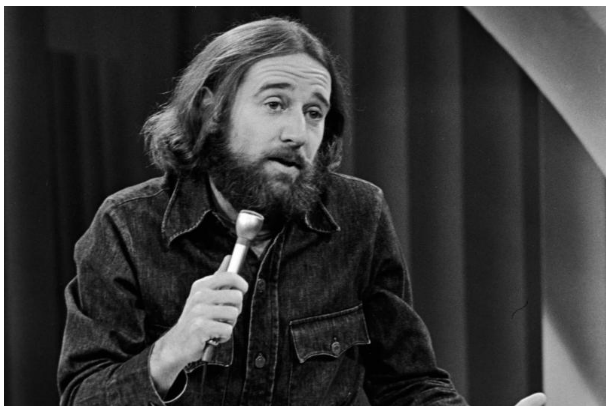
THE ROSENBAUM LAW FIRM P.C.

ADVISORS ADVANTAGE

A Publication for Retirement Plan Professionals

Why 401(k) Plan Providers Should Push Automatic Enrollment.

It just makes sense.



We have a retirement crisis in this country thanks to a Social Security program that has too many retirees to pay to, and the death of the pension plan in the private sector. The fact is that while 401(k) plans are an effective savings vehicle for retirement, they're only effective when employees actively participate by deferring their income. For many reasons, employees don't participate and this is problematic for the plan sponsor because it may impact compliance testing in a negative way and if their 401(k) plans don't achieve critical mass, then they won't get the better pricing reserved for larger plans. So automatic enrollment for a 401(k) plan that automatically enrolls employees who don't affirmatively opt-out of deferring is an effective tool to get employees to save as well as improving the compliance aspects of a 401(k) plan. As a plan provider, you need to take advantage of opportunities and I believe automatic enrollment is something you should advocate for.

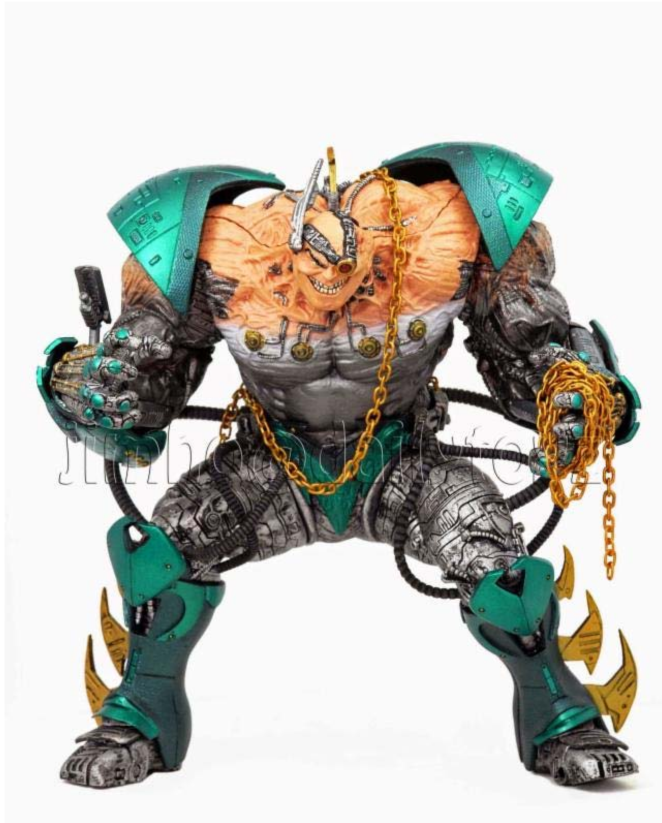
To read the article, please click here.

401(k) Litigation Overkill.

It will come to that point.

The landscape for the retirement plan business has radically changed since when I first started in 1998. Normal courses of business such as revenue sharing and non-transparency of fees were the order of the day. No one cared when the stock market was rolling in the returns.

The stock market in 2000 and the dot.bomb mess as well as the financial crisis in 2008 brought 401(k) fees to



the forefront because when 401(k) returns go south, issues regarding 401(k) plans go north. Thanks to fee disclosure regulations and litigation, the business landscape for retirement plans has radically changed.

The problem with 401(k) litigation is that we're going to come to a point where it's going to be overkill. Sometimes when I see some of the new cases propping up, I think we may already be there or close to there.

Cases like ABB and Edison International have been landmark cases when it comes to fiduciary responsibility; it's corrected some big mistakes that have cost 401(k) plan participants dearly in the past. The problem is that with anything, oversaturation of 401(k) litigation is going to lead to overkill where some providers who aren't necessarily doing anything wrong are going to get sued or already have been sued.

ERISA litigators have to eat too and I think they will eventually start cases on large to medium sized plans where the arguments over plan fees are going to be over 3-5 basis points. Already we have one of the most noted value providers of index funds that has already been sued. Eventually we are going to have litigation that is going to argue over pennies on the dollar that will eventually get tossed at the huge expense of ERISA litigators who took these cases on contingency.

