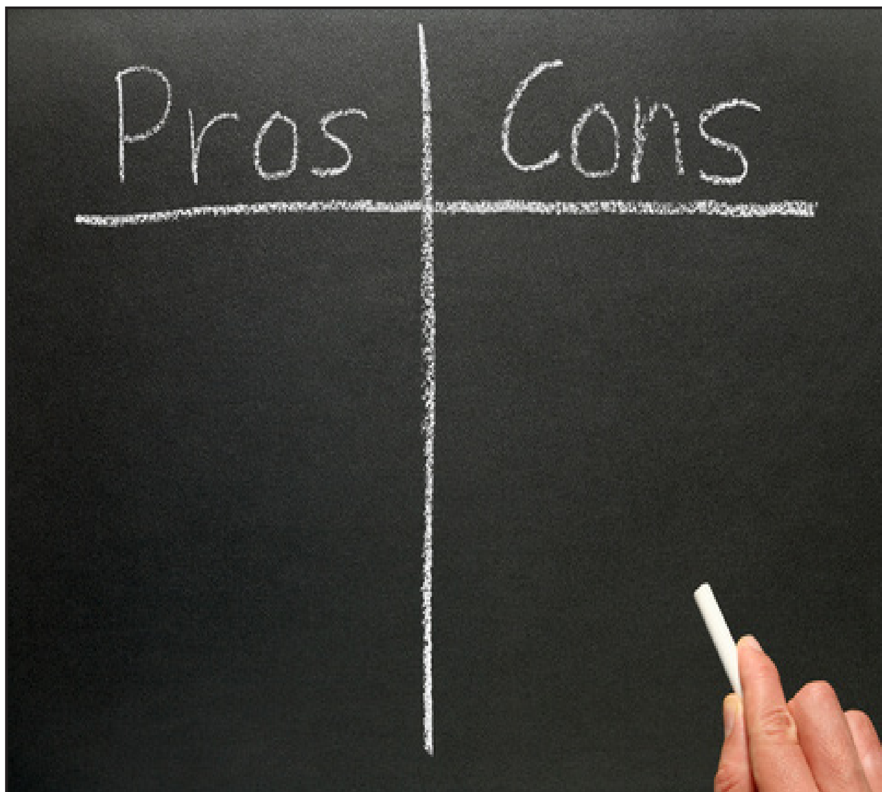
Bad Reasons For Hiring 401(k) Plan Providers

By Ary Rosenbaum, Esq.

As people, we make mistakes and the mistakes we often make is making decisions on what impresses us that really isn't that impressive when you think about it. Substance is always more important than flash, especially when it comes to hiring plan providers for your 401(k) plan. Due to how providers may market themselves to you, you may pick a plan provider for the wrong reason and you're breaching your fiduciary duty by hiring plan providers that aren't up to the job. So this article is about things that plan providers may tout that shouldn't really impress you because it doesn't mean they'll be good at their job.



Their offices and what they drive

I worked at a semi-prestigious law firm and they had fancy offices at the main Long Island location. While the law offices would impress any potential and current clients who would meet our attorneys there, I always would think about the overhead of the firm and how much in fees it would take to support that space. As a plan sponsor, you shouldn't be impressed with the offices that a plan provider has because you either pay for it (as a current client) or you will pay for it (if you hire them). Having worked with and for several third-party administrators (TPAs), I can attest that the fancier the office a TPA has doesn't mean that they're better at the job of day-to-day administration. The same goes with what the salesperson and/or owner of the plan provider drives. Year ago, my good friend Richard Laurita was a top salesman for the TPA I worked for. Richard decided to purchase a Porsche instead of the typical GMC Jimmy who used to drive. I told Richard that it was a bad idea because if I'm a small to a medium-sized employer, I'd question how much in fees I'm paying if the TPA salesman is driving a Porsche. There are a lot of things that should impress you about plan provider you hired or are considering to hire and their offices and what they drive aren't those reasons.

Years of experience

When I first started working as an ERISA attorney 20 years ago, I was working for a law firm aligned with a TPA that some of the law firm partners owned. I used to say that so many of the administrators are people that were hired "off the boat". This wasn't some knock about immigrants (my parents and grandparents are immigrants), it was a joke that we hired people who just graduated college and we didn't do a very good job of training them. Experience is important because you don't want to hire plan providers who just graduated from college, but you don't need to consider decades of experience that a provider has as the most important criteria. You should never discriminate on age or a lack of age. I can attest that I have worked with administrators who had 5 years of experience who were far better than administrators with 20 years of experience. I can tell you that years of experience aren't a synonym for competence. You shouldn't disqualify a TPA or an advisor because they don't have decades and decades of experience because there are a lot of younger advisors and administrators who do a heck of a job better than those with more years of experience. Just like you shouldn't measure golfers by height (obligatory Caddyshack reference), you shouldn't measure plan providers by years of experience.

