Key Concepts You Should Be Aware Of As A 401(k) Plan Sponsor

By Ary Rosenbaum, Esq.

Times change and seasons change. Yet, some things remain the same. When it comes to sponsoring a 401(k) plan, some key concepts never change, whether there is a global pandemic going on or not. This article is about the key concepts that 401(k) plan sponsors need to understand, no matter what period you're stuck in.

Hire a good TPA

I will say until I'm blue in the face, the most important plan provider that you can hire is a third party administrator (TPA). It's important to understand what a TPA does. A TPA does all the compliance testing, allocations, trades, plan document, and plan design work, and files the Form 5500. With so many intricate duties that a TPA performs, mistakes can happen. A good TPA will make fewer mistakes than a bad TPA. Even though the TPA might be at fault for the mistakes they make, the problem is that you'll still be on the hook for liability for any mistakes made. The problem is that many mistakes made by a TPA aren't discovered until there is a change of TPAs and the new TPA discovers it or if it's caught by the Internal Revenue Service (IRS) or Department of Labor (DOL) on an audit. It's costlier to fix errors on your plan years later than when it's first made. That's why it's important to hire a good TPA, rather than one that you hire based solely on cost or convenience.

Hire a financial advisor

There are so many 401(k) plans out there that still don't have a financial advisor working on the plan. I don't understand it, but it's true. While you can certainly invest on your own and maybe you don't need a financial advisor if you have some knowledge on how the stock market works, but as a plan sponsor with employees in your plan, you can't afford to do that. You can be reckless with your own money, but you can't afford to be reckless with the money of your employees. That's because you also serve as a plan fiduciary and that means you have to exercise with the highest duty of care in equity and law. So it makes zero sense for you to handle the investment side of the plan. What kind of advisor do you need to hire? There are so many financial advisors out there that tout their capability of selecting plan investments and managing the fiduciary process of the plan. They'll talk a lot about how they help you by helping develop an investment policy statement (IPS). While these good fiduciary practices are important, they're just a small piece of where your liability can be exposed. Quite honestly, you aren't going to be targeted for class action lawsuits or a lawsuit because the plan doesn't have an IPS, you are likely more prone to liability under a government audit for plan compliance issues. You need a financial advisor that understands how 401(k) plans work and/or find the right people who do. Plan investments are just a small part of what makes a 401(k) plan work or not work. You don't need advisors who are just financial advisors, you need an advisor that will also serve as a plan consultant. Hiring an investment advisor that just concentrates on the plan investments is like hiring a car mechanic that just checks under the hood. Like everything under the hood, there are so many working components to a 401(k) plan that just focus on the investments that were selected, but there is so

much more to a plan than investments. So you don't need an advisor who just checks under the hood, you need an advisor that offers a bumper-to-bumper protection level of service for the plan. What does bumper-to-bumper protection mean? It means the advisor is offering you a service that helps you manage all aspects of the plan which would include vetting the other plan providers (such as the TPA0, reviewing the work of other plan providers (such as the TPA), educating plan participants, and getting other plan providers such as an ERISA attorney when the situation warrants it. Most plan advisors aren't just financial advisors, they are like an ombudsman, Rabbi and Priest wrapped together. You need an advisor who will act as the guardian of your plan and be able to cover all of the bases.

You Need To Get Fiduciary Liability Insurance

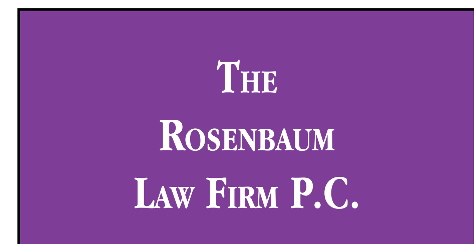
You need to understand the difference between fiduciary liability insurance and an ERISA bond, and why you need both. All retirement plans that are covered under ERISA (if it covers at least one non-owner employee) have to purchase an ERISA bond. An ERISA bond must be put in place by you as the plan sponsor to protect the participants from the theft of plan assets by fiduciaries such you or a registered investment advisor. An ERISA bond offers you zero protection if you get sued over the plan. If you do get sued, it may involve personal liability in your role as a plan fiduciary. Fiduciary liability insurance is a protection policy to defend you from that risk and that risk is litigation brought against you over sponsoring this plan. I once represented a union that sponsored a retirement plan and was sued in a class-action lawsuit over the high fees in the plan that they offered. There was over $1 million in litigation expenses even though my client won the lawsuit through summary judgment. When you get sued and win, you still lose thanks to the high cost of litigation. Thankfully, the union had a fiduciary liability insurance policy, so the union was only responsible for the $100,000 deductible. You must buy a fiduciary liability policy to protect you as a plan sponsor and individually as plan fiduciaries from the headache and potential damages resulting from litigation.

Review Your Plan

You can't have a "set it and forget it" mentality. Once you start a 401(k) plan, you can't just forget about it. A retirement plan is like a car, you need constant maintenance to make sure that your 401(k) plan running in optimum shape. Over time, plan assets change; the demographics of your company change, the stock market changes, and the retirement plan industry change. As a fiduciary with the potential liability that goes with it, you can't stand pat. Every1-3 years, you should have the "hood" of your retirement plan lifted to make sure that everything is in working condition and what needs to be replaced that isn't. That includes reviewing all aspects of your plan including plan design and all of your plan providers to see if what used to work, still does.

Review Your Fees

Most 401(k) plan sponsors that receive fee disclosures from their plan providers don't review them. The problem is that as a plan sponsor and a plan fiduciary, you need to understand what they mean and what you have to do with it. Putting the disclosure in your back drawer isn't an option. You need to determine whether your plan expenses are reasonable and the only way to do it is to benchmark them by using a service, shopping the plan around to other providers, or working with an ERISA attorney. As a plan fiduciary, you have a fiduciary duty to only pay reasonable plan expenses. Reasonableness is determined by the fees paid for the service provided. So you can pay more in plan expenses if you receive a level of service that justifies those fees. Again, you don't have to pick the cheapest plan provider and I believe you make a huge mistake if you hire plan providers just based on them charging you the lowest fees. Some of the lowest cost providers are the lowest quality providers and the cost to fix the errors that these providers cause outweigh any of the upfront savings you may get.



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