# The Value Of A Good TPA

## By Ary Rosenbaum, Esq.

When I was younger, my favorite hobby was collecting baseball cards. I'd venture to the local comic book store to pick up some packs and I would cherry pick the rookie cards from the rest of the lot. I would collect the rookie cards which I thought would increase in value, rather than the common cards of bench players. These days, I collect good third party administration (TPA) firms so I can refer my client's retirement plans to them. There is a tremendous value of a good TPA, so I need to cherry pick them from the batch of average or below average TPA firms. Somehow, a good TPA firm is a lot more valuable than a 1988 Donruss Gregg Jefferies Mets rookie card.

**What is a TPA?**

While the plan sponsor is their retirement plan's administrator, they don't have the background or the stomach to administer the plan on their own and make the required governmental filings. That is why the will delegate that role to a TPA, who can properly provide that service as they are staffed with employees who understand the requirements of proper plan administration.

When it comes to retirement plan providers, the most important role is that of the TPA. While an ERISA attorney is important for making sure that the plan maintains qualification under the Internal Revenue Code and the investment advisor makes sure that the investments in the plan are proper, it is the TPA that is the glue that holds the retirement plan together. The TPA handles the day to day administration of the plan, including distributions, discrimination testing, asset reconciliation, and governmental filings. When I speak to financial advisors and warn them that usually the TPA makes the error, it is not a slight to the TPA, but an acknowledgement of how many different tasks that the TPA must complete. The sad fact is that plan advisors and plan sponsors don't understand the value of a good TPA until it's too late, after the plan has been botched by one of those not very good TPAs.

**An Invaluable Service At A Valuable Price**

Retirement plan recordkeeping has no room for amateurs. The rules regarding qualified plans are highly technical and difficult for any non-retirement plan expert to understand. The good TPA offers an invaluable service because their work preserves the tax qualification of retirement plans, thereby preserving the plan sponsor's tax deductions for plan contributions, and the tax deferred status of the participant's retirement savings. Based on their expertise and technological breakthroughs in recordkeeping and processing software, a good TPA offers an invaluable service at a valuable price. Even the more expensive TPAs still provide a good value because while their fees may be on the high side, it still may be reasonable based on the services provided. Plan valuations, discrimination testing, and the preparation of Form 5500 are tedious tasks, but the good TPAs' experience allows these services to be done professionally, efficiently, and cost effectively.

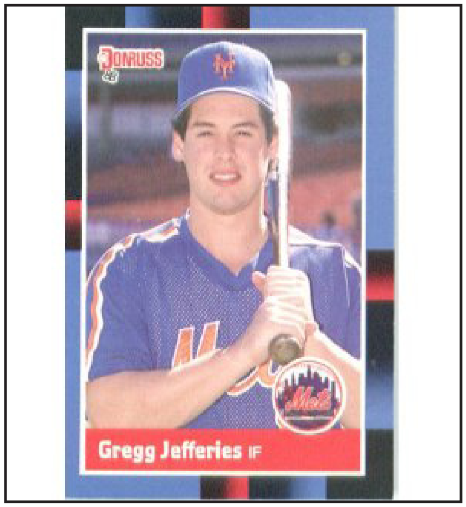
**Saving Money Through Plan Design**

Too often investment advisors and TPAs think about 401(k) and 401(k) only. The problem is that there may be other plan designs or forms of allocation that are a better fit for plan sponsors to increase tax deductions, maximize contributions to highly compensated employees, and allocating any required contributions to rank and file employees. Too many TPAs and financial advisors offer paint by numbers approach to the retirement plan needs of their clients by offering a 401(k) plan with a pro-rata (comp to comp) method of profit sharing contributions, regardless of whether that is the best fit for the plan sponsor. Some plan sponsors can augment the retirement savings of their rank and file while making larger contributions to their highly compensated employees through the use of a cross tested/ new comparability allocation, which offers a minimum gateway contributions to the rank and file and offer a contribution to the highly compensated employees that can be percentage wise, three times larger. The good TPAs will always inquire with the plan sponsor to determine whether that form of allocation is a good fit for them or whether an integrated allocation makes sense. Many professional firms like law firms, accounting firms, and medical practices have added the cross tested method of allocation to maximize contributions, which maximizes tax deductions, and increases tax savings for the plan sponsor.

