "drawer mentality" when it comes to their retirement plan, they put it in the back of their drawer and forget it. This type of mentality exposes the plan sponsor to potential liability because neglect of a retirement plan is a breach of a plan sponsor's fiduciary duty as a plan sponsor. As a plan sponsor, you need to review your plan on an annual basis to determine whether the retirement plan you have in place still works for you. You have the fiduciary responsibility to conduct a plan tune-up to see if the plan's documents, administration, fiduciary process, and expenses are in order and up to date. You also need to review your plan providers to ensure that they are diligent in their duties because, despite your delegation of duty to your providers, you are still on the hook for liability as a fiduciary. As part of my ERISA practice, I offer a Retirement Plan Tune-Up, which is a legal review of the plan terms, administration, expenses, and fiduciary process for $750. Regardless of whether you use the Retirement Plan Tune-Up or not, you should review your plan and here are a number of areas you must review:

Plan Terms: Too many times, a plan document will say one thing and the plan is administered a different way. A retirement plan must be administered according to the terms of its plan document as long as the plan document conforms to the Internal Revenue Code and ERISA. Failure to operate the plan according to its terms is a breach of fiduciary duty and risks the plan to penalties from the Internal Revenue Service with plan disqualification as the ultimate penalty.

Plan Type and Contributions: As a plan sponsor, you should review whether the retirement plan still currently fits your needs and whether the plan's method of allocation should be increased or decreased, based on their economic condition. There are too many plan sponsors with defined benefit plans that they can no longer afford or those with money purchase plans that should have been merged with profit sharing plans when the plan deduction limits for profit sharing plans was increased in 2002. In addition, if a plan could no longer afford safe harbor or other mandatory contributions, a review whether those contributions can be suspended or eliminated should be discussed. In addition, if you can't afford safe harbor contributions to avoid discrimination testing; this is something that should be reviewed. If you're flush with earnings, the third party administrator (TPA) should be contacted on whether another form of contribution allocation or an additional plan should be implemented to maximize contributions to highly compensated employees. Plan design is like a car's fuel efficiency, you need to maximize it to save on taxes and increase retirement savings.

Administration: The administration of a retirement plan is highly technical which requires precise recordkeeping and mathematical discrimination testing. Retire-

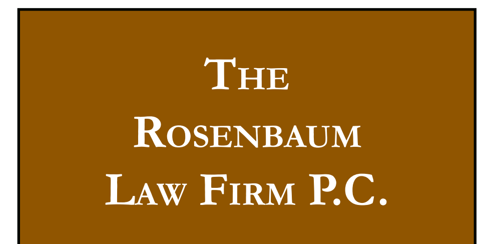
ment plans need recordkeeping and administration to preserve qualification as a tax-exempt entity. So errors in recordkeeping and administration threaten a plan's qualification and can expose you to potential liability from the Internal Revenue Service, Department of Labor (DOL), and plan participants. A review of the TPA's work by an independent party can root out errors that typically are only discovered years later when there is a change of TPAs. I once had a client who was treated by their TPA as a safe harbor 401(k) plan, even though they weren't. Therefore, required discrimination tests for non-safe harbor 401(k) plans weren't completed for a number of years. This serious error by the TPA was only discovered during the conversion process to a new TPA when I asked for discrimination tests that didn't exist. Without the change to a new TPA, I can only imagine how many more years this would have continued that the plan wasn't being administered correctly.

Fiduciary Process: When it comes to retirement plans, there are too many retirement plans without financial advisors to assist them. In addition, there are too many retirement plans with financial advisors who don't assist them. Too many plan sponsors think that the role of a financial advisor is to pick out investment options, no more and no less. So plan sponsors do it themselves or don't expect their financial advisor to do more than investment picking, so many of these advisors get a fee without doing the bulk of the work. The role of a financial advisor is to help a plan sponsor manage the fiduciary process. That entails the development of an investment policy statement (IPS), implementation, and review of plan investment options based on the IPS, as well as giving the education to plan participants if participants are directing their own investments under the Plan. I once did a Plan Tune-Up for a medical practice that had a broker netting 60 basis points (.60% of plan assets) on a $14 million 401(k) plan, which was high. The plan document and administration were in order since it was a safe harbor plan. However, the Plan had no IPS and no education is given to plan participants. In addition, the Plan offered 53 different mutual funds for investment. While offering 53 investment options isn't illegal, it does have the effect of lowering the deferral rate of plan participants because stud-

ies have shown that large fund lineups do overwhelm and confuse plan participants.

Plan costs: A plan sponsor as a fiduciary has the fiduciary duty in only paying reasonable expenses and this was often difficult in a retirement plan industry that wasn't known for its fee transparency. When it comes to using bundled providers or insurance company based platforms, many plan sponsors assumed they paid nothing for plan administration because of the myth of free 401(k) administration. The myth of free 401(k) administration was the belief that plan sponsors only pay the small upfront administration charge which may be as little as a couple thousand dollars or it may be free. They didn't understand that these platforms had wrap fees or expensive share classes that offered revenue sharing to TPAs to subsidize the cost of plan administration. Too many plans (especially that have grown to a nice asset size) were paying more than they should because they are unaware of the hidden costs of 401(k) plan administration. While the DOL has finally implemented fee disclosure regulations that require plan providers such as a TPA to divulge expenses that are directly and indirectly charged, it 's irrelevant if a plan sponsor doesn't take the disclosure and shop the plan around to determine whether the fees being paid are reasonable or not. I once used a contractor for my house who I thought was great, but I didn't realize that his fees were unreasonable until I shopped a simple sheetrock project around to other contractors and I saved $5,000 by using someone else. Nothing requires you to pick the cheapest plan provider, just that you pay reasonable plan expenses based on the services you get. So the only way you can do that is to shop the plan around to other providers. Years ago, I worked on a law firm's 401(k) plan where they thought that they were paying $10,000 in administration services while the TPA was pocketing the $3,000 they were supposed to receive to offset expenses (meaning their actual cost was $13,000 when you factor in the hidden revenue sharing). A change to a new TPA using the same fund lineup, custodian, and broker meant the fees was then $6,000 which was after $3,000 in revenue sharing was used to offset expenses. So the plan sponsor saved more than 50% in plan expenses by shopping the plan around to a new TPA. If you don't know if your fees are reasonable or not, you bear the risk that the fees are unreasonable and subject the plan to fiduciary liability.

As far as reviews, they should be done on an annual basis. They don't have to be full-blown reviews that consultants charge tens of thousands of dollars. The fees for the reviews should be reasonable as well. I remember when an advisor told me that their client was charged $100,000 by another ERISA attorney for a plan review and this was not a plan belonging to a Fortune 500 company. Whether it's the $750 Retirement Plan Tune-Up or a review from other plan providers, you need to sit down and review where the plan stands. Sort of like the State of the Union speech, except without all the pomp and circumstance. You need to be pro-active and nip problems in the bud, rather than being reactive and only fix things when problems are discovered because it's cheaper to be pro-active. A plan sponsor that is on top of their plan is a plan sponsor that is minimizing their fiduciary liability and taking their fiduciary responsibility seriously, be that plan sponsor.



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