The Issues With 401(k) Plan Provider Contracts

By Ary Rosenbaum, Esq.

I have been a lawyer for 25 years and for the most part, it's been a fun ride, especially having my own practice for the last 13 years, instead of working for insufferable attorneys (sorry, Lois). Law school was great for teaching me how to think like an attorney, but some of the coursework was useless in my role as an ERISA attorney. Aside from taxation, one of my favorite courses was contracts. Contracts, unlike many legal courses, deal with everyday life. Plus it deals with my role as an ERISA attorney, in helping financial advisors and 401(k) plan sponsors in managing the process of running a plan. This article is all about contractual issues in running a retirement plan.

Before you sign a contract, check them out

Years ago, I needed a waterproofer. I checked Google and found the first provider I saw. The problem was that while they were cheap, their service was horrible. A simple check on my county's licensing agency would have shown numerous complaints by their customers. A deeper Google review would have shown that the person running the company had his wife serve as company owner because he lost his podiatry license for Medicare fraud. Even before you sign the agreement, make sure the providers don't have dirty secrets. Financial advisors, ERISA attorneys, and accountants with multiple complaints should be avoided. I can recall a plan fiduciary who stole millions from his client's plan, that was previously banned from the securities industry. Before even drawing up contractual terms, find out who you will be hiring.

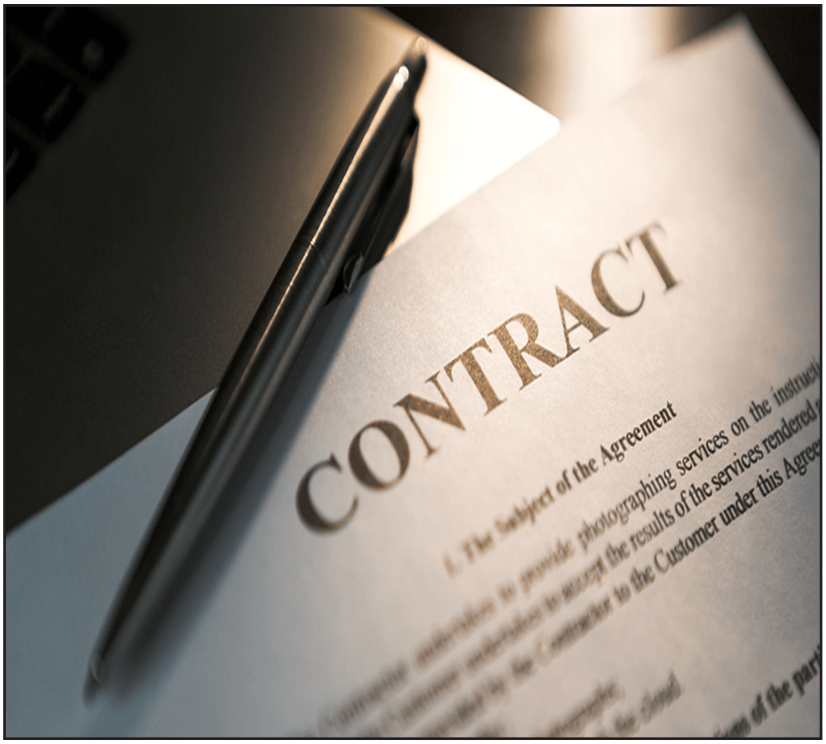
Read the contract

Even as a kid, I always read what I signed. Ms. Rosenblum was right when she said I would become an attorney as my third-grade teacher, while my mother (who claimed that she knew me better than I knew myself) thought I'd be a doctor. My grandmother made that crack about my contract reading as a 14-year-old to her son-in-law who didn't read a pool services contract that cost him dearly in the summer of 1986. Like my Uncle, most plan sponsors don't read their service contracts with plan providers. They go in there blindly, and it's an absolute mistake. A plan provider can promise you the moon in the sales process, but if the contract doesn't include the moon as promised, you just fell for a marketing gimmick. Any agreement to hire a plan provider is a bargain and acceptance, and the contract should detail the bargain and acceptance, the meeting of the minds. In the life of a 401(k) plan, you are going to end up, firing one or more plan providers. So you need to know what you're getting in the contract, the expectations, the services provided, the cost, how long the contract is for, as well as how to end the plan provider relationship. You won't know until you read the contract, and if you already signed it without reading it, you may be in a shock or two.

