Why the 401(k) Fiduciary Guarantee Should Get The F******** Out

By Ary Rosenbaum, Esq.

One of my favorite sports quotes comes from former Arizona Cardinals Coach Dennis Green who was in a press conference tirade after his team blew a 20 point lead to the Chicago Bears on a Monday Night football game in 2006. Editing for brevity and expletives, Green said: "The Bears are what we thought they were. They're what we thought they were. … But they are who we thought they were! And we let 'em off the hook!"

Retirement plan providers offer a lot of products and services that plan sponsors thought they were and sometimes plan providers try to pull a fast one and try to sell them something that sounds fancy and what they are selling is something that is not what plan sponsors thought they were. Unless surrounded by an experienced financial advisor and ERISA attorney, a plan sponsor could buy a product that is a little more genuine than a three dollar bill and a little less genuine than a magic bag of beans.

With an upswing in lawsuits against plan sponsors and fiduciaries for breaches of fiduciary duty, there has been much talk of the need to implement good practices to limit exposure to fiduciary liability from litigation by participants and/or governmental sanction. These good practices may include the hiring of an independent ERISA fiduciary to assume or assist in the fiduciary process of selecting plan investments, which along with concern over excessive plan fees are the top two reasons that plan participants sue their employer. With a boom in ERISA litigation against plan sponsors, there has certainly been a growth in the use of ERISA §3(21) and ERISA §3(38) fiduciaries who will either share in the fiduciary responsibility (§3(21)) or assume it all together (§3(38)).

While the uses of independent ERISA fiduciaries date back to the signing of ERISA in 1974, there has been a growth in that area because plan sponsors would rather hire someone to share or take over the liability burden, rather than going it alone. As with any popular service or product, there always seems to be someone which comes up with a way to cash in by offering a "knock off" product that is a pale imitation of the original product. As a preppy kid in the early 1980's I recall the popularity of Lacoste alligator shirts which were followed by manufacturers placing foxes and ducks on shirts with less success.

Since plan participants have been inundated with articles and retirement plan providers talking about increased fiduciary risks, a number of bundled plan providers have decided to cash in on this hoopla by offering what they call a "fiduciary guarantee" or a "fiduciary warranty" as part of the services they offer.

The word guarantee in business carries a whole lot of importance such as a money back guarantee. Of course, as with any guarantee, there are terms and conditions that limit that guarantee that people who don't read the fine print, find out in most unfortunate circumstances that they won't be covered.

When they hear the words "fiduciary guarantee", I assume most plan sponsors think that these plan providers will either serve in some sort of a fiduciary capacity or indemnify the plan sponsor in any lawsuits brought by plan participants for any claim for a breach of fiduciary duty. Of course, these providers go out of their way to make sure that they are not identified as serving in any fiduciary capacity and the fine print in these guarantees indicate that the providers will only defend plan sponsors only in rare instances.

A financial advisor forwarded me one of these guarantees for my thoughts. While the language on the guarantee was pretty clear, I have been an ERISA attorney for 13 years and I know the tricks of the trade. A plan sponsor who in most of these situations isn't working with an ERISA attorney assumes that the plan provider

will indemnify the plan fiduciaries in any alleged ERISA §404(c) breach in a participant directed retirement plan. The guarantee only states that the investment options that this provider selected were prudent, satisfied the Section 404(c) requirement of offering a "broad range of investment alternatives", and that the investment strategies provide a suitable basis for plan participants to construct well diversified portfolios. Sounds like a great guarantee? Actually, I don't think that the guarantee is worth the paper that it's written on.

That whole broad range requirement is rather broad; I am unaware of any plan fiduciaries ever being sued on that requirement. To comply with the simple broad range requirement, the plan fiduciaries must first decide on the asset classes (e.g., stocks and bonds) and styles (e.g., large cap U.S. equity growth fund, small cap U.S. equity value) for the "core" investments of the plan. So plan sponsors need to offer a diverse group of investments.

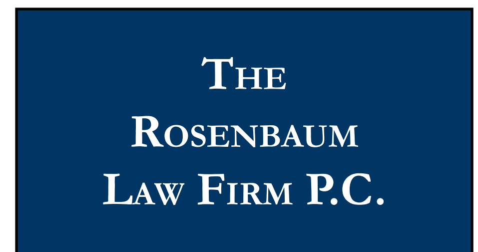
While this bundled provider state that the investments offered are consistent with the fiduciary prudent standard, the plan's investment fiduciaries still must monitor the investment options to insure that each continues to meet the criteria for the asset class and style and is performing well enough to continue to be offered to plan participants.

Guaranteeing that the investments offered in the plan are part of a broad range of investments and are prudent, these are only a couple of ways where a plan fiduciary can be sued for an ERISA Section §404(c) breach. A plan sponsor and fiduciary can still be sued for not formulating an investment policy statement or offering investment education to plan participants. There are thousands of mutual funds out there, it's not so hard to find five funds that make that broad range requirement or a claim that the investments are prudent. To steal a line from Commander Montgomery Scott in Star Trek III, "a monkey and two trainees" could pick mutual funds that would satisfy the broad range requirement. Drafting an investment policy statement, decision making meetings with the plan management committee, constant review of plan investments, and offering education to plan participants are far more difficult fiduciary functions to handle.

A fiduciary guarantee is almost absolutely no protection for plan fiduciaries, it's like buying car insurance that only covers you in a head on collision or a life insurance policy that only pays on accidental death. It's a guarantee that guarantees very little. The fiduciary guarantee is no substitute for an ERISA §3(21) or ERISA §3(38) fiduciary or a co-fiduciary. Unless a bundled provider assumes some sort of fiduciary capacity, the plan sponsor as a plan fiduciary is not being protected because the bundled provider is offering almost nothing at all.

The fiduciary guarantee is a deceptive practice. Sure, the plan providers will claim that the limits on their guarantee are fully disclosed and they are correct. However, most plan sponsors who do not use the services of an independent ERISA attorney will not understand that the protection of liability for the broad range of investments requirement under ERISA §404(c) is such a small part of fiduciary liability and very few cases against plan fiduciaries are ever litigated on that requirement because it is such an easy task to handle. Some of these plan sponsors naively believe that the fiduciary guarantee offers the same level of protection as an independent ERISA fiduciary. Remember, some of these providers didn't stop their plan sponsor clients from believing that they were charging them nothing for plan administration.

Don't be had by a pale imitation, only go for real fiduciaries and real fiduciary protection. Someone who is not willing to be a fiduciary isn't worth the same as the one who will.



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The Rosenbaum Law Firm P.C.
734 Franklin Avenue, Suite 302
Garden City, New York 11530
(516) 594-1557

http://www.therosenbaumlawfirm.com
Follow us on Twitter @rosenbaumlaw