They do something else

There are many plan providers such as a TPA or financial advisor that happens to do something else. There are many TPAs that provide financial advisory services, just like there are payroll providers and mutual fund companies that provide TPA services. There are financial advisors that provide banking services, just like there are banks that provide TPA services. Providing services to 401(k) plan sponsor can be an ancillary service of what a financial

services company is offering, just like being a TPA is an effective method of distribution for a mutual fund company. Hiring a TPA just because they're your payroll provider or bank isn't a good enough reason. Perceived convenience isn't a replacement for competence as an important criterion for hiring plan providers. This isn't to suggest that you shouldn't hire a mutual fund company as your TPA, it means you need to make sure they can do a competent job at a reasonable price.

The use of acronyms that no one really understands

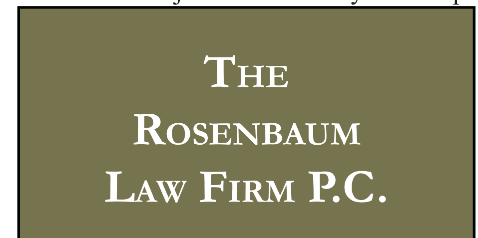
I went to three years of law school and graduated with a law degree. I then went to a tax law program and graduated with a tax LLM (Masters of Law) degree. I took and passed three different state bar exams (New York, Massachusetts, and California). Despite all those accomplishments, I haven't accomplished an acronym. When I talk about acronyms, what I really mean is an acronym that stands for some sort of accreditation. The retirement plan business seems to have been created for the use of acronyms. Whether it's CFP, CLU, QKA, QPA, CEBS, ChFC, CPC, or any other combination of three letters, the retirement plan industry is full of acronyms. I'm not going to put down any of these acronyms because there is a criterion, a testing requirement, and usually a continuing education requirement for these retirement plan industry and financial services accreditations. The fact that some providers have these acronym accreditations after their name doesn't mean that they have more experienced and/or more competent than providers who don't. I once worked at a TPA where the person in charge of the day-to-day operation who claimed to have pension accreditations from American Society of Pension and Professionals & Actuaries (ASPPA), even though he failed to continue with the continuing education requirements set forth by ASPPA. In addition, I know a financial advisor who created his own acronym accreditation that sounds more like a format to watch my iTunes movies than a financial services acronym. While these accreditation acronyms services as a standard that allows plan providers to stand out in the marketplace, I just don't think that is a reason enough to hire plan providers because there are many good and competent advisors who don't spend their money on having a bunch of acronyms behind their name.

They're related to you in business or life

As a plan sponsor, you're also a plan fiduciary and you have a fiduciary duty to do what is best for the plan and its participants. The rules bar you from making plan transactions that benefit you directly or indirectly, those are called prohibited transactions. You can't make the plan engage in a transaction that will benefit you in any way as a 401(k) plan is for the exclusive benefits of its participants, not you. So when hiring plan providers, you shouldn't hire them based on the fact that they are related to you, related to someone you know, or currently have a business relationship with you. Even if the relationship is part of the reason you hired them, I would suggest that you reconsider because any relationship that suggests impropriety is bad in your role as a plan fiduciary. Just ask the publicly traded companies being sued because they hired a large institutional owner as a TPA. Hiring the bank that provides you a credit line as your TPA and/or financial advisor doesn't look good on paper either. You can certainly hire your brother in law as your insurance broker and your second cousin to put out your marketing materials, but you can't hire plan providers just because they're related to you or "juiced in". What looks bad on paper will give people the wrong idea on how you went through hiring plan providers.

They're the cheapest

The fee disclosure regulations set forth by the Department of Labor in 2012 requires plan providers to provide 401(k) plan sponsor with fee disclosures. 401(k) plan sponsors need to review the fee disclosure regulations and benchmark them against what other providers charge. The biggest misnomer about fee disclosure is that plan sponsors need to find the cheapest plan providers. There is no race to zero, a plan sponsor just needs to make sure that the fees that are being charged against their plan are reasonable for the services provided. So it's about reasonableness, not about the cheapest. So hiring a plan provider just because they're the cheapest is an awful idea. You need to make sure that any provider you hire can do the job in a competent fashion and provide a level of service you require. So hiring a provider just because they're the cheapest might be a bad idea if they provide a no-frills service or a service that puts the plan at risk. They are some good low-cost providers, but the reason you should hire them has to be more than just the fact they're cheap.



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