Call an ERISA Attorney

Yes, attorneys like to make money. We didn't have a vow of poverty when we went to law school. Law school, all in, maybe is $80,000 a year. That being said, a contract for plan provider services has legal ramifications. I think hiring an ERISA attorney to review contracts is a good idea. Contracts can be a tricky thing when dealing with certain plan providers. Some unscrupulous providers may promise something that they aren't going to deliver, by keeping it out of the contract. An experienced ERISA attorney can certainly be beneficial in outlining the terms of the deal and making sure the 401(k) plan sponsor is getting what they bargained for. Listen, I remember the providing third-party administrator (TPA) that had an ancillary financial services advisory firm that claimed they weren't fiduciaries

in their financial advisory agreement, even though they were Registered Investment Advisors and couldn't disclaim that role. While hiring a general business attorney might be a good idea, they don't know ERISA and retirement plans. When Judge Suozzi, the named partner of that law firm I was an associate of, asked me what I practiced, and I told him ERISA, he immediately walked away and said he didn't know ERISA. He was wise, many non-ERISA attorneys are not. Non-ERISA attorneys can't dabble in the retirement plan space because they don't understand something that is quite different and unique. Reviewing a contract shouldn't take a lot of time for most seasoned ERISA attorneys. As someone who likes to avoid clients having sticker shock, any contract review I do has a flat fee that clients know, when they get my retainer letter.



The problem with vagueness and ambiguities

A lot of plan provider contracts aren't very good. I don't know if they were drafted by an attorney or if a plan provider just jotted down some points. The contract should be clear on the duties of what the plan provider, promises to perform, as well as a clear delineation of fees, and any fiduciary role the plan provider intends to serve. The problem with vague and ambiguous contracts is that they're actually held against the side that drafted them, which would be a plan provider. While that might be beneficial to you in the courts, that means you have to go to court. Years ago, as a plan sponsor, I got into a dispute with a third-party administrator (TPA). My 401(k) plan was paying the TPA an annual fee for the plan year that was supposed to include an annual valuation and Form 5500. For 2021, the TPA received $130,000 in annual fees. When I decided to terminate the TPA, effective February 28, 2022, the TPA was insistent that they didn't have to provide the 2021 annual valuation and Form 5500, because that work would be done in July or October of 2022. The TPA wanted to rip off my plan by charging plan participants $80,000 for a 2021 annual valuation and Form 5500 that we already paid for. I was insistent that since the contract was poorly drafted and was clear that an annual service includes a Form 5500 and annual valuation, regardless of when it's performed, the TPA couldn't charge the plan for a fee already paid. The problem is the TPA wouldn't agree and I didn't have tens of thousands of dollars in legal fees to fight them, I called the Department of Labor (DOL) instead. Vague and ambiguous contracts will be interpreted against those who draft them, but what's the point if you have to sue them? Most contracts for services provided for small and medium-sized plans have so little money at stake, that a lawsuit might be more costly than the monetary damages at hand. A good contractual review will clear up any ambiguities and vague terms. You won't know what's ambiguous and vague if you don't have the plan provider contract reviewed.

Firing a plan provider

Like marriage, hiring a plan provider goes with the best of intentions. The problem, like with marriage, these relationships might end. My wife and I celebrated 20 years of marriage a few weeks back, and it bothered some of my relatives that my wife and I signed an agreement on a religious divorce when we got married since Jewish law only allowed me to grant a divorce. A contract with a plan provider needs to be clear when the contract can terminate. There needs to be a termination provision that is clear on timing, notice, and fees. The biggest problem with fees in the retirement plan space, usually deals with termination, especially firing a TPA. As stated before in my situation with a certain New Jersey-owned Florida TPA, you need to know how to terminate the plan provider and what work they will do to transition to a new TPA. The problem in the TPA world is that they are the only plan provider that can charge you for deconversion fees. I think deconversion fees should be already priced into a TPA's fee because most TPAs will be fired or the plan sponsor will go out of business. My biggest problem with deconversion fees is that most TPAs don't spell them out. I'm not asking for TPAs to cite a deconversion fee to the penny, but a range of pricing will be nice. Thanks to fee disclosures and the regulations promulgated to support them, we should have true fee transparency. Yet, when it comes to deconversion fees and termination costs for a TPA, we don't have that transparency for most TPAs. While the DOL is looking at fee disclosures again, my hope is that the deconversion fee loophole that doesn't force a TPA to cite the fee or guesstimate any amount is eliminated.

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