A Good 401(k) Plan Doesn't Grow On Trees

By Ary Rosenbaum, Esq.

It doesn't grow on trees, it's not in the water (especially good bagels), and it doesn't happen by accident. It didn't happen overnight, it didn't happen in a vacuum, and it certainly didn't come out of thin air. A good 401(k) plan takes a lot of work and it happens because there is continued vigilance by the plan sponsor. So this article is about what it takes to have a great 401(k) Plan.

It Takes a Vigilant Plan Sponsor: If there is one common trait of a good 401(k) Plan, it would be a vigilant plan sponsor. Some will say that a good 401(k) Plan is a result of hiring good plan providers. Hiring good plan providers is an essential part of having a good 401(k) Plan, but the fact is that someone has to hire these good plan providers. Hiring good plan providers doesn't happen by accident, a vigilant plan sponsor does their job in hiring quality plan providers. The size of the plan is irrelevant and what the plan sponsor does for business is irrelevant as well. If you think that law firms and medical practices have the best 401(k) Plans, my experience would tell you that you'd be wrong. A vigilant plan sponsor doesn't require an advanced degree; just an understanding that a 401(k) Plan requires fiduciary responsibility and that exercising that duty in a prudent manner will save some headaches. The size of the plan is irrelevant even though smaller plans tend to have more issues because of the lack of vigilance by the plan sponsor. Plans with over a billion in assets have been in trouble in class action lawsuits even though they have countless and countless expensive plan providers. So when it comes down to it, size and sophistication aren't as important as plan sponsors who understand their role as a plan fiduciary and take it quite seriously.

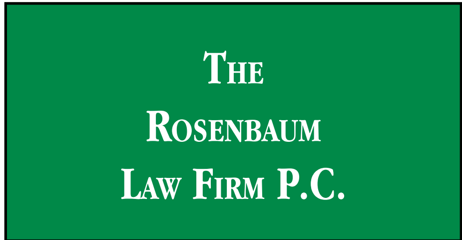
Good Plan Providers: The difference between a good plan provider and a bad one? A good plan provider will make a lot fewer mistakes than a bad one and these mistakes will be smaller in detail. 401(k) Plan administration that a third-party administrator (TPA) works on is an intricate process that requires lots of data, a lot of transactions, and lots of math. So no matter how great the TPA is, mistakes will be made. However, these errors tend to be minor and less catastrophic than the errors created by bad providers such as compliance testing that was never done or plan documents that haven't been updated since the Clinton administration. Who a plan sponsor hires as plan providers can be a determining factor as to how well the plan is taken care of. A plan sponsor needs to hire good plan providers because ultimately, the buck stops with the plan sponsor. If a plan provider makes a catastrophic error or fails to do their job, the blame and responsibility goes with the plan sponsor in hiring them in the first place. Sure, a plan provider can be sued for omissions and errors, but it's the plan sponsor who would have to answer the Department of Labor (DOL), Internal Revenue Service (IRS), or a litigious plan participant. A good TPA will keep the plan in compliance with its reporting and recordkeeping. A good financial advisor will make frequent appearances to advise of the changes in the plan and the investment marketplace, a bad financial advisor never shows up or never advises the plan sponsor as to what investments should stay or what should be replaced. A good ERISA attorney will make sure that the plan documents are in compliance, a bad ERISA attorney will never contact you on any required updates. If you need an audit, a good auditor will not only determine the assets are where

you say they are, but they will advise you of issues that threaten those assets and the qualification of the plan, a bad auditor will be just a rubber stamp on what the other providers are doing.

Avoiding Underhanded Deals: It should be pretty self-explanatory, but it happens more often than I'd like. The purpose of a 401(k) Plan is for the benefit of the plan participant; the assets of the plan are for the exclusive benefit of its participants. So that means that the plan sponsor shouldn't be using the assets of the plan as leverage to make self-dealing transactions or to curry favor. Plan sponsors can't borrow from the plan or use assets of the plan to buy a building or to enrich themselves. That is also true of hiring plan providers. Hiring plan providers should be done through a fair and proper process. Simply using a cousin or other relative, as a plan provider is a bad idea, so is hiring the plan sponsor's bank as a plan provider just to get better terms from the bank on the business side of things. The plan was put in place for the employees; it was not put in place to enrich the employer. So it's important for the plan sponsor to be above reproach and that all transactions dealing with the plan including hiring plan providers should be on the level and free from a conflict of interest. The best plan providers that a plan sponsor can hire are independent and don't owe their hiring for some favor or because of nepotism.

Inform Plan Participants: I worked at a school paper at Stony Brook where our motto was: "Let Each Become Aware." Information is knowledge and the more information that someone gets, the smarter they become. The same can be said with plan participants, especially plan participants who direct their own investment under a 401(k) Plan. Not only is having a plan participant more informed if they direct their own investment good for them, but it also helps the plan sponsor minimize liability A participant-directed plan under ERISA §404(c) will help a plan sponsor limit their liability. The problem is that liability limitation isn't some sort of bulletproof suicide pact. The liability limit is dependent on how much information a plan participant gets from their plan sponsor in directing their investment. With apologies to a former human resources director at a law firm I worked at, simply handing out mutual fund profiles doesn't work. A plan sponsor needs to provide investment education (preferably by a plan provider) that will help a plan sponsor understand the basics of investing. Investment advice can also be offered and that's specific investment advice to a plan participant that would be dependent on their economic position, age, and risk tolerance. Better-educated plan participants have better investment returns than those who do not and participants who do better with their retirement savings are less likely to sue than those who do not. The investment education/advice is also in conjunction with the work of the plan's investment advisor. Sorry again to that human resources director, but that 10 years where investments were not reviewed or replaced before I helped her fix the plan was not going to help them escape liability under ERISA §404(c). A better-educated plan participant is less of a headache than one who isn't.

Constant Review: As my grandmother Rose always said: "life doesn't go to plan." When a plan sponsor implements a 401(k) Plan, they do so at a certain time and place in their business history. So what was good when the plan had 5 employees may not be so good when there were 100. Business needs have changed, the business' pocketbook has changed, and retirement laws have probably changed too. A 401(k) Plan is like a motor vehicle, it needs constant maintenance. Circumstances may change that may require a new type of plan or plan design to maximize or minimize employer contributions. Changes in plan size may also require a change to a less expensive plan investment or a change of plan providers. 401(k) Plans aren't set in stone; economic realities need to make them fluid and open to change when needed.



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