How You May Get "No Respect", But a Lot of Liability as a Retirement Plan Sponsor

By Ary Rosenbaum, Esq.

Aside from health insurance, there is probably no better employee benefit than an employer sponsored retirement plan. On paper, the thought that an employee can save for retirement on a tax deferred basis through employee and/or employer contributions is a fantastic benefit. The problem is that many employees don't understand or appreciate the benefits that an employer sponsored retirement plan can offer. I worked for a law firm that offered a 401(k) plan that gave every employee a fully vested contribution of 5% of their salary and I was amazed that many of my fellow employees didn't appreciate that benefit. Perhaps I had a better appreciation since my old employer offered employer contributions based on a 7 year vesting schedule. Regardless of the type of a retirement plan that an employer sets up, they usually don't understand the gravity and responsibility that comes with sponsoring a retirement plan. They don't understand that many of the issues or problems that go with starting and maintaining a retirement plan including those that they might not even have control over is going to be their responsibility.

A retirement plan sponsor can certainly be like Rodney Dangerfield in getting no respect. If an employer sponsors a retirement plan that is run correctly and allows for a great accumulation of retirement savings, they get none of the credit because as retirement plan sponsors that is what they are supposed to do. When things go wrong for an employer sponsored retirement plan, the plan sponsor as a plan fiduciary is ultimately at fault because the buck stops with them regardless of who committed the transgression under the plan. While plan sponsors may not get any respect like Rodney, it is far more important that they avoid the liability pitfalls that are there for retirement plans sponsors, whether they realize that or not.

Being a retirement plan sponsors mean being a plan fiduciary and being a fiduciary requires a fiduciary duty that is a legal relationship of trust between them and plan participants. A fiduciary duty is the highest standard of care at either equity or law. So when a fiduciary duty is imposed on the plan sponsor and the plan trustees, equity requires a stricter standard of behavior than the comparable tortious duty of care at common law. So as a plan sponsor, you should be aware of the ways you can breach your fiduciary duty and subjecting yourself to liability, even if the transgression is not your direct fault because as plan fiduciary you are always at fault. As Rodney would say being a plan sponsor can give good headache.

Plan Expenses: If you buy an item at a store and find out a competing store is selling it for less, the only punishment is that you feel some grief that you overpaid. As a plan sponsor when it comes overpaying for plan expenses, it can be a breach of fiduciary duty. Plan fiduciaries have been held liable for paying unreasonable plan expenses and even for having more expensive retail share classes of mutual funds when less expensive institutional share class of the same funds were available. As plan sponsors, you should be aware that there will be fee disclosure regulations in April 2012 that will allow you for the first time to find out exactly the direct and indirect fees collected by your plan providers. In addition, in mid-2012, plan participants will get a disclosure of fees as well. One of the major conundrums in the retirement plan industry was that you were not entitled to get fee disclosure from your plan providers, yet as plan fiduciaries you have the fiduciary responsibility of prudence to make sure that the fees that you pay to your providers are reasonable. So many of you have been led to believe that you pay nothing for plan administration because your plan providers make it appear that way by hiding it in your plan investments. So it was hard to find out if the plan expenses were reasonable if you didn't know what they were. Now that fee disclosure regulations will be put in place, at least that conundrum is over. You will also understand the myth of free administration as the providers that charge you "nothing" for plan administration actually do. However, fee disclosure regulations have a downside to it in the fact that it will add more responsibilities to you as plan fiduciaries. The regulations will require you to identify your plan providers, make sure you will receive those fee disclosures, and make sure that the expenses you pay are reasonable. Any failure in your duty may result in the Department of Labor (DOL) determining that the arrangements with your plan providers are prohibited transaction, which is a breach of fiduciary duty and subject you to excise taxes and penalties. The way to avoid this dilemma is ensuring that your plan providers will comply with these regulations and that you will shop your plan to other providers to compare price. Now you are not required to pick the cheapest providers (which you shouldn't do if the quality of service will diminish), just make sure that the expenses you pay for the plan are reasonable as to what is offered in the marketplace. If you don't know about your plan expenses or don't try to determine whether the expenses are reasonable, you will certainly get more than a free bowl of soup, you may get sued by aggrieved plan participants.

Plan Investments: Another one of the major fallacies with being a plan sponsor is that if you allow your participants to direct the investments under their retirement account, you will be not be liable for the financial losses that your participants incur. This fallacy was caused by a misreading of ERISA Section 404(c). Just giving your participants a menu of investment options to select isn't enough, you have to complete a process in order to minimize liability. That process which is part of the process about of being fiduciary is about putting plan participants in a position where they can make informed decisions in choosing plan investments. That means that you have to work with your financial advisor in developing an investment policy statements (IPS) that serve as a Bible on what plan investments should be selected and when they should be replaced. Developing an IPS isn't enough; you need to sit down with your advisor on an annual or semi-annual basis to determine whether the plan investments still meet the criteria set forth by the IPS. In addition, you need to provide plan participants enough information on these investment options. So it is wise for you to make sure that investment education is provided to your plan participants. Now that the DOL will us allow plan providers to provide investment advice to plan participants, it should be provided to them as well. Plan sponsors have been held liable for losses sustained by their participants because they neglected their duties in managing the fiduciary process of selecting plan investments. Even if the plan is directed by trustees, plan sponsors still need to have an investment advisor to help develop an IPS and make those investment reviews.

Plan Providers: When you hire an attorney or an accountant that is incompetent, you have the opportunity to sue for malpractice and the damage you suffered from that malfeasance is the extent of your damages because you are not at fault for the transgressions of the professionals you hire. As a plan sponsor, you don't get off that lightly. While you can certainly sue your incompetent plan providers for negligence, the fact is that as a plan fiduciary, you are still responsible for their transgressions. So if your financial advisor is running a Ponzi scheme or your TPA hasn't filed your Form 5500 for the last 5 years or your ERISA attorney hasn't updated your plan document since the Clinton administration, you are still on the hook for liability because the buck stops with you as a plan fiduciary. Selecting plan providers is a fiduciary duty and clearly, selecting an incompetent plan provider is a breach of that duty. Selecting plan provider is an important fiduciary duty that should not be taken lightly. As a plan sponsor, all plan providers should be selected through a process, simply tapping a TPA or a financial advisor because they gave you tickets to the Mets, played a nice round or golf with you, or are related to you isn't enough. Plan sponsors need to review a wide variety of providers as part of that process. Potential service providers should be evaluated to determine whether they are a good fit for you and your plan. In addition, after selecting a plan provider, it's wise to have them evaluated for service and competence by either hiring a retirement plan consultant or an ERISA attorney. to review them. Too often, plan sponsors are only aware of errors made in the administration of their plan simply when changing providers. I had a client using a TPA for almost 30 years and was being sued by the DOL because the TPA was so incompetent; the DOL insisted the owner of the company was stealing money from the plan. While the owner of the company was insisting it wasn't their fault and how they could have known their TPA's incompetence, they were at fault because they hired the TPA and never bothered to have the TPA's work evaluated. Regardless of the provider you hired, you should always understand that whatever happens, you are at fault if something goes wrong. That is why you need to evaluate and review your plan provider on a consistent basis.

The role of this article is not to scare you from sponsoring a retirement plan; it is just that simply sponsoring a retirement plan is not enough. Like your car, your house, and your finances, your retirement plan should not be neglected. Unlike with your car, your house, and your finances, you may be sued for the damages caused from your neglect. The solution to avoid this problem is hiring a good TPA, a good financial advisor, and a good ERISA attorney. You retirement plan is only as good as your team of plan providers, so take your role as a plan sponsor seriously even if you get no respect.

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