401(k) Plan Provider Marketing Traps You Should Avoid

By Ary Rosenbaum, Esq.

I love marketing and I never took a class on it, I probably learned it with student politics at Stony Brook. They say that marketing s the process of exploring, creating, and delivering value to meet the needs of a target market in terms of goods and services. I love good marketing by 401(k) plan providers, but I hate marketing that takes advantage of plan sponsors because it's disingenuous. So this article is all about the 401(k) plan provider marketing traps you can avoid.

401(k) administration is free

In the days before fee disclosure regulations that were implemented in 2012, 401(k) plan sponsors could reasonably believe they were paying nothing for 401(k) plan administration because their third-party administrator (TPA) didn't have to tell them how much they were directly or indirectly receiving in compensation. For example, a TPA could charge nothing upfront and claim they were receiving no direct compensation from the plan but didn't have to tell the plan sponsor how much they were making in revenue-sharing payments from mutual fund companies. These days, fee disclosures that plan sponsors are supposed to receive from their plan providers will dictate what total compensation they're receiving. However, that is not stopping certain TPAs from still claiming that their administration is free. How can they claim it's free when fee disclosures will say that it isn't? Well, what they don't say is that as the plan's advisor (through a subsidiary), they will be making an asset-based fee. It costs money for a TPA to administer their client's plans, that is why I know quite a few TPAs that went out of business in the past 25 years. So whether they make it through the assets or charge $1,000 for a distribution package, the TPA is making money somehow. Uhura said the cloaked Klingon Bird of Prey must have had a tailpipe in Star Trek VI: The Undiscovered Country, a TPA has to make money on administration somehow. Don't fall for the con.

The fiduciary warranty

My favorite hockey player Mark Messier made a guarantee that my Rangers would beat the New Jersey Devils in Game 6 of the 1994 Eastern Conference Finals. Not only did they win, but Messier also scored a hat trick (3 goals for those non-hockey fans). As a result of the game and winning the Stanley Cup, Messier will never have to buy a drink in New York City ever again. Patrick Ewing of the Knicks made a similar guarantee one year in the playoffs and the team lost, being clutch was never his thing. There are still plan providers out there. that issue is something called a fiduciary warranty, which is free and doesn't protect the plan sponsor from almost any liability because plan sponsors never get sued for what the warranty is supposed to protect plan sponsors from. While a fiduciary warranty is just a marketing gimmick, I never thought it was dangerous. I always saw it as a marking throwaway. I recently received information from my client regarding a plan provider touting their fiduciary warranty that I find to be dangerous. The materials and the email from the plan provider make it seem that a fiduciary warranty can be used as a replacement for a plan sponsor using an ERISA §3(21) or §3(38) fiduciary. A fiduciary warranty "protects" a plan sponsor from liability when dealing with the broad range of investment requirements for plan investments. To quote Montgomery Scott from Star Trek III: "A monkey and two trainees" can meet that requirement. The same goes for selecting the QDIA fund as well. Plans easily meet

the broad range requirement and anyone who can read a Morningstar profile can pick a QDIA. That's far different from what a §3(21) or §3(38) fiduciary does in limiting the plan sponsor's liability with investment selections, fiduciary process, and participant investment education. A fiduciary warranty is worthless as opposed to hiring a financial advisor, which is what a plan sponsor needs. I find it reckless that any plan provider would suggest that a fiduciary warranty can replace the effectiveness of a financial advisor. A fiduciary warranty is worthless but harmless on its own. However, it is marketed and used as some alternative to hiring a good financial advisor, it is misleading and fraudulent advertising.

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Sports

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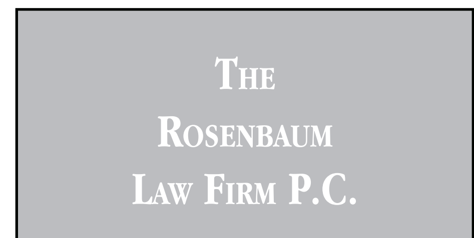
Payroll integration and having your payroll provider be the TPA

If there is one opinion in the retirement plan business that draws the most support and hate is my opposition to hiring the largest payroll providers as a 401(k) TPA. My opinion is my opinion, it's based on 25 years of experience as an ERISA attorney. I believe that the TPA business is a very tough job, it just shouldn't be someone's ancillary business. My problem with payroll provider TPAs is that they require too much of the plan sponsor to do the heavy lifting, aren't very creative in plan design, and take an assembly-line approach to retirement plans. Henry Ford once said you could pick the color of a Model T as long as it was black. Offering retirement plans on some sort of plain vanilla prototype with no discussion of other designs and combo plans with cash balance or defined benefit is malpractice if it costs the plan sponsor money by not maximizing the use of employer contributions. The Mcdonald's approach to fast food is fine, but retirement plans administration isn't something that you could quickly push out. Payroll Provider TPAs aren't a black-or-white issue; I'm sure a three-employee company using a safe harbor 401(k) might be a good fit. For most plan sponsors, it's not. I've seen fewer problems with standalone TPAs than those two big payroll providers in terms of issues and plan errors. Standalone TPAs have less of a churn rate than payroll provider TPAs, they have larger plans, more plans under administration, and are more efficient in plan design. These payroll provider TPAs will tout the importance of payroll integration. If payroll integration is such a big deal for ADP and Paychex, why do they offer that same payroll integration to other TPAs? Payroll integration is something that is a strong selling point, but non-payroll provider TPAs may offer that integration with ADP, Paychex, or another payroll provider that is wise enough not to be in the TPA business.

Free fiduciary service for a limited time

I hate free limited-time offers or a free 30-day trial because it's a gimmick where the offeror is betting the person talking up the free limited offer will forget to cancel the offer when it's no longer free. It's like the old rebate gimmicks where the manufacturer is enticing people to buy a product based on a rebate with the idea that many people will fail to complete the rebate form and mail it in. If you fall for a rebate gimmick or free limited-time offer and use your own money, that's on you. When you fail for a gimmick that costs plan participants, that could be a fiduciary breach. A plan provider offering §3(16) or 3(38) fiduciary services free for a limited time is hoping you will forget to cancel the service before they start charging you. You should pick a fiduciary service because it's the right fit, not because it's free for a limited time.



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