One of the pitfalls of 401(k) plans is required discrimination testing for both employee salary deferrals and matching contributions. For example, if highly compensated employees as a group defer more than 2% than non-highly compensated employees, the plan will fail the test and the plan sponsor will have to correct that failure by making a make-up contribution to non-highly compensated employees or refund some of the deferrals to highly compensated employees. Needless to say, refunding deferrals to highly compensated employees plus any earnings as taxable income doesn't make a plan sponsor very popular. There is a better way to avoid this problem.

A safe harbor form of 401(k) plan can eliminate this discrimination testing by giving the rank and file employees a mandatory profit sharing or matching contribution that is fully vested at all times. I have seen too many plans over the years that have failed the deferral and/or matching discrimination test without the financial advisor or the TPA bringing the idea of a safe harbor plan design to the table. A perfect example is a client of mine that had their plan administered by one of those payroll providers acting as the TPA. The plan failed the deferral discrimination test and the owner of the company received a refund of $10,500 of her $12,000 salary deferral. What the payroll provider TPA failed to do was inform them of the benefits of a safe harbor plan design, as well as letting them know that if the company only made a $7,500 make up contribution, the owner would have been allowed to keep all her salary deferrals for that year in the plan. Needless to say, this client changed TPAs and implemented a safe harbor design to avoid discrimination failure and salary deferral refunds for the past 8 years. They could have stuck with the low cost, payroll provider TPA, but by doing so, it would have cost them more money in lost salary deferrals and more taxable income for highly compensated employees.

The 401(k) plan is not the only plan in town. 401(k) plans can be augmented with or replaced by a cash balance plan or a defined benefit plan. It depends on the client's needs and wallet. A full service TPA will take a look at the company's census and determine which type of plan is actually the best fit. Sometimes it's a 401(k) plan, sometimes it's not. I have a client who is an attorney and received $500,000 in attorney's fees and wanted to know whether he could contribute more than the $49,000 limit (at that time) in his profit sharing plan, which was handled by one of those discount brokerage houses with no administrative support. Based on his age of 75 and the fact he had no employees, made the implementation of a defined benefit plan a good idea. The TPA I recommended designed a defined benefit plan where this attorney could deduct $230,000 from his personal return as a plan contribution. This attorney would have forfeited an additional $181,000 in deductible plan




contributions if he didn't decide to stray from the discount brokerage firm that gave him absolutely no administrative support. They often say that you get what you pay for; I say that you might end up paying more after paying less. People don't like to scrimp on their health and safety, so why do plan sponsors scrimp on retirement health and retirement plan safety? They don't understand the value of a good TPA.

**They Will Hold Your Hand And Not Steer You Wrong**

I always liken my position as an ERISA attorney to holding my client's hand in sifting through the calamitous waters of retirement plan sponsorship. The same can be said of the good TPA. Plan sponsorship is loaded with potential pitfalls that may cause fiduciary liability to the plan sponsor and the individual trustees. The TPA insures proper plan compliance and helps to minimize the plan sponsor's liability since they have been delegated with the job of handling the plan sponsor's function as plan administrator. The good TPA makes very few errors in plan administration and quickly takes the blame when it's discovered. The not so good TPAs make many errors in plan administration and always blame everyone else when it's discovered. One of the major misconceptions is that if a TPA makes a major error or neglects to properly fulfill their job, then the plan sponsor is off the hook. While a plan sponsor may have grounds in a lawsuit with a cause of action for negligence and/or breach of contract, the plan sponsor an d the individual trustees are still ultimately liable for the plan even if the transgressions were made by someone else's error or neglect. So if the plan sponsor is ultimately responsible for any transgressions of the TPA, is going with the lowest cost provider the best option?

**They Will Be Anything You Need**

The good TPA will not only be the third party administrator, but also a consultant and a major back office support that will help the plan sponsor navigate the calamitous waters of plan sponsorship and limit their liability. I have one defined benefit client who lost all their assets to Bernie Madoff. The TPA did more than what an actuarial firm had to do; they went above and beyond to assist the plan sponsor in their time of need. This TPA helped the plan sponsor through a Department of Labor investigation as well as navigating the mess of the prior TPA. A good TPA doesn't just have to be a third party administrator; they can be a part of your inner circle of advisors.

When looking for a TPA concentrate on their level of service and their expertise, instead of solely concentrating on the amount of the fee. Fees should always be a consideration, but not the sole consideration. Sometimes you get what you pay for; sometimes it costs more down the line by going with the low cost provider.

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