These Reasons Alone Aren't Reasons To Hire A Plan Provider For Your 401(k) Plan

By Ary Rosenbaum, Esq.

When picking plan providers, you must have a rational process in place to that. There must be a variety of reasons why you should select them in your role as a plan sponsor. The biggest mistake you can make in selecting a plan provider is by focusing on just one factor to the detriment of other factors that you should consider. Each supporting factor for a particular plan provider can be explained away because one factor just isn't enough to select a plan provider.

Number of plans on the books

Selecting a plan provider just based on the numbers of the plan that the provider handles is silly. You don't pick a doctor based on the number of patients they have, so why would you pick plan providers on that criteria? McDonald's is the most popular hamburger joint in the United States in terms of locations, but does that mean it has the best burger? I can name a half dozen franchise and chain burger places that are better. Two of the largest payroll providers that are also third-party administrators (TPAs) are on the list of the largest TPAs in terms of plans on the book and I think most of the people in the industry that understand good administration that there is no way they'd put them on a list of quality providers. Besides, those two plan providers tend to have smaller plans because while they are high on the list of TPAs by plans under administration, they are lower on the list of TPAs when we consider assets under management. Bigger is not necessarily better, so picking a plan provider such as a TPAs just based on the number of plan sponsor clients is silly.

Years of experience

One of my favorite scenes from the movie Caddyshack is when Judge Elihu Smails played by Ted Knight interacts with Ty Webb played by Chevy Chase in the lockerroom. Smails is shocked that Ty Webb never keeps score and asks him how he measures himself against other golfers then. Ty Webb says: "by height." It's a funny line but height isn't a real measure of how good a golfer is. One measuring stick that many people use in measuring plan providers is years of experience. That factor by itself is as almost as absurd of judging golfers by height. I have 21 years of experience I don't think that those 21 years make me better than an attorney with 5 years of experience and I say that because when I had 5 years of experience, I would see plan administrators and actuaries with 15-20 plus years of experience who had absolutely no idea of what they're doing. Years of experience don't matter if the experience wasn't any good and the person never had the proper training, to begin with. I worked for TPAs who did little training for new administrators and those administrators would never get better because they never learned how to properly do their job. When I was the head attorney of a TPA before I was 30 (with only 4 years of experience), I replaced an ERISA attorney who had 30 plus years of experience. What good was his experience when he wrote a plan document that required hours of service for a safe harbor contribution (which violates the Internal Revenue Code)? I'm not suggesting some who just graduated from college is a better pick than someone who has 20 plus years of experience, it's just to point out that something as arbitrary as years of experience doesn't mean that's the reason you should hire someone for that reason alone. When picking a financial advisor, you want someone with some experience, but I assure you that you shouldn't pick someone with more experience just because they have more experience because you have no idea whether its good experience or not.

They've won awards

Yes, it's very nice when plan providers win awards. The problem with picking a plan provider just because they won some awards is that you're not sure whether the award is bonafide or not. Speaking as a lawyer, many of those best lawyer awards (especially from magazines) are predicated on the size of the ad that a specific law firm buys in that magazine. I've had several experiences with lawyers that are cited as one of those "best lawyers" and they're far from the best, they would have been on the cover of "Mediocre Lawyers" if such a title existed. Our local Long Island Business News magazine would also put out lists of top business people and top lawyers or lawyers to watch and my old law firm always seemed to dominate these awards. I should know, I was pegged as one of those "lawyers to watch". Don't watch a lawyer, watch your wallet when you see one! I was tapped as one to watch because my old law firm was consistently advertising in the newspaper. They kept on heaping awards on the managing attorney for her business savvy. Under her leadership, the law firm lost three offices and shrunk in half, yet the Long Island Business News has never asked for that award back. Not all awards are jokes, most are legitimately won and are prestigious. The problem is that as a plan sponsor and not someone well versed in the industry, you have no idea which award is legitimate or which one was awarded because of money changing hands. You don't have the time to figure out which award is legitimate and what's not, so don't use awards as the factor in picking a plan provider.

You already do business with the provider

Many plan providers do business in other areas such as banking and payroll. If you're using a bank for your commercial needs, hiring them as a plan provider for just that reason is wrong. Just because your commercial bank does TPA or advisory work isn't a reason enough to hire them. You also want to make sure that any hiring decision isn't perceived as gaining any favor with them. If you're deciding to hire your bank as a plan provider, keep in mind that hiring them might be perceived as trying to curry favor with them. You can't make any plan provider selection that benefits you directly or indirectly such as getting better credit line treatment by hiring your plan as TPA or advisor. Any provider selection that benefits you directly or indirectly is likely a prohibited transaction. Even if you don't getter better credit terms, it still might be perceived as a prohibited transaction. Perception and appearances matter when it comes to decisions you make for your 401(k) plan. Hiring a plan provider just because they happen to do something else for you is never a good idea.

They're related to someone you know

Charity begins at home, but it doesn't begin with your 401(k) plan. Hiring a plan provider just because they're related to someone you know is an awful idea. Again, hiring a plan provider must be through a rational process. So hiring someone just because they were "juiced in" is wrong. If you hire someone such as a plan fiduciary's spouse or child as a plan provider, it is a prohibited transaction.

They're the cheapest

As a plan sponsor, you have a fiduciary duty to only pay reasonable plan expenses. Reasonable doesn't necessarily mean cheapest. Picking up a plan provider just because they're the cheapest is a bad idea. There are a lot of cheap providers that are good and there are also a lot of cheap providers who aren't very good. You need to make sure that any provider you hire is up to the task and just because they're the cheapest doesn't mean that they are.

They are very flashy

Many plan providers do some pretty cool and flashy things. It might be a website or how they present at a plan enrollment/ education meeting. However, those aren't reasons alone that you should hire them as your plan provider. Just because a plan provider has a cool participant and plan sponsor website isn't reason enough to hire them for your 401(k) plan. A cool website or cool marketing materials doesn't prove that these providers are good. It just means they spent a lot of money on technology and marketing, probably because they can afford to. While cool websites might make your job and the job of participants easier, it's just not reason enough to hire them as a plan provider.

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