Plan participants have been on a huge winning streak when it comes to litigation over the past 10 years. Like the golden age Celtics, Yankees, and Montreal Canadiens, all winning streaks come to an end. Thanks to fee disclosure and the narrowing 401(k) fees as well as those landmark 401(k) cases, big rip-offs of 401(k) participants are now fewer and far between. I think eventually providers and plan sponsor are going to go on a big winning streak when this overkill in litigation reaches critical mass. You can't get blood from a stone and ERISA litigators aren't going to get big wins from plan providers and plan sponsors over 3-5 basis points.

Revenue Sharing Demolition Night.

We'll look back at how it ended.

When I was a kid in the 1970's, disco was the biggest thing. By 1980, disco was dead thanks to a backlash. People didn't know it at the

time, but disco died the night of July 12, 1979, thanks to the riot during a White Sox doubleheader promotion called Disco Demolition Night.

When I started in the 401(k) plan business back in 1998, revenue sharing was a big thing. The idea that selecting certain mutual funds would "lower" plan administrative expenses when those certain mutual funds "kicked back" a fee to the third party administration (TPA). While we don't have a Revenue Sharing Demolition Night, I believe that revenue sharing is dead.

I have never been a big fan of revenue sharing and I never will because I think it's always been a shell game. Selecting certain mutual funds that pay revenue sharing is a shell game because the funds that pay them tend to be more expensive than those that don't. If plan participants are paying 50 extra basis points in mutual fund expenses just to get a 25 basis point revenue sharing fee to the TPA doesn't save the plan participant any money.

In my mind, revenue sharing is dead man walking because of the amount of litigation brought against larger 401(k) plans where revenue sharing factored into the decision making of selecting plan investments. Plan sponsor have been paying the consequence of using revenue sharing as a basis for selecting plan investments. For years, I have been advocating for a revenue sharing neutral fund lineup because I believe that's the model we've been heading anyway. Revenue sharing is getting the reputation of asbestos except that revenue sharing never killed anyone. Thanks to the rampant litigation, I believe the mutual fund companies will decide that revenue sharing just isn't worth the litigation. Unfortunately, there won't be a promotion like Revenue Sharing Demolition Night.

You can always be a step away from getting sued

It can easily happen.

A well-respected registered investment advisor was recently named as a defendant in a class-action lawsuit against a $1 billion 401(k) plan.

I'm not going to cite the particulars and I'm not going to opine because a complaint filed in Federal court isn't evidence that this advisor did anything wrong. The point is that no matter the processes you put in place or the respect that you have in the industry, you can get sued in a class action lawsuit as a plan provider whether you have done anything wrong or not.

You can never keep your eye off the ball and you have to understand the pressures that come when dealing with plan costs, revenue sharing, and share classes. There are ERISA litigators hunting for plans to sue and these issues I just named are currently the issues being litigated about. Only constant vigilance will keep you more than a step away from getting sued.

Big Fish and Service Provider Lawsuits.

ERISA litigators are chomping at the bit.

It seems like every week, there is another major lawsuit against a plan sponsor and one of their service providers.

Allegations of impropriety are just allegations until decided by a trier of fact of whether they are substantiated or not. Just because a plan sponsor and their service provider is being sued, doesn't mean they did anything wrong.

ERISA litigators have to eat too and sometimes they pick cases that aren't going to put food on the table. I've seen too many lawsuits against some big time plan providers that I know will end up going nowhere because the service provider being alleged to have done something wrong is being sued because the ERISA litigator is considering that service provider is a fiduciary. Alleging that a service provider is a fiduciary is one thing, proving that is a lot harder.

I just saw a lawsuit against one of the big time service provider in this business where the plan participants claim that they are a fiduciary and that they breached their fiduciary duty by farming out their fiduciary duties to another provider. It's a head scratcher because this service provider is pretty careful and I doubt any of their actions as a plan provider made them a fiduciary.

ERISA litigators like to go fishing and they like big fishes like Fidelity and Vanguard. Whether they catch them or not is a whole other story.

The Problem With Providers Using Their Own Funds In Their 401(k) Plan.

It's almost always a mistake.

I always say that I come up with many ideas, but most of them are bad. Seriously, there are so many bad ideas out there in the 401(k) space and one of the really bad ideas out there are bundled plan providers using their own, expensive proprietary funds for their own 401(k) plans. If you think ERISA litigators are sharks, then consider the provider's proprietary funds are blood in the water.

Bundled providers are in the 401(k) plan business and a good chunk of their business is their own proprietary funds. Let's be honest, the reason that so many mutual fund companies serve as a bundled provider because being a provider is a great mechanism to distribute their own funds. The problem is that when you have bundled providers who don't have a sterling reputation as a low cost mutual fund like Vanguard or reasonably priced like Fidelity, there is going to be an issue especially if the provider is an insurance company.

In a new proposed action, two participants are suing New York Life because New York Life is using their Mainstay S&P 500 Index in their own plan. The problem, Mainstay is 17 times more expensive than a Vanguard 500 Index Fund. New York Life's index fund isn't also popular with plan sponsor. A look at 750 of the largest 401(k) plans out there, no of them offered that

MainStay fund while 250 offered a Vanguard Institutional Index fund. This isn't the first time that New York Life had issues with their own 401(k) plan, they settled a $14 million suit in 2008.

The point here is that if a bundled provider is going to use its own proprietary funds in their plan, a cost is one of the most important considerations as well as the rate of return if the funds are actively managed.

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